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OUTBOUND MERGER AND AQUISITIONS

ABSTRACT

Merger and acquisitions are more common in order to spread the wings in the business field especially in the corporate era. Outbound mergers are those in which the Indian company invests in one of the foreign company and acquires it. For example in 2008 the Tata company has invested in the jaguar which received world-wide acclaim as it is one of the international acquisition done by the Indian company. India is considered as one of the top growing economies as it stands next to china and US. In olden days it was a difficult task to merge with Indian companies whether it may be in bound or outbound because of the poor drafted documents related to the company law. But with the increasing scope of development in the law and economy the merger and acquisitions became easier with India. Today most of the foreign companies are ready and also started to invest in the Indian start-ups and even Indian corporates are able to merge with many of the foreign companies by mergers and acquisitions.

So in this paper the author wants to research on the mergers and acquisitions which are especially outside India also known as outbound M &A. The author discusses the law related to outbound M & A in the Indian Companies Act, 2013 along with the different case laws and also how the law has evolved from time to time.

OBJECTIVE OF THE STUDY

- The main aim of this paper is to give an over view of law related to outbound m and a in the Indian law.
- To know how the law has been evolved through the time in relation to M & A especially which were happened outside India.
- To unveil the advantages and disadvantages of outbound M & A.

SCOPE OF THE STUDY

The researcher has limited herself to the merger and Acquisitions that has taken place outside India by the Indian companies also known as Outbound M&A especially in regard to the Indian Companies Act, 2 013

LITERATURE REVIEW

1) **Afsharipour, Afra. "Rising multinationals: Law and the evolution of outbound acquisitions by Indian companies."** ***UC Davis L. Rev.*** **44 (2010): 1029.**

   In this article the author has explained about the rise of outbound M & A of most of the developing countries especially focusing on Indian scenario. The author has explained bout the rising Outbound M & As by Indian corporates.

2) **Singla, Chitra. "Antecedents of inbound and outbound M&A: Industry-level analysis from India."** ***Management International Review*** **59.5 (2019): 703-739.**

   In this article the author focused on both inbound and out bound M & A focusing more on the industrial side. He has beautifully articulated the antecedents and the post obligations of merger and acquisitions.

INTRODUCTION AND HISTORICAL BACKGROUND

Merger and Acquisitions are the best way to expand the business in the other countries. With the growing developments in the law and economy of the country India became one of the most powerful nation for the cross border transactions. If two or more companies want to combine and becomes one company then it is called as a merger. In the process of merging the companies which are ready to merge will merge all the assets, liabilities and becomes a company. Acquisition is a bit different from merging. In the process of acquisition one company will buy the other company and takeover it completely. The moment the former company takes over the latter, the latter will cease to exist.

The law related to merger and acquisitions also slowly developed in a way that it attracts the foreign investments and also gave more scope for the Indian corporates to become multinational companies by investing in the foreign companies through the process of mergers and acquisitions which is shortly known as outbound M & A. there

is an enormous increase of foreign investments by emerging economies like India and china especially from the early 20th century. The concept of liberalisation in 1991 also became one of the major reason for the increase of M & A to the unprecedented level. Legal norms and rules and the development of laws related to it can also be considered as one major reason for the M & A. In cross border M & A India has much potential because of non-governmental public bodies.[1] The decade of 2000 to 2010 is considered as the golden year for outbound M & A as there was rapid increase of investments by Indian companies in other countries through acquisitions. Since India is one of the most rapidly developing nations all the other nations are trying to invest capital in India. Recent developments in the law related to the M & A and the concept of liberalisation has increased the M& A in the unprecedented level.

NEED OF OUTBOUND M & A

India realised the importance of foreign investments for strengthening its business and understood the importance of being a global investor by giving a tough competition in the global market. The significant event in the merger and Acquisitions has taken place after the Tata Company acquired the jaguar in 2008. The Indians got access to establish multinational companies through the cross border transactions. Hindalco of Aditya Birla which is one of the oldest conglomerates has started acquiring the small and domestic businesses in the foreign companies and developed them into global entities and the Hindalco is one such classic example.

OUTBOUND M & A – ADVANTAGES AND DISADVANTAGES

Indian law has its origin from the common law countries and the most of the company law which was codified in the year 1956 has mostly adopted from the UK company law. English being the dominant language in India after independnce it becomes easier for the Indians to analyse the law of other countries as there is no language difficulty. The then government congress was also more open about the competitiveness which is an important factor to stand in the global level. According to the statistics most of the Indian firm's acquisition that had happened in the early 2000's is with in the developed economies like majority

[1] Singla, Chitra. "Antecedents of inbound and outbound M&A: Industry-level analysis from India." *Management International Review* 59.5 (2019): 703-739.

License raj system which was existed in the period of 1960 to 1990 has limited the Indian companies' access to the foreign countries. This also restricted the flow of cash between the nations to participate in equity transactions. The high tariff rates for the cross border transactions, less rate of imports and exports is one of the disadvantage at that time. But this was also seen as a positive side by some of the economists as it lead to the Indian business tycoons to strengthen their balance sheets which eventually lead to the foreign investments by the Indian companies.

From Post liberalisation there is a paradigm shift within the law and economy especially in relation to the cross border transactions. The government has also removed the remittance and limitation of cash flow regarding to the foreign investments. There are many advantages as it let the Indians to expand its business to the foreign nations there by becoming the global company. More or less there are some disadvantages like it is an expensive process. It becomes a challenge for the Indian companies to withstand in the global market. Marketing and taking the things into the public is not an easy task for the outsiders. The ads and marketing will costs so much for the companies especially in the foreign nations than with in India

LAW IN RELATION TO OUTBOUND M & A

Till the year 2017 there was no clarity on the outbound mergers and Acquisitions though they mentioned about the Inbound M & A. The companies Act, 2013 talks about the Merger and Acquisitions it didn't specifically mention about the outbound M & A under section 234 of Companies Act, 2013. Later in the year 2017 the Ministry of Corporate Affairs and added a provision under Company Rules 2016 with the effect of 2017. In this they inserted the Rule 25-A and annexure – B to it. Outbound M & A is regulated by Companies Act, 2013, Insolvency and Bankruptcy code, SEBI, Income Tax and many other.

For acquisition of any foreign company by the Indian company the prior approval of RBI is mandatory. Proviso to sub-section (1) of Section 234 provides, 'that the Central Government may make rules, in consultation with the Reserve Bank of India, in connection with mergers and amalgamations provided under this section.' Sub-section (2) of Section 234 requires a prior Reserve Bank approval in the cross-border mergers. The requirement of approval by the RBI is expected to ensure

regulatory supervision over the proposed mergers including safeguarding of interest of the concerned stakeholders.[2]

The cross border regulations in relation to outbound M & A

For a company to merge or acquire under 234 of the Companies Act, 2013 it should be in accordance with the section 230 – 232 of the Companies Act, 2013 and also Rule 25-A of Company rules, 2016. Once it should take prior permission of the RBI before the process. After this, the company should approach National Company Law Tribunal and file an application before it. This would generally takes up to 5-6 months. For the cross border transaction the government has removed the restrictions and made it liberal in order to encourage global marketing.

Companies (Compromises, Arrangements and Amalgamations) Rules, 2016

Rule 25A of the above-mentioned rules mandates the transferee company to ensure that recognised professional valuers in its jurisdiction conduct the valuation and the same is according to internationally accepted standards. While applying for the Reserve Bank of India's approval, the transferee is required to attach a declaration regarding the valuation.

Foreign Exchange Management Regulations:

In case of an inbound merger (a cross-border merger where the resultant company is an Indian company), Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2017 will apply. For a Person Resident Outside India to invest in an Indian company prior approval of the Reserve Bank of India has to be sought. Under various schedules, procedures for different types of Persons Resident Outside India are provided. (Pakistan-Bangladesh investors, Foreign Portfolio Investors etc.)

Under these regulations:

- Once the merger scheme is granted by the National Company Law Tribunal, within two years the resultant Indian company has to sell its assets and clear its liabilities that it acquired overseas due to this inbound merger. This is a

[2] AVTAR SINGH, COMPANY LAW 612 (18th ed. 2017).

requirement when this acquiring of assets and liabilities is not permitted under the Foreign Exchange Management Act, 1999.

- All the overseas offices of the amalgamating company (here foreign company) will be hereinafter considered as the deemed to be offshore offices of the amalgamated company (resultant Indian company).

For the outbound mergers (a cross-border merger where the resultant company is a foreign company), Overseas Direct Investment Regulations come into the picture:

- Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) Regulations, 2016 will apply because in an outbound merger all the Indian offices will be considered as the offshore branches of the resultant foreign company.

Income Tax Act, 1961

Claiming benefits under Double Taxation Avoidance Agreement: As per Section 90(2) of the Income Tax Act, 1961 for the foreign corporation to claim tax benefit, it has to belong to the country that is part of Double Taxation Avoidance Agreement with India. According to Section 90(4) and (5) of the Income Tax Act, 1961 the foreign company has to provide details of its status, name of the country in which it was incorporated, its tax identification number in its country and also any other important information asked from time to time. All the benefits can be availed at the time of filing income tax returns with the Indian Tax authorities.

If the amount paid to the foreign company is taxable in India then the tax payable is withheld as mentioned under Section 195 of the Income Tax Act, 1961. 20 per cent is the withholding rate on dividends payable to non-resident shareholders.

In the case of **In Re: Bid Services Division (Mauritius) Ltd**[3], the capital gains tax benefit was rejected to the Mauritius entity. This capital gains tax benefit is provided under article 13(4) of the Indian Mauritius Double Taxation Avoidance Agreement. Here, the Mauritius entity has purchased shares of an Indian Joint Venture Company. The reason given by the Authority for Advance Rulings was that the Mauritius entity was shown as a mere shell entity and not a beneficial owner of the shares which were transferred.

[3] [2020] 114 taxmann.com 434 (AAR – Mumbai)

Capital gain tax is levied whenever any asset or securities are transferred in India. There are different rates for listed and unlisted shares. For the former, it is 15 per cent and for the latter, it is 10 per cent. Long term capital gain on transfer of any other asset would attract 20 per cent. This capital gain tax can be exempted if the merger (termed as amalgamation under the Income Tax Act, 1961) is a tax-neutral merger. A tax-neutral merger is when all the liabilities and assets of the amalgamating company (company A) becomes the liabilities and assets of the amalgamated company (company B) (Where A is merging into B). Here the resultant company has to be an Indian company (inbound merger).

Section 47 (vi) of the Income Tax Act, 1961 attracts capital gains tax upon transfers. However certain exemptions are provided for cross-border mergers. For this, the transfer of capital assets and shares have to be done by an amalgamating company (company A) to the amalgamated company (company B) and 75 per cent of shareholders of the amalgamating company (company A) have to become part of the amalgamated company (company B). Inbound mergers have an edge over the outbound mergers concerning capital gains tax.

Another tax case of a foreign acquisition is the **Vodafone International Holdings v Union of India** [4] case. Hutchison Telecommunications International Ltd, a telecommunications giant wholly-owned CGP Investments Ltd. Both the companies were based in the Cayman Islands. This CGP Investments Ltd held indirectly 67 per cent stake in Hutchison Essar Ltd (Joint Venture). Hutchison Telecommunications International Ltd sold CGP Investments Ltd to the Dutch-based Vodafone International Holdings and Vodafone bought it to gain control over Hutchison Essar operations. Now Hutchison Essar turned into Vodafone Essar. In 2007, Indian Tax Authorities filed for recovering taxes against Vodafone International Holdings and Vodafone Essar to the tune of approximately $ 2Billion. Contentions of the Indian Tax Authorities: The acquisition by the Vodafone International Holdings of CGP Investments Ltd led to direct control over Hutchison Essar making it Vodafone Essar. This results in selling off many Indian assets which attract capital gains that have to be taxed in India.

[4] [2012(1)SCALE530]

Contentions of the Vodafone Holdings: A transaction that occurred between Hutchison Telecommunications International Ltd and Dutch-based Vodafone International Holdings is a transaction between two foreign entities and that cannot be taxed in India.

Vodafone had approached the Bombay High Court that held: Although CGP Investments Ltd was acquired this entity did not have an existence of its own and neither did it have a bank account of its own. Therefore the intentions of the Vodafone Holdings can be drawn towards the fact that CGP comes with Hutchison Essar. Also, this transaction cannot be complete without selling Indian assets. It was ruled against the Vodafone authorities.

Vodafone had approached the Apex Court which held: The main question that was discussed by the Hon'ble Court was whether there was a deliberate attempt on part of the Vodafone Holdings to avoid taxes. The assessee could prove that there was no ill intention to avoid taxes. It was ruled in favour of them.

That is when the Indian Government had brought in the General Anti-Avoidance Rule where retrospectively they would get the power to reassess all the past transactions even those which date back to 1962. This amendment affected the tax code and forced Vodafone Holdings to go for international arbitration.

Vodafone's contentions: The two Bilateral Investment Treaties, India-Netherlands Bilateral Investment Treaty and India-UK Bilateral Investment Treaty have mentioned about fair and equitable treatment. The International Court had ruled in favour of Vodafone Holdings stating that the Indian government has breached the terms of the Bilateral Investment Agreements.

Competition Act, 2002:

Section 5 of the Competition Act, 2002 defines a combination to be any direct or indirect acquisition of an asset or amalgamation of an enterprise which exceeds the financial threshold.

The financial thresholds are as follows:

- In India - The acquirer and the target jointly have more than INR 20 Billion worth assets or a turnover crossing INR 60 Billion.

- Globally – The acquirer and the target have more than $ 1Billion worth assets with assets crossing INR 10 Billion in India itself or their turnover is more than $ 3 Billion with more than INR 30 Billion in India itself.
- Acquirer group - The acquirer and the target jointly have more than INR 80 Billion worth assets or a turnover crossing INR 240 Billion.
- Acquirer group - The acquirer and the target have more than $ 4Billion worth assets with assets crossing INR 10 Billion in India itself or their turnover is more than $ 12 Billion with more than INR 30 Billion in India itself.

For certain combinations, there is an exemption meaning, they are exempted from notifying to the Competition Commission of India:

- When the target's assets in India are worth INR 3.5 Billion or less or
- When the target's turnover in India is worth INR 10 Billion or less.

As per section 6(2) of the Competition Act, 2002 this combination has to be notified to the Competition Commission of India for its approval to proceed with the transaction. The term Appreciable Adverse Effect on Competition (AAEC) is mentioned in section 3(1) of the Competition Act, 2002. AAEC although not defined under the act simply means restricting the competition in the market. So when the financial thresholds are breached upon notifying to the Competition Commission of India, this commission looks into the merits of the case to see if the combination has any Appreciable Adverse Effect on Competition. In the **Titan International acquiring Titan Europe][5] case,** Titan International acquired Titan Europe. Here although Titan International had no revenue accruing from any business in India, still it was mandated by the Competition Commission of India to get the acquisition notified because by acquiring Titan Europe there is an indirect acquisition of Wheels India. Any combination (be it acquisition, merger or an amalgamation) that takes place outside India but might harm competition in the Indian market has to be notified failing which will attract a penalty.

If the Competition Commission of India concludes that the said arrangement will cause Appreciable Adverse Effect on Competition, then the Commission will mandate modifications as was done in the case of **Bayer (a German corporation - acquirer) acquiring Monsanto (an agricultural company incorporated in the United States-**

[5] [C-2013/02/109

target)[6]. Both the acquirer and the target have several subsidiaries in India. This acquisition was a reverse triangular merger which will make Monsanto the wholly-owned subsidiary of Bayer. Upon receiving notification under section 6(2) of the Competition Act, 2002 investigation was conducted under section 29 of the same act. Upon analysing, the commission found that this reverse triangular merger will cause an Appreciable Adverse Effect on Competition in several Indian markets and therefore had asked Bayer to send a show-cause notification. Although Bayer had proposed certain divestments, the commission disagreed to those and had mandated many modifications. Stating that complying with these modifications will only enable Bayer to acquire Monsanto.

Securities and Exchange Board of India:

The SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 mandates:

- Obligation to make an offer to remaining shareholders: Regulation 3 read with regulation 7 of the Takeover code creates an obligation on the acquirer when he acquires 25 per cent or more in the target company. The obligation is to make an offer to the rest of the shareholders of the target company to further acquire 26 per cent of the voting capital of the company.
- Obligation to make an open offer: If the acquirer holds 25 per cent from the beginning itself which is less than 75 per cent, then again holds another 5 per cent, the acquirer is obligated to make an open offer.

The SEBI (Listing Obligations and Disclosing Requirements) Regulations, 2015 mandates:

Before filing an application for approval of the merger scheme before the National Company Law Tribunal, a listed company has to follow certain listing regulations:

- Every listed company involved in an arrangement has to file its scheme before relevant stock exchanges seeking a no-objection letter.
- Their scheme has to be well within the provisions of the SEBI and the stock exchanges.

[6] [C-2017/08/523

- The listed company has to file the pre and post arrangement shareholding pattern with stock exchanges of India and the country where the foreign company is listed in. (in case of a listed foreign company)

CONCLUSION

The amendment of 2017 which allows the outbound M & A is obviously a most welcome amendment as it allows Indian companies to expand it wings globally. This will also help in the development of amicable relations with all other countries. As India is a rapidly emerging economy the outbound M & A would take it to next level in this global era.

There are differences in the applicability of tax and the lack of tax neutrality is considered as a major draw-back and the provisions of foreign exchange Management will not allow the foreign company to do business in India full-fledged manner by establishing an Indian entity would make it an unattractive one. So this has to be relooked and should be made necessary changes accordingly.

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