Research Paper

Submitted to

Mr. Manoj Pandey (IRS)
Director (Law)

Competition Commission OF India

"A STUDY ON ACQUISITION, CONTROL, MERGER AND AMALGAMATION UNDER SECTION 5 & 6 OF COMPETITION ACT, 2002"¹

A CRITICAL ANALYSIS

¹Prepared in fulfilment of the requirement as part of the academic curriculum of PGDM(Finance) in XISS, Ranchi
# Table of Contents

Disclaimer.............................................................................................................6

Acknowledgement....................................................................................................7

I. List of figures, tables and equations........................................................................8

II. List of abbreviations..............................................................................................9

Preface..................................................................................................................10

1. Introduction.............................................................................................................11-15

2. Research Methodology.........................................................................................16-17

   2.1 Research Objectives

   2.2 Research Questions

   2.3 Justification of the Study

   2.4 Sources of Information

   2.5 Scope and Limitations

3. General Meaning..................................................................................................18-19

4. Overview of M&A trends in India........................................................................20-24

5. Definition in detail...............................................................................................25-31

   5.1 Merger & Amalgamation.................................................................................25-29

   5.2 Acquisition........................................................................................................29-31

   5.3 Control..............................................................................................................31
6. Reasons and Rationale for M&A .......................................................... 32-34

7. Benefits of Merger and Acquisitions .................................................. 35-37

8. Valuation for M&A .............................................................................. 38-43
   8.1 Comparative ratio
   8.2 Replacement cost
   8.3 Discounted cash flow
   8.4 WACC
   8.5 HHI

9. Accounting in M&A ........................................................................... 44

10. Legal Framework of M&A in India .................................................... 45-61
    10.1 Mergers and Amalgamations ........................................................ 45-54
        10.1.1 As per Competition Act, 2002
        10.1.2 As per Companies Act, 1956
        10.1.3 As per Income Tax Act 1961
        10.1.4 As per Accounting Standard
        10.1.5 As per FEMA Act, 1999
        10.1.6 As per Indian Stamp duty
        10.1.7 As per TRAI
        10.1.8 As per Companies Bill, 2011
    10.2 Acquisitions .................................................................................. 54-55
10.2.1 As per Competition Act, 2002

10.2.2 As per SEBI (SAST) Regulations, 2011

10.2.3 As per Companies Bill, 2011

10.3 Control...............................................................................................................................56-59

10.3.1 As per Competition Act, 2002

10.3.2 As per Companies Bill, 2011

10.3.3 Control under SEBI laws

10.3.4 As per SEBI (SAST) Regulation, 2011

10.4 Regulation of Combination under section 6 of Competition Act, 2002.................................................................60-61

11. Analysis.................................................................................................................................62-64

11.1 Comparative Study

11.2 Critical Analysis

11.3 SWOT Analysis

12. Findings......................................................................................................................................65-68

12.1 Economic effect

12.2 Managerial effect

12.2.1 Product Life cycle model and M&A

12.2.2 What do managers need for successful M&A?

13. Conclusion..................................................................................................................................69
14. Recommendations.................................................................70-71

15. Future Perspectives..................................................................72

References...................................................................................73-74

III. List of Appendices..................................................................75-78

   Appendix 1: Benefits of M&A.....................................................75
   A.1.1 Economies of Scale
   A.1.2 Synergy

   Appendix 2: Game Theoretic Approach.......................................76
   A.2.1 Game Theory
   A.2.2 Prisoner’s Dilemma
Disclaimer

This project report/dissertation has been prepared by the author as an intern under the Internship Programme of the Competition Commission of India for academic purposes only. The views expressed in the report are personal to the intern and do not necessarily reflect the view of the Commission or any of its staff or personnel and do not bind the Commission in any manner. This report is the intellectual property of the Competition Commission of India and the same or any part thereof may not be used in any manner whatsoever, without express permission of the Competition Commission of India in writing.
Acknowledgement

The project work bears the imprint of many people, and I express my gratitude to all those who have helped me and rendered their help in all the possible ways in a completion of my project report.

It is a matter of immense pleasure to express my gratitude to my intern guide the Director (Law) Mr. Manoj Pandey (IRS) for his guidance and excellent insights which gave direction and focus to this paper. I thank him for lending his precious time in making this project an authentic piece of work.

I also owe sincere gratitude to the staff at library for always helping in the process of finding material and other sources for research. I am very grateful to all the individuals involved in the subgroup for their contributions and assistance in compiling this report and the recommendations that go with it: they are the outcome of an open, interactive and creative cooperation.

I also thank social networking site for searching the required information in precise and as per needed. How I can forget to give credit and my satisfaction to the whole team of CCI for conducting an Internship Programme for students to enhance and broaden their area of knowledge regarding competition issues. My institution and family really supported me throughout in my endeavours to which I am honoured to thank.

At last, I express my heartfelt gratitude to the God Almighty, without whose blessing and motivation, the completion of this project would have been impossible.

Thanks to all.............
## List of figures, tables and equations

### TABLES :

1. Table 1.1 Merger Waves ......................................................12
2. Table 4.1 Top 10 M&A in India 2010 .................................21
3. Table 4.2 Top 10 outbound M&A deals in India all time ....22
4. Table 6.1 Rationale for M&A ..............................................34
5. Table 8.1 HHI certain threshold ........................................43
6. Table 11.1 SWOT Analysis ................................................64

### FIGURES :

1. Figure 4.1 M&A deals in India from Jan 2010 to Dec 2011 ....23
2. Figure 4.2 M&A deals in India from Jan 2010 to Dec 2011 ....24
3. Figure 7.1 Merger gain .......................................................36
4. Figure 12.1 Profit earned by a Company A and Company B ...65
5. Figure 12.2 Profit earned by Company after M&A ..............66
6. Figure 12.3 Product Life Cycle model .................................67

### EQUATIONS :

1. Equation 1 Why we go to acquire ..................................30
2. Equation 2 Synergistic operating economies ..................32
3. Equation 3 Discounted Cash Flow .................................39-40
4. Equation 4 WACC .........................................................41-42
5. Equation 5 HHI .............................................................42
# List of abbreviations

<table>
<thead>
<tr>
<th></th>
<th>Abbreviation</th>
<th>Full Form</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>CCI</td>
<td>Competition Commission of India</td>
</tr>
<tr>
<td>2.</td>
<td>M&amp;A</td>
<td>Mergers and Acquisitions</td>
</tr>
<tr>
<td>3.</td>
<td>MRTP</td>
<td>Monopoly Restricted and Trade Practices</td>
</tr>
<tr>
<td>4.</td>
<td>SAST</td>
<td>Substantial Acquisition of Shares and Takeovers</td>
</tr>
<tr>
<td>5.</td>
<td>SEBI</td>
<td>Securities and Exchange Board of India</td>
</tr>
<tr>
<td>6.</td>
<td>FEMA</td>
<td>Foreign Exchange Management Act</td>
</tr>
<tr>
<td>7.</td>
<td>ICAI</td>
<td>The Institute of Chartered Accountants of India</td>
</tr>
<tr>
<td>8.</td>
<td>NPV</td>
<td>Net Present Value</td>
</tr>
<tr>
<td>9.</td>
<td>WACC</td>
<td>Weighted Average Cost of Capital</td>
</tr>
<tr>
<td>10.</td>
<td>HHI</td>
<td>Herfindahl Hirschman Index</td>
</tr>
<tr>
<td>11.</td>
<td>SAT</td>
<td>Securities Appellate Tribunal</td>
</tr>
</tbody>
</table>
The principle objective of competition law is to protect the interest of consumers and as well as producers and also to promote free and fair competition in the market. Economic reforms took place in 1990s which gave rise to need for enactment of a new Act in place of erstwhile MRTP, Act. The MRTP Act not concerned about the promotion of competition in the market. It only addressed the areas of monopolistic, restrictive and unfair trade practices. The government of India enacted Competition Act, 2002 on 13th January 2003. Later on it was amended in 2007 and 2009. The main features of new law:-

1. Prohibits Anti competitive agreements (section 3)
2. Prohibits Abuse of dominant position (section 4)
3. Provides for Regulation of Combinations (section 5&6), and
4. Enjoins Competition Advocacy[section 49(3)]

The objectives of the Act are sought to be achieved through the Competition Commission of India. The commission is also required to give opinion on a reference received from a statutory authority established under any law and to undertake competition advocacy and create public awareness on competition issues.

My primary focus of research paper is to understand the meaning of Acquisition, Control, Merger and Amalgamation. It will also cover the critical analysis on comparing it with definitions under different laws. The Provisions of the Act relating to regulation of combinations have been enforced with effect from 1st June, 2011.
Chapter 1

INTRODUCTION

Since the liberalization process was initiated in 1992 by the then-Finance Minister, Mr. Manmohan Singh (today, India’s Prime Minister), Indian corporate houses have faced great competitive pressures but have surmounted various impediments and obstacles to acquire global presence and strength to challenge foreign MNCs in their “home” markets. Mergers and Amalgamations have been very important strategies for growth of corporate sector. During times of recession, consolidation\(^2\) of business alone is thought as the panacea for all evils of the economy. The subject of Mergers and Amalgamations not only interests, owners of business but also corporate consultants and tax experts alike. M&A are the most popular means of corporate restructuring or business combinations\(^3\). But there is no denying a fact that no other event is more difficult, challenging, or chaotic as a merger and acquisition. It is imperative that everyone involved in the process has a clear understanding of how the process works.

If we look to the emergence of M&A the timelines will look as under;

i) The first merger occurred between 1890 and 1904, in the United States

ii) The second began at the end of the World War I and continued through the 1920s.


\(^3\) Broadly Combination includes acquisition of control, shares, voting rights or assets, acquisition of control by a person over an enterprise where such person has control over another enterprise engaged in competing businesses, and mergers and amalgamations between or amongst enterprises where these exceed the thresholds specified in the Act in terms of assets or turnover(according to Competition Act,2002)
iii) The third merger commenced in the latter part of World War II and continues to the present day.\(^4\)

The economic history has been divided into *Merger Waves* based on the merger activities in the business world as:

**Table 1.1: Merger Waves**

<table>
<thead>
<tr>
<th>Period</th>
<th>Name</th>
<th>Facet</th>
</tr>
</thead>
<tbody>
<tr>
<td>1897–1904</td>
<td>First Wave</td>
<td>Horizontal mergers</td>
</tr>
<tr>
<td>1916–1929</td>
<td>Second Wave</td>
<td>Vertical mergers</td>
</tr>
<tr>
<td>1965–1969</td>
<td>Third Wave</td>
<td>Diversified conglomerate mergers</td>
</tr>
<tr>
<td>1981–1989</td>
<td>Fourth Wave</td>
<td>Congeneric mergers; Hostile takeovers; Corporate Raiding</td>
</tr>
<tr>
<td>1992–2000</td>
<td>Fifth Wave</td>
<td>Cross-border mergers</td>
</tr>
<tr>
<td>2003–2008</td>
<td>Sixth Wave</td>
<td>Shareholder Activism, Private Equity, LBO</td>
</tr>
</tbody>
</table>

**Source:** Hitt, Harrison and Ireland, 2001

Mergers and Acquisitions have since the 1990s become popular among firms as a way to expand and pursue corporate goals (Gaughan 2005).\(^5\) Earlier merger waves were mainly carried through with a focus on restructuring and on core and related business. Later waves have focused on strengthening the firms’ competitiveness through achieving economies of scale and scope and market power (Hitt, Harrison and Ireland, 2001).\(^7\) Sherman and Hart (2005)\(^8\) mention a number of key reasons for engaging in M&As;

---


\(^6\) The increase in efficiency of production as the number of goods being produced increases. Typically, a company that achieves economies of scale lowers the average cost per unit through increased production since fixed costs are shared over an increased number of goods. Read more: [http://www.investopedia.com/terms/e/economiesofscale.asp#ixzz1sTnvhb4Y](http://www.investopedia.com/terms/e/economiesofscale.asp#ixzz1sTnvhb4Y)

\(^7\) Hitt, Michael A.; R. Duane Ireland and Jeffrey S. Harrison, 2001, “Mergers and Acquisitions: A Value Creating or Value Destroying Strategy”

\(^8\) Sherman, Andrew J. and Milledge A. Hart, 2005, “Mergers and Acquisitions from A to Z”
1. First of all, it is an efficient way to enter a new market, expand the product line or increase distribution reach.

2. Second, acquiring a firm makes it possible to obtain their “knowledge workers” apart from products and intellectual property.

3. Third, M&As may be motivated by the need to transform the firm’s corporate identity.

4. Fourth, it offers an opportunity to spread the risk and cost associated with developing new technology.

5. Fifth, firms may reach the conclusion that they need to expand their current product or service line in order to handle seasonal and cyclical market trends.

6. Lastly, through an M&A a firm is able to acquire brand loyalty and customer relationship which would have been more expensive to build.

A study on these merger waves said that buyers aren’t necessarily hungry for the target companies’ hard assets. Some are more interested in acquiring thoughts, methodologies, people and relationships. Paul Graham\(^9\) recognized this in his 2005 essay "Hiring is Obsolete", in which he theorizes that the free market is better at identifying talent, and that traditional hiring practices do not follow the principles of free market because they depend a lot upon credentials and university degrees.

The basic purpose of corporate restructuring is to enhance the shareholder’s value. A company should periodically evaluate its portfolio\(^10\) of businesses,

\(^9\) He is an enthusiast, successful tech entrepreneur and author of the excellent book Hackers and Painters

\(^10\) It is a grouping of financial assets such as stocks, bonds and cash equivalents, as well as their mutual, exchange-traded and closed-fund counterparts. Portfolios are held directly by investors and/or managed by financial professionals.

Read more: [http://www.investopedia.com/terms/p/portfolio.asp#ixzz1s0KybpU](http://www.investopedia.com/terms/p/portfolio.asp#ixzz1s0KybpU)
capital mix\textsuperscript{11} and ownership and assets arrangements to find opportunities for increasing the shareholder value.

In the words of Justice DHANANJAYA Y. CHANDRACHUD-

“Corporate restructuring is one of the means that can be employed to meet the challenges and problems which confront business. The law should be slow to retard or impede the discretion of corporate enterprise to adapt itself to the needs of changing times and to meet the demands of increasing competition. The law as evolved in the area of mergers and amalgamations has recognised the importance of the Court not sitting as an appellate authority over the commercial wisdom of those who seek to restructure business.”\textsuperscript{12}

Under corporate restructuring these terms are like accepted concepts for growth and expansion. Notwithstanding, I am going to study these concepts taking consideration of section 5&6 of Competition Act, 2002 (as amended) and definitions defined under various laws like SEBI Act,1992, Companies Act,1956, Income Tax Act,1961,etc

Mergers and Acquisitions (or combinations) refer to a situation where the ownership of two or more enterprises is joined together. A merger is said to occur when two or more companies combine to form a new company. Mergers & Acquisitions have been seen as the solution by many market players to strengthen their hold over the markets as well as by the governments to remedy inefficiencies\textsuperscript{13}.

\textsuperscript{11} It is a mix of a company's long-term debt, specific short-term debt, common equity and preferred equity.

Read more: http://www.investopedia.com/terms/c/capitalstructure.asp#ixzz1sHRGWWRE

\textsuperscript{12} Ion Exchange (India) Ltd., In re, (2001) 105 Comp Cases (Bombay).

\textsuperscript{13} Ibid
Therefore, an entrepreneur may grow its business either by internal expansion or by external expansion. In the case of internal expansion, a firm grows gradually over time in the normal course of the business, through acquisition of new assets, replacement of the technologically obsolete equipments and the establishment of new lines of products. But in external expansion, a firm acquires a running business and grows overnight through corporate combinations. These combinations are in the form of mergers, acquisitions, amalgamations and takeovers. They are being used in a wide array of fields such as information technology, telecommunications, and business process outsourcing as well as in traditional businesses in order to gain strength, expand the customer base, cut competition or enter into a new market or product segment. In the wake of economic reforms, Indian industries have also started restructuring their operations around their core business activities through acquisition and takeovers because of their increasing exposure to competition both domestically and internationally.
Chapter 2

RESEARCH METHODOLOGY

The research design is qualitative and quantitative both in nature.

2.1 Research Objective:

1) To study the definition of acquisition, control, merger and amalgamation in general
2) To study the concept of acquisition, control, merger and amalgamation under Competition Act, 2002 and other acts in India
3) To do the comparative study of concepts under various laws
4) To study the impact of mergers and acquisitions
5) To study the basic economic forces that lead to M&A
6) To do the critical analysis of the meaning under various laws that create confusion in the minds of organization
7) To find the required conclusion and suggestion for better M&A policy to be followed for industry growth

2.2 Research Questions:

The project will ascertain the answer of certain questions arising in the mind of beginners (either for a student or for any entrepreneur):

- What is the general meaning of Acquisition, Control, Merger and Amalgamation? Do they differ with each other?
- What is the definition of these terms defined under Competition Act, SEBI Act, FEMA Act, Accounting Standard (14), Companies Act, etc?
- Do these terms differ with each other under Competition Act?
What is the comparative analysis of these terms defined by various laws?
What is threshold limits of Combination defined under section 5 of the Competition Act, 2002 (as amended)?

2.3 **Justification of the Study:**

The Project Report justifies the concept of the terms chosen for the study under various laws with reference to the Competition Act in particular. It forwarded the relevant solution and opinion to CCI for necessary improvements and changes, if required. It justifies:

i. The gainer and loser in the M&A, taking large firms and small firms in consideration
ii. Asset and Turnover estimates
iii. Recommendations

2.4 **Sources of Information:**

The researcher has predominantly referred to primary sources, such as statutes, regulations and guidelines, in the course of writing this paper, and has also referred to a few relevant commentaries and observations of jurists and experts in order to elucidate her arguments.

2.5 **Scope and Limitations:**

This paper is limited to the issues surrounding meaning of Acquisition, Control, Merger and Amalgamation, types of merger, thresholds for mergers and acquisitions, and other factors considered for M&A. Due to constraints of space and time, the researcher has not extensively gone into the procedural requirements while inspecting the terms chosen for research, but rather has dealt with these subjects only to the extent that they are required to explain the arguments put forth.
Chapter 3

GENERAL MEANING

There is a great deal of confusion and disagreement regarding the precise meaning of terms relating to the business combination, viz., merger, acquisition, control, takeover and amalgamation. Sometimes, these terms are used in broad sense, encompassing most dimensions of business combination, while sometimes they are defined in a restricted legal sense. However, this research paper delineates these concepts or terms keeping in mind the relevant legal framework in India.

Mergers and Acquisitions (or Combinations) refer to a situation where the ownership of two or more enterprises is joined together. Merger\(^{14}\) is a general term used to refer to the consolidation of companies. A merger is said to occur when two or more companies combine to form a new company while an acquisition\(^{15}\) is the purchase of one company by another in which no new company is formed. In merger, two or more companies may merge with an existing company or they may merge to form a new company. The assets and liabilities of the transferor company become the assets and liabilities of the transferee company after the merger. The purpose of a merger is usually to create a bigger entity, which accelerates growth and leads to economies of scale. However, a merger may lead to unwanted socioeconomic implications that are often frowned upon. This was proved when the European commission on competition blocked the merger of GE and Honeywell, which would have been one of the largest industrial mergers in history. This merger however, was earlier

\(^{14}\)Read more:  
http://www.investopedia.com/terms/m/mergersandacquisitions.asp?partner=TOD04#ixzz1swFYTgIK

\(^{15}\)Read more:  
http://www.investopedia.com/terms/m/mergersandacquisitions.asp?partner=TOD04#ixzz1swHtTSJK
cleared by the concerned US agency – the Department of Justice. This clearly shows each country has its own rules on competition. What one perceives as a threat may not be taken the same way by the other. India, which has now opened itself to global competition, now has its own competition law along with other laws which defines M&A in their own way.

In India, mergers and acquisitions are regulated through the provision of Companies Act 1956, the MRTP Act 1969 now the Competition Act, 2002(as amended), the FEMA Act 1999, Income Tax Act 1961 and through SEBI laws.
Chapter 4

Overview of M&A Trends in India

Mergers and Acquisitions, in today’s world are the most fundamental elements of a corporate strategy, be it for a huge Multinational Corporation in course of taking over a fast growing gazelle company (the recent acquisition of Skype by the software giant Microsoft for a whopping $8.5 billion), or for two equals in the process of undergoing a merger (the merging of the then giant pharmaceuticals Glaxo Wellcome and SmithKline Beecham, to form a new pharmaceutical company, GlaxoSmithKline). The Indian economic reform since 1991 has opened up a whole lot of challenges both in the domestic and international spheres. The increased competition in the global market has prompted the Indian companies to go for mergers and acquisitions as an important strategic choice. The trends of mergers and acquisitions in India have changed over the years. The immediate effects of the mergers and acquisitions have also been diverse across the various sectors of the Indian economy.

India had very less cases of Mergers and Acquisitions (M&A) earlier. But in past four years, things have changed and there is a sharp increase in Inbound\textsuperscript{16} and Outbound\textsuperscript{17} M&A. After a dismal 2009, 2010 proved to be just the year for M&As in India. There has been total number of 116 Mergers and Acquisitions (M&A) only in the month of January (56) and February (60) 2010' successfully with an value of about $3.86 billion, whereas in 2009 in total there has 330

\textsuperscript{16} Inbound M&A means the foreign companies are making an investment in the Indian companies. \\
\textsuperscript{17} Outbound M&A means the companies which have Indian origin and make an investment in the foreign based companies.
number of deals which was valued about $11.96 billion are registered. The overview of M&A in India in the year 2011:

- Overall deal activity in M&A involving India slowed down as value and deal counts have declined 43.7% and 27% as compared to 2010.
- Domestic deal activity reached 6.6 billion, down 52.4% from 2010.
- India’s acquisitions overseas witnessed a 65.6% sharp decline.

The percentage share of total valuation of M&A deals that took place in India during the first nine months of FY’11 is as below:

- Telecom sector- 28.26%
- Energy sector - 23.59%
- Metal & Mining sector – 23.19%
- Pharmaceuticals and BFSI (banking, financial services and insurance) sector – 8.20% and 5.74% respectively

Table 4.1: Top 10 M&A in India for 2010

<table>
<thead>
<tr>
<th>Rank</th>
<th>Company</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Tata Chemicals buys British Salt</td>
<td>US$ 13 Billion</td>
</tr>
<tr>
<td>2.</td>
<td>Reliance Power and Reliance Natural Resources merger</td>
<td>US$ 11 Billion</td>
</tr>
<tr>
<td>3.</td>
<td>Airtel’s acquisition of Zain in Africa</td>
<td>US$ 10.7 Billion</td>
</tr>
<tr>
<td>4.</td>
<td>Abbott’s acquisition of Piramal healthcare solutions</td>
<td>US$ 3.72 Billion</td>
</tr>
<tr>
<td>5.</td>
<td>GTL Infrastructure acquisition of Aircel towers</td>
<td>US$ 1.8 Billion</td>
</tr>
<tr>
<td>6.</td>
<td>ICICI Bank buys Bank of Rajasthan</td>
<td>Rs 3,000 cr</td>
</tr>
<tr>
<td>7.</td>
<td>JSW and Ispat Ki Kahani</td>
<td>Rs 2,157 cr</td>
</tr>
<tr>
<td>8.</td>
<td>Reckitt Beinkiser goes shopping</td>
<td>US$ 726 Million</td>
</tr>
<tr>
<td>9.</td>
<td>Mahindra goes International</td>
<td>US$ 463 Million</td>
</tr>
<tr>
<td>10.</td>
<td>Fortis Healthcare acquisition</td>
<td>Rs 1,332 cr</td>
</tr>
</tbody>
</table>


---

Table 4.2: Top 10 Outbound M&A deals in India all time

<table>
<thead>
<tr>
<th>Acquirer Company</th>
<th>Targeted Company</th>
<th>Deal Value (In Billions)</th>
<th>Industry</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tata Steel</td>
<td>Corus (UK)</td>
<td>$12.2</td>
<td>Steel</td>
</tr>
<tr>
<td>Hindalco Industries</td>
<td>Novelis Inc (USA)</td>
<td>$6</td>
<td>Aluminium</td>
</tr>
<tr>
<td>Oil &amp; Natural Gas Corporation (ONGC) Videsh Ltd</td>
<td>Imperial Energy PLC (UK)</td>
<td>$2.8</td>
<td>Oil &amp; Gas</td>
</tr>
<tr>
<td>Tata Motors Ltd</td>
<td>Jaguar &amp; Land Rover Operations (UK)</td>
<td>$2.3</td>
<td>Automotive</td>
</tr>
<tr>
<td>Suzlon Energy Ltd</td>
<td>RE Power (Germany)</td>
<td>$1.7</td>
<td>Power &amp; Energy</td>
</tr>
<tr>
<td>Essar Steel Holdings Limited</td>
<td>Algoma Steel Inc (Canada)</td>
<td>$1.58</td>
<td>Steel</td>
</tr>
<tr>
<td>United Spirits</td>
<td>Whyte &amp; Mackay (UK)</td>
<td>$1.11</td>
<td>Breweries &amp; Distilleries</td>
</tr>
<tr>
<td>Tata Power</td>
<td>PT Kaltim Prima Coal; PT Arutmin Indonesia (30% Stake - Indonesia)</td>
<td>$1.10</td>
<td>Power &amp; Energy</td>
</tr>
<tr>
<td>GMR Infrastructure Ltd</td>
<td>InterGen NV (50% - Stake Netherlands )</td>
<td>$1.10</td>
<td>Power &amp; Energy</td>
</tr>
<tr>
<td>Tata Chemicals Limited</td>
<td>General Chemical (USA)</td>
<td>$1</td>
<td>Plastic &amp; Chemicals</td>
</tr>
</tbody>
</table>

According to the ISI emerging markets database the calendar year 2011 saw M&A deals in India fall by more than 50% over the last year, as only 195 deals

were announced. Compared to this nearly 400 deals were announced in the calendar year 2010. Even the net deal value fell to ~USD 18bn as compared to ~USD 45bn in the previous year.

![Graph showing M&A deals in India from Jan 2010 to Dec 2011]

**Fig: 4.1**

i) The biggest deal of the 2011 was British Petroleum which took over 30% stake in 23 oil and gas blocks of Reliance Industries Limited for an aggregate of US$ 7.2bn,

ii) Tata Steel sold its 26% stake in Australian miner Riversdale to Rio Tinto for US$ 1.1bn.

iii) Bain Capital and GIC, the investment arm of the Government of Singapore bought a 30% stake in Hero Investment (P) Ltd, which owns 17% of Hero Honda Motors for US$ 0.8bn

iv) Piramal Healthcare purchased ~5.5% of the issued equity share capital of Vodafone Essar Ltd from ETHL Communications Holdings Ltd for a cash consideration of US$ 0.6bn.

---

20 Source of the information: ISI emerging market is an Internet Securities, Inc., which trades as ISI Emerging Markets, is an information company that provides electronic subscription based data and information on emerging market economies.
Out of the total deals announced in 2011, 95 were domestic deals amounting to a deal value of ~US$ 4bn, 38 were outbound deals where Indian companies acquired a foreign target (deal value ~US$ 3.5bn) while 50 inbound deals saw Indian companies being acquired by foreign firms (deal value ~US$ 10.5bn). Biggest decline was in inbound deals where they fell by ~65% in comparison to 2010. This is shown in Figure-4.2 below:

Looking at the current scenario\textsuperscript{21}, I think we’ll really have to keep our fingers crossed for this year. While some courageous mid-sized Indian organizations might still scout around for small strategic overseas buyouts, this year could see most Indian companies cutting back on overseas acquisitions (Thermax and Marico have already postponed their M&A plans). And as there will be uncertainty in both the outbound as well as inbound markets, the coming year could see a fair amount of increase in the percentage of domestic deals. But we will continue to see some amount of interest in inbound deals in this year as the western world continues to be seduced by the ‘India growth story’ and for most of them the option of not being in India does not really exist!

\textsuperscript{21} For more information about 2012 M&A held and approved by CCI is given in the CCI website http://www.cci.gov.in/index.php?option=com_content&task=view&id=171
Chapter 5
DEFINITION IN DETAIL

The term ‘Merger’, ‘Amalgamation’, ‘Acquisition’, and ‘Control’ are often used interchangeably in common parlance. However, there are differences.

5.1 MERGER

According to Oxford Dictionary, the expression “Merger” or “Amalgamation” means “combining of two commercial companies into one” or “merger of two or more business concerns into one”. ‘Merger’ is a fusion between two or more enterprises, whereby the identity of one or more is lost and the result is a single enterprise. We will use the terms merger and amalgamation interchangeably.

Merger or Amalgamation may take two forms:

- Merger through absorption
- Merger through consolidation

Absorption

Absorption is a combination of two or more companies into an existing company. All companies except one lose their identity in a merger through absorption. An example of this type of merger is the absorption of Tata Fertilisers Ltd. (TFL) by Tata Chemicals Ltd. (TCL). TCL, an acquiring company (a buyer), survived after merger while TFL, an acquired company (a seller), ceased to exist. TFL transferred its assets, liabilities and shares to TCL.

Consolidation

A consolidation is a combination of two or more companies into a 'new company'. In this form of merger, all companies are legally dissolved and a new entity is created. Here, the acquired company transfers its assets, liabilities and shares to the acquiring company for cash or exchange of shares. For example, merger of Hindustan Computers Ltd, Hindustan Instruments Ltd, Indian Software Company Ltd and Indian Reprographics Ltd into an entirely new company called HCL Ltd.

TYPES OF MERGER

- **Horizontal merger**
  Take place when two merging companies manufacture similar goods and belong to the same industry. For example, the combination of two book publishers or two luggage manufacturing companies to gain dominant market share.

- **Vertical merger**
  It is a combination of two or more firms involved in different stages of production or distribution of the same product. For example, the joining of a TV manufacturing (assembling) company and a TV marketing company or joining of a spinning company and a weaving company. Vertical merger may take the form of forward or backward merger. When a company combines with the supplier of material, it is called backward merger and when it combines with the customer, it is known as forward merger. For example, ICICI Ltd with ICICI Bank is an example of vertical merger with backward linkage as far as ICICI Bank is concerned.

- **Conglomerate merger**
  It occurs when the two merging companies belong to two different industrial sectors. For example, the merging of different businesses like for
instance, manufacturing of cement products, fertilizer products, electronic products, insurance investment and advertising agencies. L&T and Voltas Ltd are examples of such mergers. Such kind of merger can be broadly classified into:-

i. **Product-extension merger** - Conglomerate mergers which involves companies selling different but related products in the same market or sells non-competing products and use same marketing channels of production process. E.g. Phillip Morris-Kraft, PepsiCo- Pizza Hut, Proctor and Gamble and Clorox

ii. **Market-extension merger** - Conglomerate mergers wherein companies that sell the same products in different markets/geographic markets. E.g. Morrison supermarkets and Safeway, Time Warner-TCI.

iii. **Pure Conglomerate merger** - The two companies which merge have no obvious relationship of any kind. For e.g. Bank Corp of America- Hughes Electronics.

❖ **Congeneric merger**

These are mergers between entities engaged in the same general industry and somewhat interrelated, but having no common customer-supplier relationship. A company uses this type of merger in order to use the resulting ability to use the same sales and distribution channels to reach the customers of both businesses.\(^{23}\)

❖ **Cash Merger**

In a typical merger, the merged entity combines the assets of the two companies and grants the shareholders of each original company shares in the new company based on the relative valuations of the two original companies. However, in the case of a ‘cash merger’, also known as a

‘cash-out merger’, the shareholders of one entity receives cash in place of shares in the merged entity.

- **Triangular Merger**
  A triangular merger is often resorted to for regulatory and tax reasons. As the name suggests, it is a tripartite arrangement in which the target merges with a subsidiary of the acquirer. Based on which entity is the survivor after such merger, a triangular merger may be forward (when the target merges into the subsidiary and the subsidiary survives), or reverse (when the subsidiary merges into the target and the target survives).

- **Reverse Merger**
  A type of merger used by private companies to become publicly traded without resorting to an initial public offering. It is also known as a "reverse merger" or "reverse IPO".

- **Dilutive Merger**
  Dilutive mergers take place when a company with a low price to earnings ratio acquires a company with a high price to earnings ratio. This causes the purchasing company’s earnings per share to decrease. This type of merger is the opposite of an accretive merger.

- **Accretive Merger or Acquisition**
  Accretive mergers occur when a company with a high price to earnings ratio purchases a company with a low price to earnings ratio. This makes the purchasing company’s earnings per share increase.

5.2 **AMALGAMATION**

‘Amalgamation’ signifies blending of two or more existing undertakings into one undertaking, the blended companies losing their identities and forming themselves into a separate legal identity. The term ‘amalgamation’, as per
Concise Oxford Dictionary, Tenth Edition, means, ‘to combine or unite to form one organization or structure’.

There may be amalgamation either by the transfer of two or more undertaking to a new company, or by the transfer of one or more undertaking to an existing company.

Merger is also defined as amalgamation. Merger is the fusion of two or more existing companies. All assets, liabilities and the stock of one company stand transferred to Transferee Company in consideration of payment in the form of:-

   i)  Equity shares in the transferee company,
   ii) Debentures in the transferee company,
   iii) Cash, or
   iv)  A mix of the above mode

5.3 ACQUISITION

Acquisition in general sense is acquiring the ownership in the property. In the context of business combinations, an acquisition is the purchase by one company of a controlling interest in the share capital of another existing company. The term "acquisition" refers to the acquisition of assets by one company from another company. In an acquisition, both companies may continue to exist. It generally refers to the purchase of controlling interest by one company in the share capital of an existing company. This may be by:

1. An agreement with majority holder of Interest.
2. Purchase of new shares by private agreement
3. Purchase of shares in open market (open offer)
4. Acquisition of share capital of a company by means of cash, issuance of shares
5. Making a buyout offer to general body of shareholders
Equation 1: Why we go to acquire?

If company A wants to buy company B, then NPV of purchase must be >0

\[ \text{NPV} = \text{Gain} - \text{Cost} > 0 \]

\[ \text{Gain} = \text{PV}_{AB} - (\text{PV}_A + \text{PV}_B) = \text{Value of Synergy}, \text{i.e., PV of combined company AB must be greater than PV of each separate.} \]

Suppose it is a cash purchase, then

\[ \text{Cost} = \text{cash} - \text{PV}_B \]

Thus,

\[ \text{NPV} = [\text{PV}_{AB} - (\text{PV}_A + \text{PV}_B)] - [\text{(cost} - \text{PV}_B)] = \text{gain} - \text{cost} \]


TYPE OF ACQUISITION

- **Hostile**
  In case of Hostile acquisitions, the company, which is to be bought, has no information about the acquisition. The company, which would be sold, is taken by surprise.

- **Friendly**
  In case of Friendly acquisition, the two companies cooperate with each other and settle matters related to acquisitions

- **Leveraged Buyouts**
  These are form of takeovers where the acquisition is funded by borrowed money. Often the assets of the target company are used as collateral for the loan. This is a common structure when acquirers wish to make large acquisitions without having to commit too much capital.

- **Bailout Takeovers**
  Another form of takeover is a ‘bail out takeover’ in which a profit making company acquires a sick company to set off of the losses of the sick company against the profits of the acquirer, thereby reducing the tax
payable by the acquirer. This kind of takeover is usually pursuant to a scheme of reconstruction/rehabilitation with the approval of lender banks/financial institutions. This would be true in the case of a merger between such companies as well.

5.4 CONTROL

The term ‘control’, with respect to companies, may be defined in various ways, including, with reference to shareholding, voting rights, right to appoint directors on the board, management rights, veto rights etc. A layman’s understanding of the term would be the ability to control the management and policy of a company, whether by holding a majority of shares or by having majority representation on the board of directors of the company or by any other means. Control over an enterprise can be of two types²⁴:-

➢ **Sole control**- An enterprise is under sole control if party exercising such control does not require the assent of other shareholders for any meaningful decision-making.

➢ **Joint control**- A party who is enjoying joint control has to take into account the potentially different interests of the other parties concerned. Thus more than one party simultaneous exercises control over an enterprise in cases of joint control.

Chapter 6

Reasons and Rationale for M&A

Ideally, mergers are executed with the expectation that the target will increase the equity value of the acquirer. Below some common merger motivations are described.

- **Synergistic operating economies:** Synergy\(^{25}\) may be defined as; \(V_{AB} > V_A + V_B\), In other words the combined value of two firms or companies shall be more than their individual value. This may be result of complimentary services economies of scale\(^{26}\) or both. On similar lines, economies of large scale are also one of the reasons for synergy benefits. The difference between the combined value and the sum of the values of individual companies is usually attributed to synergy(Equation-2 below)

\[
\text{Equation 2: Value of acquirer + Stand alone value of target + Value of synergy} = \text{Combined Value}
\]

(Source: ICAI, 2005)

There is also a cost attached to acquisition. The cost of acquisition is the price premium paid over the market value plus other costs of integration. Therefore, the net gain is the value of synergy minus premium paid.

\(V_A = 100, V_B = 50, V_{AB} = 170, \text{Synergy} = V_{AB} - (V_A + V_B) = 25\), If premium is 10 then, Net Gain = 25-10=15

\(^{25}\) Brief notes in Appendix 1

\(^{26}\) Brief notes in Appendix 1
• **Cost Synergies**: Mergers have the potential to lower costs for the combined companies, either through the elimination of redundant functions or by eliminating profits from “middle-man” points in the value chain.

• **Revenue Synergies**: Mergers may provide the combined companies an opportunity to cross sell complementary products.

• **Growth**: Merger and Acquisition mode enables the firm to grow at a faster rate than other mode e.g. Capital Budgeting because the merged and the acquiring company enters in the market. It might provide a company with more rapid growth potential than organic growth provided by reinvesting earnings.

• **Pricing Power**: A horizontal merger can reduce competition and allow the acquirer to raise its prices. A vertical merger can allow the acquirer to better control prices downstream or upstream in the value chain. When a merger has the potential to provide an acquirer with too much market power, government regulations may prevent the merger from taking place.

• **Increased Capability**: An acquiring company may pursue a target for its in-house technical expertise.

• **Unlocking Value**: An acquirer may view a target as underperforming financially and feel confident that it can facilitate the realization of the target’s full potential after taking control.

• **Diversification**: Companies themselves are investors who seek to reduce risk and increase returns through the successful deployment of capital.
- **International M&A Concerns**: Companies may engage in M&A beyond their domestic borders for multiple financial or strategic reasons.

- **Taxation**: The provision of set off and carry forward of losses as per Income Tax Act may be another strong reason for merger and acquisition. Thus, there will be Tax saving or reduction in tax liability of the merged firm having substantial earning.

- **Consolidation of Production Capacities and increasing market power**: Due to reduction in competition market power increases and also the production capacities are increased by combined of two or more plants. The following table shows the key rationale for some of the well known transactions which took place in India in the past.

<table>
<thead>
<tr>
<th>Rationale for M&amp;A</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Instantaneous growth, Snuffing out competition, Increased market share</td>
<td>HLL-Lakme, Glaxo – Smithkline, Daimler – Chrysler.</td>
</tr>
<tr>
<td>Acquisition of a competence or a Capability</td>
<td>ICICI – ITC classic (retailer network &amp; depositor’s base), IBM-Daksh</td>
</tr>
<tr>
<td>Entry into new markets/product segments</td>
<td>Vodafone – Mannesman, Mannesman – Orange, Tata- Tetley</td>
</tr>
<tr>
<td>Access to funds</td>
<td>TDPL- Sun Pharma since TDPL wanted to Have funds to launch new products.</td>
</tr>
<tr>
<td>Tax benefits</td>
<td>Ashok Leyland Information Technologies with Hinduja Finance</td>
</tr>
</tbody>
</table>

Source: ICAI, data base, 2005
Chapter 7

BENEFITS OF MERGERS AND ACQUISITIONS

The benefits of M&A are higher to the firm what the different firms can earn individually, this helps the smaller firms to earn more after merger and larger firms when they acquire. This can be easily explained by the GAME-THEORETIC APPROACH\textsuperscript{27}. The incentives for firms to collude, and the difficulties of sustaining collusion can be illustrated by the ‘Prisoner’s Dilemma’ in Table - 5.

In the following game, there are two firms, Firm A and Firm B, who can either have competitive or cooperating strategies.

<table>
<thead>
<tr>
<th>Firm A/ Firm B</th>
<th>Competitive</th>
<th>Merging or Acquiring</th>
</tr>
</thead>
<tbody>
<tr>
<td>Competitive</td>
<td>20,20</td>
<td>30,0</td>
</tr>
<tr>
<td>Merging or Acquiring</td>
<td>0,30</td>
<td>19,19</td>
</tr>
</tbody>
</table>

The first number in each quadrant in the above Figure shows the profits earned by Firm A and the second number shows the profits earned by Firm B. For example, if Firm A tries to play in a competitive set up while Firm B wants to merge or acquire, then firm A will get a payoff of 30, while firm B will end up getting Zero payoff (top right quadrant). Thus, looking at the diagram, it is clear that if both the firms merge or acquire, they can together earn higher profits, and may pass on the benefits to the consumers, thus, increasing the overall welfare of the society.\textsuperscript{28}

\textsuperscript{27} Note that this type of collaboration can be an explicit or a tacit collusion.

\textsuperscript{28} Notice that the payoffs are such that there is no incentive for the firms to deviate from the set equilibrium.
The merger and acquisition gains can be seen through this diagram:

**Exhibit: Merger Gain(Figure-7.1)**

![Diagram showing merger gain components](image)


As we all should know that the Mergers and acquisitions are caused with the support of shareholders, managers and promoters of the combining companies.

**From the standpoint of shareholders**

Investment made by shareholders in the companies subject to merger should enhance in value. The sale of shares from one company’s shareholders to another and holding investment in shares should give rise to greater values i.e. the opportunity gains in alternative investments. Shareholders may gain from merger in different ways viz. from the gains and achievements of the company i.e. through

(a) Realization of monopoly profits;
(b) Economies of scales;
(c) Diversification of product line;
(d) Acquisition of human assets and other resources not available otherwise;
(e) Better investment opportunity in combinations.

---

From the standpoint of managers

Managers are concerned with improving operations of the company, managing the affairs of the company effectively for all round gains and growth of the company which will provide them better deals in raising their status, perks and fringe benefits. Mergers where all these things are the guaranteed outcome get support from the managers. At the same time, where managers have fear of displacement at the hands of new management in amalgamated company and also resultant depreciation from the merger then support from them becomes difficult.

Promoter’s gains

Mergers do offer to company promoters the advantage of increasing the size of their company and the financial structure and strength. They can convert a closely held and private limited company into a public company without contributing much wealth and without losing control.

Benefits to general public

Impact of mergers on general public could be viewed as aspect of benefits and costs to:

(a) Consumer of the product or services;
(b) Workers of the companies under combination;
(c) General public affected having not been user or consumer or the worker in the companies under merger plan.
Chapter 8
VALUATION FOR M&A

The value of a business is a function of the business logic driving the M&A and is based on bargaining powers of buyers and sellers. Since business is based on expectation which are dynamic, valuation also tends to be dynamic and not static which means that the same transaction would be valued by the same players at different values at two different times. Because of the Competitive nature of the acquisition market, companies not only need to respond wisely but often must respond quickly as well.

Naturally, both sides of an M&A deal will have different ideas about the worth of a target company: its seller will tend to value the company at as high of a price as possible, while the buyer will try to get the lowest price that he can. There are, however, many legitimate ways to value companies. The most common method is to look at comparable companies in an industry, but deal makers employ a variety of other methods and tools when assessing a target company. Here are just a few of them:

8.1 **Comparative Ratios** - The following are two examples of the many comparative metrics on which acquiring companies may base their offers:

- **Price-Earnings Ratio (P/E Ratio)** - With the use of this ratio, an acquiring company makes an offer that is a multiple of the earnings of the target company. Looking at the P/E for all the stocks within the same industry group will give the acquiring company good guidance for what the target's P/E multiple should be.
• **Enterprise-Value-to-Sales Ratio (EV/Sales)** - With this ratio, the acquiring company makes an offer as a multiple of the revenues, again, while being aware of the price-to-sales ratio of other companies in the industry.

8.2 **Replacement Cost** - In a few cases, acquisitions are based on the cost of replacing the target company. For simplicity's sake, suppose the value of a company is simply the sum of all its equipment and staffing costs. The acquiring company can literally order the target to sell at that price, or it will create a competitor for the same cost. Naturally, it takes a long time to assemble good management, acquire property and get the right equipment. This method of establishing a price certainly wouldn't make much sense in a service industry where the key assets - people and ideas - are hard to value and develop.

8.3 **Discounted Cash Flow (DCF)** - A key valuation tool in M&A, discounted cash flow analysis determines a company's current value according to its estimated future cash flows. Forecasted free cash flows (operating profit + depreciation + amortization of goodwill – capital expenditures – cash taxes - change in working capital) are discounted to a present value using the company's weighted average costs of capital (WACC). Admittedly, DCF is tricky to get right, but few tools can rival this valuation method. There are six steps involved in the valuation given below:

**Equation 3:**

**Step 1: Determine Free Cash Flow**

Free cash flow is the cash flow available to all investors in the company both shareholders and bondholders after consideration for taxes, capital expenditure and working capital investment.

Free cash flow = NOPAT + Depreciation

(Capital Expenditure + Working Capital Investment)
Estimate the most likely incremental cash flows to be generated by the target company with the acquirer as owner. Note that financing is not incorporated in the cash flows. Suitable adjustments for the specific financing of the acquisition will be made in the discount rate.

**Step 2: Estimate a suitable Discount Rate for the Acquisition**

The acquiring company can use its weighted average cost of capital based on its target capital structure only if the acquisition will not affect the riskiness of the acquirer. If the acquirer intends to change the capital structure of the target company, suitable adjustments for the discount rate should be made. The discount rate should reflect the capital structure of the company after the acquisition.

**Step 3: Calculate the Present Value of Cash Flows**

Since the life of a going concern, by definition, is infinite, the value of the company is = PV of cash flows during the forecast period + terminal value. We can set the forecast period in such a way that the company reaches a stable phase after that.

**Step 4: Estimate the Terminal Value**

The terminal value is the present value of cash flows occurring after the forecast period. If we assume that cash flows at a constant rate after the forecast period, the terminal value,

\[ \text{TV} = \frac{\text{CF}_t (1 + g)}{k - g} \]

where,

- \( \text{CF}_t \) = Cash flow in the last year
- \( g \) = Constant growth rate
- \( k \) = Discount rate

**Step 5: Add Present Value of Terminal Value**

**Step 6: Deduct the Value of Debt and other Obligations assumed by the acquirer**

8.4 **WACC** - There is two basic methods for valuing companies by discounted cash flows given below:

**Equation 4:**

**Method 1:** Using the expected equity cash flow (ECF) and the required return to equity (Ke).

[I] \[ E_0 = PV_0 \cdot Ket; ECF_t \] , Equation (I) indicates that the value of the equity (E) is the present value of the expected equity cash flows (ECF) discounted at the required rate of return to equity (Ke).

[II] \[ D_0 = PV_0 \cdot Kdt; CFdt \] , Equation (II) indicates that the value of the debt (D) is the present value of the expected debt flows (CFd) discounted at the required return to debt (Kd).

**Method 2:** Using the free cash flow and the WACC. The free cash flow (FCF) is the hypothetical equity cash flow when the company has no debt. The expression that relates the FCF with the ECF is:

[III] \[ ECF_t = FCF_t + \Delta Dt - It \cdot (1-T) \] where, \( \Delta Dt \) is the increase in debt, and it is the interest paid by the company. \[ CFdt = It - \Delta Dt \]

[IV] \[ E_0 + D_0 = PV_0 \cdot WACC_t; FCF_t \] , Equation (IV) indicates that the value of the debt (D) + shareholders’ equity (E) is the present value of the expected free cash flows (FCF) that the company will generate, discounted at the weighted average cost of capital.

The WACC is the rate at which the FCF must be discounted so that equation (IV) gives the same result as that given by the sum of (I) and (II). By doing so, the expression of the WACC is given by Equation [V]:

[V] \[ WACC_t = \frac{Et - 1 \cdot Ket + Dt - 1 \cdot Kdt \cdot (1-T)}{Et - 1 + Dt - 1} \]

T is the effective tax rate applied to interest in equation (III). \( Et - 1 + Dt - 1 \) are not market values nor book values: in actual fact, \( Et – 1 \) and \( Dt – 1 \) are the values obtained when the valuation is performed using formulae [I], [II] or [IV]
The WACC is a weighted average of two different magnitudes:

- A cost: the cost of debt, and
- A required return: the required return to equity (Ke). Although Ke is called many times cost of equity, there is a big difference between a cost and a required return.

Thus the WACC is neither a cost nor a required return, but a weighted average of a cost and required return. To refer to WACC as “cost of capital” can be misleading because it is not a cost.

8.5 HHI: HHI measures market concentration and is a metric used by government oversight bodies in the U.S. to determine if a merger should be allowed or blocked.

HHI calculates the sum of squared market shares for competing companies.

\[
HHI = \sum \left( \left( \frac{\text{Sales}_{\text{firm } i}}{\text{Sales}_{\text{Market}}} \right) \times 100 \right)^2
\]

For an individual firm, HHI is calculated once; for a merger of two companies the HHI of the combined entity will be the sum of their individual market share HHI values.
When HHI crosses a certain threshold, the government may legally challenge the proposed merger given below:

Table 8.1: HHI threshold

<table>
<thead>
<tr>
<th>COMBINED ENTITY HHI</th>
<th>HHI CHANGE</th>
<th>LIKELY RESPONSE OF COMPETITION AGENCIES</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt; 1,000</td>
<td>Irrelevant</td>
<td>None.</td>
</tr>
<tr>
<td>1,000 – 1,800</td>
<td>≥ 100</td>
<td>Potential legal challenge to merger.</td>
</tr>
<tr>
<td>1,800+</td>
<td>≥ 50</td>
<td>Definite challenge to merger.</td>
</tr>
</tbody>
</table>

Source: www.google.co.in/HHI/threshold

Note that a small change to HHI in a heavily concentrated industry may be more scrutinized than a large change to HHI in a highly competitive industry.
Merger and acquisition accounting is done either by the purchase or pooling of interests methods. There are some differences between these two accounting methods which are discussed below:

i) **Purchase Method**

The asset and liabilities of the merged company are presented at their market values as on the date of acquisition, in order to ensure that the resulting values of the accounting process are able to reflect the market values. This refers to the value, which was recorded before the final settlement of the acquisition deal at the time of bargaining. In this process, the total liabilities of the joint company equal the sum of individual liabilities of the two separate firms. The purchase price then determines the amount by which the acquiring firm’s equity is going to increase. However, one of the drawbacks with purchase method is the chance that it may overrate depreciation charges. This is because the book value of assets used in accounting is generally lower than the fair value if there is inflation in the economy.

ii) **Pooling of Interests Method**

In this method, transactions are considered as exchange of equity securities. Here, assets and liabilities of the two firms are combined according to their book value on the acquisition date. The total asset value of the joint company equals the sum of assets of the separate firms. In this case, the accounting income is found to be higher than in the purchase method, as the depreciation in the pooling method is calculated based on the historical book value of asset.
Chapter 10

LEGAL FRAMEWORK OF M&A IN INDIA

In India, mergers are regulated under the Companies Act, 2002 and also under the SEBI Act, 1992. With the enactment of the Competition Act in 2002, mergers have also come within the ambit of this legislation. In the Companies Act, 1956, mergers are regulated between companies *inter alia* to protect the interests of the secured creditors and the SEBI Act it tries to protect the interests of the investors. Apart from protecting the interests of private parties, these objectives are different and mutually exclusive. In the Competition Act, 2002, the objective is much broader. It aims at protecting the appreciable adverse effect on trade-related competition in the relevant market in India (AAEC).

10.1 Mergers and Amalgamations

10.1.1 As per Competition Act, 2002 (as amended)


It defines Combination under section 5&6 of the competition act, 2002. It says:

Any **merger or amalgamation** in which—

(i) The enterprise remaining after merger or the enterprise created as a result of the amalgamation, as the case may be, have,—

(A) Either in India, the assets of the value of more than rupees one thousand and five hundred crores or turnover more than rupees four thousand and five hundred crores; or

---

*Inter alia*(in-tur eh-lee-ah) prep. Latin for "among other things." This phrase is often found in legal pleadings and writings to specify one example out of many possibilities. Example: "The judge said, inter alia, that the time to file the action had passed."
(B) [in India or outside India, in aggregate, the assets of the value of more than seven hundred and fifty million US dollars, including at least rupees seven hundred and fifty crores in India, or turnover more than two thousand two hundred and fifty million US dollars, including at least rupees two thousand two hundred and fifty crores in India; or]

(ii) The group, to which the enterprise remaining after the merger or the enterprise created as a result of the amalgamation, would belong after the merger or the amalgamation, as the case may be, have or would have,—

(A) Either in India, the assets of the value of more than rupees six thousand crores or turnover more than rupees eighteen thousand crores; or

(B) [in India or outside India, in aggregate, the assets of the value of more than three thousand million US dollars, including at least rupees seven hundred and fifty crores in India, or turnover more than nine thousand million US dollars, including at least rupees two thousand two hundred and fifty crores in India;]

10.1.2 As per Companies Act, 1956:

The term M&A have not been defined in the Companies Act, 1956 through this voluminous piece of legislation which contains more than 50 definitions in section 2 of the Act. For the purpose of this Act the term ‘Merger’ and ‘Amalgamation’ are synonymous. The statutory provisions relating to merger and amalgamation are contained in sections 390 to 396A.

Whenever two or more companies agree to merge with each other, they have to prepare a scheme of amalgamation. The acquiring company should prepare the scheme in consultation with its merchant banker or financial institution. It should be ensured that the scheme is just and equitable to the shareholders and employees of each of the amalgamating company and to the public. The scheme of merger / amalgamation is governed by the provisions of Section 391-394 and Section 111 of Companies Act 1956.
Legal Procedures

The summary of legal procedures for mergers or acquisition laid down in the Companies Act, 1956 is given here below:

- **Permission for merger**
  Companies can amalgamate only when amalgamation is permitted under their memorandum of association. Also the acquiring company should have the permission in its object clause to carry on the business of the acquired. Otherwise it is necessary to seek the permission of the shareholders, board of directors and the Company Law Board before affecting the merger.

- **Information to the stock exchange**
  The acquiring and the acquired companies should inform the stock exchanges where they have listed about the merger

- **Approval of board of directors (BODs)**
  The BODs of the individual companies’ should approve the draft proposal for amalgamation and authorize the managements of companies to further pursue the proposal.

- **Application in the High Court**
  An application for approving the draft amalgamation proposal duly approved by the BODs of the individual companies should be made to the High Court. The High Court convenes a meeting of the shareholders and creditors to approve the amalgamation proposal. The notice of meeting should be sent them at least 21 days in advance.
- **Shareholders’ and creditors’ meetings**
  The individual companies should hold separate meetings of their shareholders and creditors for approval of scheme of merger. At least 75 percent of shareholders and creditors must accord their approval to the scheme.

- **Sanction by the High Court**
  After the above approvals, the High Court will pass order sanctioning the amalgamation scheme, only if scheme is fair and reasonable. If necessary, court can modify the scheme.

- **Filling the Court order**
  After the Court order, its certified true copies will be filed with the Registrar of the companies.

- **Transfer of Assets and Liabilities**
  The assets and liabilities of the acquired company will be transferred to the acquiring company in accordance with the approved scheme with effect from the specified date.

- **Payment by cash or securities**
  As per the proposal, the acquiring company will exchange shares and debentures and pay cash for the shares and debentures of the acquired company. The securities will be listed on the stock exchange.

**10.1.3 As per Income Tax Act, 1961:**

Amalgamation is defined under section 2(1b) of the Income Tax Act, 1961 means the merger of one or more companies with another company or the merger of two or more companies to form one company in such a manner that the following conditions can be satisfied:-
a) All the property of the amalgamating company or companies immediately before the amalgamation becomes the property of the amalgamated company by virtue of the amalgamation.

b) All the liabilities of the amalgamating company or companies immediately before the amalgamation become the liabilities of the amalgamated companies by virtue of the amalgamation.

c) Shareholders holding at least three-fourths in value of the shares in the amalgamating company or companies (other than shares already held therein immediately before the amalgamated company or its nominee) becomes the shareholders of the amalgamated company by virtue of the amalgamation.

The following are the major tax benefits available to the amalgamated company:

a) One of the motives for mergers is the tax savings under Income Tax Act, 1961, Section 72A. It is attractive for amalgamation of a sick company with a healthy and profitable one through which the amalgamated company seeks to avail the benefits of set-off/carry forward of losses and unabsorbed depreciation of the amalgamating company against its future profits. The conditions are:

   o The amalgamating company is not financially viable by reasons of its liabilities, losses and other relevant factors immediately before such amalgamation.

   o Amalgamation is in public interest.

   o Any other conditions of the central government to ensure that the benefit under this section is restricted to amalgamations which enable rehabilitation or revival of the business of the amalgamation company.
b) Deduction of following expenditure or expenses would be made in the books of amalgamated company in the same manner as would have been allowed to the amalgamating company:

- Expenditure on scientific research
- Expenditure on acquisition of patent rights or copy right
- Expenditure on know-how
- Preliminary expenses
- Expenditure on prospecting of certain minerals
- Bad debts etc.

The Income tax Act for all types of business mergers and acquisition has become fully tax natural. The unwritten-off amount with respect to all the above items is treated in the hands of the amalgamated company in the same manner as would have been treated by the amalgamating company. Thus, the amalgamated company is not put to any disadvantage as far as the income tax concessions and incentives are concerned.

d) The tax concessions to the amalgamating company are summarized below:

- According to Section 47 (VI) where there is a transfer of any capital asset by an amalgamating company to any Indian amalgamated company, such transfer will not be considered as transfer for the purpose of capital gain.
- According to Section 45(b) of the Gift Tax Act, where there is a transfer of any asset by an Indian amalgamating company, gift tax will not be attracted.
- According to Section 47 (vii), where a shareholder of an Indian amalgamating company transfer his shares, such transaction will be disregarded for capital gain purposes, provided the transfer of shares is made in consideration of the allotment of any share to him or shares in the amalgamated company.
10.1.4 **As per Accounting Standard:**

According to the mandatory Accounting Standard-14(AS-14) issued by the Institute of Chartered Accountants of India (ICAI), "amalgamation" means an amalgamation pursuant to the provisions of the Companies Act, 1956 or any other statute which may be applicable to companies. Under the said AS-14 the following two methods of amalgamation have been contemplated:

1) **Amalgamation in the nature of merger**:—

   Amalgamation in the nature of merger is an amalgamation which satisfies all the following conditions:—
   a) All the assets and liabilities of the transferor company become, after amalgamation, the assets and liabilities of the transferee company.
   b) Shareholders holding not less than 90% of the face value of the equity shares of the transferor company (other than the equity shares already held there in, immediately before the amalgamation, by the transferee company or its subsidiaries or their nominees become equity shareholders of the transferee company by virtue of the amalgamation.
   c) The consideration for the amalgamation receivable by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company wholly by the issue of equity shares in the transferee company, except that cash may be paid in respect of any fractional shares.
   d) The business of the transferor company is intended to be carried on, after the amalgamation, by the transferee company.
   e) No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in

---

the financial statements of the transferee company except to ensure uniformity of accounting policies.

2) **Amalgamation in the nature of purchase:**

Amalgamation in the nature of purchase is an amalgamation which does not satisfy any one or more of the conditions specified in (1) above.

**10.1.5 As per FEMA Act, 1999**

According to section I (10) **Acquisition of shares under Scheme of Merger / Amalgamation:** Mergers and amalgamations of companies in India are usually governed by an order issued by a competent Court on the basis of the Scheme submitted by the companies undergoing merger/amalgamation. Once the scheme of merger or amalgamation of two or more Indian companies has been approved by a Court in India, the transferee company or new company is allowed to issue shares to the shareholders of the transferor company resident outside India, subject to the conditions that:

(i) The percentage of shareholding of persons resident outside India in the transferee or new company does not exceed the sectoral cap, and

(ii) The transferor company or the transferee or the new company is not engaged in activities which are prohibited under the FDI policy.

**10.1.6 As per Indian Stamp duty**

The Indian Stamp Act, 1899 do not specifically provide for any specific entry in Schedule I with regard to merger, de-merger, hive off, and slump sale of a business by an Indian company. However, this does not mean that no stamp duty is payable on instruments which are used to implement such transactions. The issue is subject to several litigation and the revenue authorities take different views in different cases.
In states like Maharashtra and Gujarat, the matter is resolved to some extent by providing specific entries for levying stamp duty on merger and de-merger which are implemented under the Companies Act, 1956.

10.1.7 As per TRAI

The sector regulator proposed that companies should be allowed to merge if their combined subscriber or revenue market share does not exceed 60 per cent, although its consent would be required for any merger that would create a company with a market share of between 35 and 60 per cent.

Under current rules, two companies can merge only if their combined market share does not exceed 40 per cent

10.1.7 As per Companies Bill, 2011

The term ‘merger’ is defined, as the undertaking of property and liabilities of one or more companies, including the company in respect of which the compromise or arrangement is proposed, are to be transferred to another existing company, it is a merger by absorption, or where the undertaking, property and liabilities of two or more companies, including the company in respect of which the compromise or arrangement is proposed, are to be transferred to a new company, whether or not a public company, it is a merger by formation of a new company; Along with it, the references to merging companies are in relation to a merger by absorption, to the transferor and transferee companies, and, in relation to a merger by formation of a new company, to the transferor companies 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
Proposed changes in the companies bill, 2011:

Merger of small companies- M&A between two small companies (share capital of Rs. 50 lakh turnover of Rs.2 crore) or between a holding company and a wholly owned subsidiary company not required to be filed with the Tribunal.

10.2 Acquisition

10.2.1 As per Competition Act, 2002(as amended)

The acquisition of one or more enterprises by one or more persons or merger or amalgamation of enterprises shall be a combination of such enterprises and persons or enterprises, if—

(a) Any Acquisition where,

   (i) The parties to the acquisition, being the acquirer and the enterprise, whose control, shares, voting rights or assets have been acquired or are being acquired jointly have,—

      (A) Either, in India, the assets of the value of more than rupees one thousand and five hundred crores or turnover more than rupees four thousand and five hundred crores; or

      (B) [in India or outside India, in aggregate, the assets of the value of more than seven hundred and fifty million US dollars, including at least rupees seven hundred and fifty crores in India, or turnover more than two thousand two hundred and fifty US dollars, including at least rupees two thousand two hundred and fifty crores in India; or]

   (ii) the group, to which the enterprise whose control, shares, assets or voting rights have been acquired or are being acquired, would belong after the acquisition, jointly have or would jointly have,—

      (A) Either in India, the assets of the value of more than rupees six thousand crores or turnover more than rupees eighteen thousand crores; or
(B) [in India or outside India, in aggregate, the assets of the value of more than three thousand million US dollars, including at least rupees seven hundred and fifty crores in India, or turnover more than nine thousand million US dollars, including at least rupees two thousand two hundred and fifty crores in India; or]

*Explanation:*
As per section 2(a) of the Act “acquisition” means, directly or indirectly, acquiring or agreeing to acquire-

i) shares, voting rights or assets of any enterprise; or

ii) control over management or control over assets of any enterprise;

**10.2.2 As per SEBI (SAST) Regulations, 2011**

As per its section 2[1(a)], “acquirer” means any person who, directly or indirectly, acquires or agrees to acquire whether by himself, or through, or with persons acting in concert with him, shares or voting rights in, or control over a target company;

As per its section 2[1(b)], “acquisition” means, directly or indirectly, acquiring or agreeing to acquire shares or voting rights in, or control over, a target company

**10.2.3 As per Companies Bill, 2011**

In the event of an acquirer, or a person acting in concert with such acquirer, becoming registered holder of ninety per cent or more of the issued equity share capital of a company, or in the event of any person or group of persons becoming ninety per cent. Majority or holding ninety per cent of the issued equity share capital of a company, by virtue of an amalgamation, share exchange, conversion of securities or for any other reason, such acquirer, person or group of persons, as the case may be, shall notify the company of their intention to buy the remaining equity shares.
10.3 Control

10.3.1 As per Competition act, 2002 (as amended)

acquiring of control by a person over an enterprise when such person has already direct or indirect control over another enterprise engaged in production, distribution or trading of a similar or identical or substitutable goods or provision of a similar or identical or substitutable service, if—

(i) the enterprise over which control has been acquired along with the enterprise over which the acquirer already has direct or indirect control jointly have,—

(A) Either in India, the assets of the value of more than rupees one thousand and five hundred crores or turnover more than rupees four thousand and five hundred crores; or

(B) [in India or outside India, in aggregate, the assets of the value of more than seven hundred and fifty million US dollars, including at least rupees seven hundred and fifty crores in India, or turnover more than two thousand two hundred and fifty million US dollars, including at least rupees two thousand two hundred and fifty crores in India; or]

(ii) The group, to which enterprise whose control has been acquired, or is being acquired, would belong after the acquisition, jointly have or would jointly have,—

(A) Either in India, the assets of the value of more than rupees six thousand crores or turnover more than rupees eighteen thousand crores; or

(B) [in India or outside India, in aggregate, the assets of the value of more than three thousand million US dollars, including at least rupees seven hundred and fifty crores in India, or turnover more than nine thousand million US dollars, including at least two thousand two hundred and fifty crores in India; or]
Explanation—

(b) "Control" includes controlling the affairs or management by—
   i) One or more enterprises, either jointly or singly, over another enterprise or group;
   ii) One or more groups, either jointly or singly, over another group or enterprise;

(c) "Group" means two or more enterprises which, directly or indirectly, are in a position to —
   i) Exercise twenty-six per cent or more of the voting rights in the other enterprise; or
   ii) Appoint more than fifty per cent of the members of the board of directors in the other enterprise; or
   iii) Control the management or affairs of the other enterprise;

10.3.2 As per Companies Bill, 2011

As per section 2(27), “control” shall include the right to appoint majority of the directors or to control the management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholders agreements or voting agreements or in any other manner.

10.3.3 Control under SEBI laws:

The Securities and Exchange Board of India Act 1992 (the 1992 Act) established the SEBI to protect the interests of investors and to promote and regulate the securities market in India. Sections 11 and 11A of the 1992 Act empower the SEBI to take various steps in the aforesaid objectives, including by introduction of regulations to govern the issue of securities, regulation of stock brokers and
other intermediaries, regulation of substantial acquisition of shares, promotion of investor education, prohibition of insider trading etc. While the 1992 Act itself does not have a separate definition for the term ‘control’, various regulations and guidelines made under the 1992 Act have defined the term ‘control’.

While some SEBI regulations have their own tailor-made definition of ‘control’ depending upon the specific needs of those regulations, the definition as appearing in the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations 1997 as amended from time to time (the 1997 Code) has been adopted or referred to in several other regulations of the SEBI.

Under the SEBI (Merchant Bankers) Regulations 1992, the SEBI (Portfolio Managers) Regulations 1993 and the SEBI (Registrars to an Issue and Share Transfer Agents) Regulations 1993, ‘control’ is defined in a narrow sense whereby controlling interest is an interest, whether direct or indirect, to the extent of at least 51% of voting rights in the body corporate. This specific definition of ‘control’ has been adopted in light of the fact that these regulations set up a regulatory regime for market intermediaries and their operations have a potential effect upon the investors in specific and the market in general.

However, as already pointed out, a number of SEBI regulations have adopted the definition of ‘control’ as it appears in the 1997 Code. The SEBI (Buyback of Securities) Regulations 1998, the SEBI (Issue of Sweat Equity) Regulations 2002, the SEBI (Issue of Capital and Disclosure Requirements) Regulations 2009 (SEBI ICDR 2009) and the SEBI (Delisting of Equity Shares) Regulations 2009 all incorporate the definition of ‘control’ as it appears in the 1997 Code. Under the SEBI (Delisting of Equity Shares) Regulations 2009, a company seeking delisting of securities has to disclose the persons who are in control of the company by means of a public announcement. Under the SEBI (Buyback of
Securities) Regulations 1998, buyback of securities from the promoters or persons in control is prohibited.

10.3.4 **As per SEBI (SAST) Regulations, 2011**

In light of the large number of SEBI regulations that have adopted the definition of ‘control’ as provided in the 1997 Code, SEBI has defined ‘control’ under SAST regulations, 2011. According to its section 2[1(a)], **Control** includes the right to appoint majority of the directors or control management or policy decisions by virtue of shareholding or management rights or shareholding/voting agreements or in any other manner. Where there are two or more persons in control over the Target Company, the cesser of any one of such persons from such control shall not be deemed to be change in control of management. Joint control to sole control is automatically exempted under Regulation 3(1) (e) i.e. inter se\(^{32}\) transfer among promoters. It may be noted here that this definition is only illustrative in nature.

**Acquisition of shares, voting rights or control (trigger limit):**

- **Initial Trigger (acquisition of shares)** - Acquisition of 25% or more of voting rights

- **Subsequent Trigger (acquisition of shares)** - A creeping acquisition limit of 5% per financial year is permitted to any person holding more than 25% but less than maximum permissible non-public shareholding percentage. The acquisition can be through any means.

---

\(^{32}\) Latin for "among themselves," meaning that, for instance, certain corporate rights are limited only to the shareholders or only to the trustees as a group.
10.4 Regulations of Combination

Competition Act, 2002 provide the regulations of combination under section 6, as per this section:-

(1) No person or enterprise shall enter into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and such a combination shall be void.

(2) Subject to the provisions contained in sub-section (1), any person or enterprise, who or which proposes to enter into a combination, shall give notice to the Commission, in the form as may be specified, and the fee which may be determined, by regulations, disclosing the details of the proposed combination, within thirty days of—

(a) approval of the proposal relating to merger or amalgamation, referred to in clause (c) of section 5, by the board of directors of the enterprises concerned with such merger or amalgamation, as the case may be;

(b) execution of any agreement or other document for acquisition referred to in clause (a) of section 5 or acquiring of control referred to in clause (b) of that section.

33[(2A)No combination shall come into effect until two hundred and ten days have passed from the day on which the notice has been given to the Commission under sub-section(2) or the Commission has passed orders under section 31, whichever is earlier.]

(3) The Commission shall, after receipt of notice under sub-section (2), deal with such notice in accordance with the provisions contained in sections 29, 30 and 31.

(4) The provisions of this section shall not apply to share subscription or financing facility or any acquisition, by a public financial institution, foreign

33 Subs. by Competition (Amendment) Act, 2007 for “may, at his or its option”
34 Subs. by Competition (Amendment) Act, 2007 for “seven days”
35 Ins. by Competition (Amendment) Act, 2007
institutional investor, bank or venture capital fund, pursuant to any covenant of a
loan agreement or investment agreement.

(5) The public financial institution, foreign institutional investor\textsuperscript{36}, bank or
venture capital fund\textsuperscript{37}, referred to in sub-section (4), shall, within seven days from
the date of the acquisition, file, in the form as may be specified by regulations,
with the Commission the details of the acquisition including the details of
control, the circumstances for exercise of such control and the consequences of
default arising out of such loan agreement or investment agreement, as the case
may be.

\textsuperscript{36} "Foreign institutional investor" has the same meaning as assigned to it in clause (a) of the Explanation
to section 115AD of the Income-tax Act, 1961(43 of 1961);

\textsuperscript{37} "Venture capital fund" has the same meaning as assigned to it in clause (b) of the Explanation to
clause (23 FB) of section 10 of the Income-tax Act, 1961(43 of 1961);
Chapter 11

ANALYSIS

11.1 COMPARATIVE STUDY

On a perusal of above Acts mentioning the term ‘merger, ‘amalgamation’, control and ‘acquisition’ ends up with few questions.

The Competition Act, 2002 (as amended) if can be compared then we will get to know that the definition of ‘acquisition’ is same as defined under SEBI, 1997, ‘amalgamation or merger’ is not defined and the meaning of ‘control’ is too ambiguous as it is uncertain in other laws as well. These terms revolve around the asset and turnover limits as prescribed by law.

The companies Act, 1956 gives the huddle in understanding the term ‘control’ as it is used in variety of contexts and hence a uniform definition of the term would not suffice for this statute. The definition of ‘control’ is also covered under SEBI laws and according to the definition given above in detail states that the regulation does not provide a clear answer to this. It gives only certain illustrative instances like-

- Shareholding
- management right
- shareholders agreement
- voting agreements

Hence, after doing a comparative analysis with the other laws to Competition law came to few conclusions:

a) ‘Merger or Amalgamation’ is not defined anywhere in the Competition Act that should be defined.
b) ‘Control’ should be defined clearly, according to me it can be defined as, “one or more enterprise or group either jointly or singly, over another group or enterprise shall appoint more than 50% of the other enterprise or to control the management affairs of the other enterprise or policy decisions by virtue of shareholding or management rights or voting rights or in any manner exercisable by a person or person acting individually or in concert, directly or indirectly.”

11.2 CRITICAL ANALYSIS

The Act does not prohibit all mergers per se but regulates only those combinations which cause or are likely to cause an appreciable adverse effect on competition within the “relevant market” in India. *It takes a threshold of assets and turnover as the judging criteria of combination* and the asset and turnover estimates calculated on what basis is not well defined in the act. It also gives *the limit value of M&A considering same value for all types of M&A* (types of M&A have defined in detail in the introduction part of the dissertation).

*The commission is not empowered at many places* as banking M&A are regulated by RBI.

The definition defined by the Competition Act, 2002 (as amended) is already being discussed above but the question arises in the context of ‘acquisition’ as defined in the 2002 Act includes acquisition of control (over management or assets of the enterprise) and this definition is similar to the definition of ‘acquirer’ in the SEBI Act, 1997. This may imply that the meaning of ‘control’ as it appears in the 1997 Act may be referred to while scrutinising any acquisition under the 2002 Act.

The another question arises on ‘control’ as whether the definition provided in the 2002 Act would suffice for an effective analysis of a combination that involves ‘acquisition of control’ and subsequently facilitate identification of the adverse
anticompetitive effects of the proposed combination. The term ‘control’ is not at all mentioning whether it is directly or indirectly, done by a person or person acting individually or in concert. Therefore, it creates ambiguity in definition.

### 11.3 SWOT ANALYSIS

The swot analysis of CCI is done as below in Table 11.1:-

<table>
<thead>
<tr>
<th>STRENGTH</th>
<th>Vast benefit to Indian consumers</th>
<th>Game changer</th>
</tr>
</thead>
<tbody>
<tr>
<td>WEAKNESSES</td>
<td>Increase regulatory hurdles for the businesses in India</td>
<td>Delay and uncertainty may come up due to the time frame under the Competition Law</td>
</tr>
<tr>
<td>OPPORTUNITY</td>
<td>Will use its powers to the international mergers or export cartels, which are being promoted and protected by their own countries</td>
<td>Future time is pregnant with opportunities in the case of M&amp;A for CCI to play its challenging role</td>
</tr>
<tr>
<td>THREAT</td>
<td>meaning revolving around asset and turnover and asset and turnover value estimation is not defined properly</td>
<td>Control definition ambiguity</td>
</tr>
</tbody>
</table>
Chapter 12

FINDINGS

Under the research paper few findings have come into light and they are as:

12.1 ECONOMIC EFFECTS

The main idea behind competition law is economic theory. Value creation through M&A delineates M&A will create an economic advantage when the combined present value of the merged firms is greater than the sum of their individual present values as separate entities. Economic theory gives the following analysis for it. First of all we will see to the single firm market condition. In the diagrams shown below, x-axis is the quantity of Company while y-axis shows the price and cost.

![Figure 12.1](image1)

38 Rising portion of MC curve is the supply curve. MC is the rate at which total cost changes with respect to output.

39 It is average cost curve and is a total cost per unit of output.

40 Average Revenue is the total revenue per unit of output. It can be called as demand curve.

41 Marginal Revenue is the rate at which total revenue changes with respect to output.
In the above diagram, we have shown two different figures (fig 1&2) for the two companies A&B respectively. These are free hand curves, drawn without any data. The AC and AR curves of the two companies are drawn differently to show that the cost structure and the consumer preference for the two companies are different.\textsuperscript{42} Equilibrium is attained at a point where MR=MC. Thus, the shaded region is the profit for the two firms.

![Diagram](image)

**Figure 12.2**

The above diagram in Figure-5 shows the M&A activity done by the company A&B. When two firms get together they form a new company, where, its cost structure and demand challenge for the new firm will change. The price and quantity demanded will also change. The shaded region is the new profit of the merged or acquired firm. Thus, we can see the economic effect of the M&A activity of the firm shows why company go for this policy.

12.2 MANAGERIAL EFFECT

12.2.1 Product Life Cycle Model and M&A

The argument in favour of the assignment of well defined Merger, Acquisition, Control, and Amalgamation is given by the product life cycle model. All products and services have certain life cycles. The life cycle refers to the period from the product’s first launch into the market until its final withdrawal and it is split up in

\textsuperscript{42} It is beyond the scope of this paper to measure the exact demand and cost structures of the firm.
phases. During this period significant changes are made in the way that the product is behaving into the market i.e. its reflection in respect of sales to the company that introduced it into the market. Since an increase in profits is the major goal of a company that introduces a product into a market, the product’s life cycle management is very important. According to my opinion, companies cross these phase too and accordingly judgement can be made whether company can survive or have to merge. The first stage states the emergence of company; second stage introduces the company to the market, third stage says the growth of the company, fourth stage gives the opportunity to the new company to enter and existing companies to word hard for their survival in the market as it is a longer period, it gives much time to existing companies to regain their value in the market and finally, fifth stage is the stage of decline where company is unable to fight in the competition and searching for alternatives to survive their name or company. The five stages can be showed diagrammatically as below:

![Product Life Cycle](image)

*Fig 12.3- Source: William D.*

**An analysis**

Therefore, as all product crosses to different phases to exist in the market likewise, companies do also cover all these phases. According to me, this can also
be termed as ‘Company Life cycle model’. When company enters the 4th and 5th stage, then the condition of M&A can happen, otherwise in all other stages companies do have an option to work as single entity and to enhance the business worth and challenges. Hence, I think it can be a win-win situation for a small firm as well as large firm.

12.2.2 The Bottom Line: What Do Managers Need for Successful M&As?

What lessons do the results convey in terms of thinking about mergers and acquisitions? There are two major takeaways. First, successful M&As appear to be driven primarily about the potential for real side synergies and complementarities. As Amit Kalyani, Executive Director, Bharat Forge, says, "…Each acquisition gave us something new - access to the new passenger car market, to the global market for aluminium components, to the US pick up market, to the engine business in Europe… To them, we offer technology, money, and a strategy to grow their business worldwide." As Kalyani's statements indicate, M&As are primarily about expanding firms' boundaries to exploit organisational skills and capabilities. M&As are not really about expansive empire-building by managers with a taste for large size.

Second, the results suggest that managers need a somewhat unexpected skill set to be successful at M&As - skill at restructuring targets. Mergers are not about passive absorption of targets. Rather, an M&A sets in motion a vigorous restructuring process in which a large proportion of the target assets are hived off. Given the extensive restructuring that follows mergers, successful acquirers should be skilled at restructuring - in deciding what to keep, what to sell, what to close, and how to extract improvements and synergies from what is kept - all within a short period of time. The more effective the planning and execution of the post-merger restructuring, the more likely it is that an M&A is successful.
Chapter 13

CONCLUSION

With the FDI policies becoming more liberalized, Mergers, Acquisitions and alliance talks are heating up in India and are growing with an ever increasing cadence. Whether it’s Indian companies wanting to expand by capturing foreign markets or foreign companies wishing to acquire market share in India, M&A have been used as means to achieve crucial growth and are becoming more and more accepted than ever as a tool for implementing business strategy. Major factors like favourable government policies, buoyancy in the economy, additional liquidity in the corporate sector, and dynamic attitudes of Indian entrepreneurs have helped in facilitating the M&A transactions in India. Therefore conclusion can be drawn from the research paper:

- According to Competition Act, it is a win-win situation for both small and large firms to go for M&A policy
- The threshold limits being specified under competition law and other laws of India help to control the M&A policy so that it should be used as an arsenal and not as fun because coming time is for “survival of the fittest”
- The term ‘control’ has been given various meanings depending on the domain of the concerned legislation. The multiplicity of definitions of the term has at times created uncertainty and ambiguity in the corporate world and among the investor community as rightly said “too many crooks spoil the broth”

Last but not the least, As George Bernard Shaw famously said, “We are made wise not by the recollection of our past, but by the responsibility for our future”; and the future of India is definitely bright!
Chapter 14

RECOMMENDATIONS

The recommendations can be made from the dissertation are as follows:

i. **Ambiguity in the definition of control:** The definition defined in the competition act regarding control is ambiguous because “Control” has been defined under the Act to include controlling the affairs or management of one or more enterprises or group, either jointly or singly. The definition of control is ambiguous and not clear. It should be properly defined what control is and parameters taken for any person, enterprise and organization to go for controlling.

SEBI has come up with a proposal to define control as, “Control” includes the **right or the ability** to appoint majority of the directors or control management or policy decisions by virtue of shareholding or management rights or shareholding/voting agreements or in any other manner. A director or officer of a target company shall not be considered to be in control over the Target Company, merely by virtue of holding such position.

However, addition of word ‘ability’ to the definition of control will only add to the subjectivity to the concept which is most debated and contentious issues.

ii. **Asset and Turnover analysis:** The definition of Combination is revolving around asset and turnover but the clear evaluation of assets and turnover is not mentioned. Therefore, what assets include - current asset, fixed asset or Total asset, Capital asset, etc and what turnover includes- ‘Gross’ or ‘Net’ turnover, inventory turnover, asset turnover, number of shares, etc. Along with this does it have any assumptions or exemptions in asset and turnover limit?
iii. **CCI to be empowered to provide threshold**

iv. **Strategic fit:** The strategic fit between the merging and acquiring companies and the competition laws is vital. As such, understanding the target company and preparing the process on the assumptions is essential.

v. **Synergy should be defined under law:** Synergy should be clearly defined under the competition law because it is one of the very important reasons for the M&A. In general terms, synergy has been defined in the research paper, but if, it touches the legal boundary then the contours of term ‘synergy’ will be more clear and concise in the law book as well as in the organization diary for M&A policy.

Thus, the said suggestions are not against the spirit of the Act, but to enhance the same and make the final outcome more meaningful and perhaps more effective.
Three ideas have come up while working on the project; incentives, benchmark and evaluation on which further research may go.

With regard to incentives, some studies have already been performed but further research on “How to compose the right incentive steps by the CCI to motivate managers and employees to act in the interest of shareholders and other stakeholders of the company in a M&A transaction” is of interest. Incentives mean conceptual clarity, remedies, etc.

The empirical review and study have raised the question on “How to create the right benchmark when studying M&A under different laws of India”. It is not possible to conduct strong empirical studies. Therefore, the semi – strong studies should then be strengthened as much as possible. As such, looking further into the composition of benchmarks could be another area of analysis.

One last perspective brought forward by this project is “The effect of Competition Act, 2002 in M&A evaluation and as well as the effect of other laws and evaluated the comparison for providing the best legal incentives for the organization to use while doing M&A”. Hence, I think this area can be looked deeper into the justification and can come up with few more findings.

There is no doubt that M&A will continue to be carried out. This study has shown that several elements and areas should be considered in order to achieve success when realizing M&A. Due to the continuing M&A activity, regular examinations of the concept under competition and other laws of India should be overviewed.
Chapter 16

REFERENCES

14. The Competition Commission of India Regulations, 2011
15. Gupta, Rajan D. and Arjya B. Majumdar, “Competition issues in M&A”
18. Competition Commission of India, 2010-2011, Annual Report

**Websites Used:**

www.economictimes.com
www.cci.gov.in
www.sebi.gov.in
www.rbi.org.in/FEMA
www.caclub.org.in
www.google.com
www.iclg.co.uk
www.luthra.com
www.nishithdesai.com
www.investopedia.com
www.investorwords.com
http://www.referenceforbusiness.com/management/Str-i/Synergy.html#ixzz1MMIv0LBu
http://en.wikipedia.org/wiki/Monopolistic_competition
Appendix 1: Benefits of M&A

A.1.1 Economies of Scale

It arises when increase in the volume of production leads to a reduction in the cost of production per unit. This is because, with merger, fixed costs are distributed over a large volume of production causing the unit cost of production to decline. Economies of scale may also arise from other indivisibilities such as production facilities, management functions and management resources and systems. This is because a given function, facility or resource is utilized for a large scale of operations by the combined firm. "Economies of scale" is a long run concept and refers to reductions in unit cost as the size of a facility and the usage levels of other inputs increase. The diagram below can define it clearly:

A.1.2 Synergy

According to the American Heritage Dictionary, the term “synergy” is derived from the greek word sunergos, meaning “working together”. Positive synergy is sometimes called the $2 + 2 = 5$ effect. Operating
independently, each subsystem can produce two units of output. However by combining their efforts and working together effectively, the two subsystems can produce five units of output.

Appendix 2: Game Theoretic Approach

A.2.1 Game Theory

Game theory is a method of studying strategic decision making. More formally, it is "the study of mathematical models of conflict and cooperation between intelligent rational decision-makers." An alternative term suggested "as a more descriptive name for the discipline" is interactive decision theory. Game theory is mainly used in economics, political science, and psychology, as well as logic and biology. The first known discussion of game theory occurred in a letter written by James Waldegrave in 1713. Game theory did not really exist as a unique field until John Von Neumann published a paper in 1928. Von Neumann's original proof used Brouwer's fixed-point theorem on continuous mappings into compact convex sets, which became a standard method in game theory and mathematical economics. His paper was followed by his 1944 book *Theory of Games and Economic Behaviour*, with Oskar Morgenstern, which considered cooperative games of several players.

<table>
<thead>
<tr>
<th>Player 2 chooses Left</th>
<th>Player 2 chooses Right</th>
</tr>
</thead>
<tbody>
<tr>
<td>Player 1 chooses Up</td>
<td>4, 3</td>
</tr>
<tr>
<td></td>
<td>– 1, – 1</td>
</tr>
<tr>
<td>Player 1 chooses Down</td>
<td>0, 0</td>
</tr>
<tr>
<td></td>
<td>3, 4</td>
</tr>
</tbody>
</table>

*Normal form or payoff matrix of a 2-player, 2-strategy game*
The extensive form of the Game Theory used to formalize games with a time sequencing of moves and the normal game is usually represented by a matrix which shows the players, strategies, and pay-offs.

A.2.2 Prisoner’s Dilemma

The prisoner's dilemma is a canonical example of a game analyzed in game theory that shows why two individuals might not cooperate, even if it appears that it is in their best interest to do so. It was originally framed by Merrill Flood and Melvin Dresher working at RAND in 1950. Albert W. Tucker formalized the game with prison sentence payoffs and gave it the "prisoner's dilemma" name (Poundstone, 1992). A classic example of the prisoner's dilemma (PD) is presented as follows:

Two men are arrested, but the police do not possess enough information for a conviction. Following the separation of the two men, the police offer both a similar deal—if one testifies against his partner (defects/betrays), and the other remains silent (cooperates/assists), the betrayer goes free and the co-operator receives the full one-year sentence. If both remain silent, both are sentenced to only one month in jail for a minor charge. If each 'rats out' the other, each receives a three-month sentence. Each prisoner must choose either to betray or remain silent; the decision of each is kept quiet. What should they do?

Generalized Form:

The structure of the traditional Prisoners’ Dilemma can be analyzed by removing its original prisoner setting. Suppose that the two players are represented by colours, red and blue, and that each player chooses to either "Cooperate" or "Defect".
If both players play "Cooperate" they both get the payoff $A$. If Blue plays "Defect" while Red plays "Cooperate" then Blue gets $B$ while Red gets $C$. Symmetrically, if Blue plays "Cooperate" while Red plays "Defect" then Blue gets payoff $C$ while Red gets payoff $B$. If both players play "Defect" they both get the payoff $D$.

In terms of general point values:

<table>
<thead>
<tr>
<th>Canonical PD payoff matrix</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
<tr>
<td><strong>Cooperate</strong></td>
</tr>
<tr>
<td><strong>Defect</strong></td>
</tr>
<tr>
<td><strong>Cooperate</strong></td>
</tr>
<tr>
<td>$A, A$</td>
</tr>
<tr>
<td>$C, B$</td>
</tr>
<tr>
<td><strong>Defect</strong></td>
</tr>
<tr>
<td>$B, C$</td>
</tr>
<tr>
<td>$D, D$</td>
</tr>
</tbody>
</table>

To be a prisoner's dilemma, the following must be true:

$B > A > D > C$

It is not necessary for a Prisoner's Dilemma to be strictly symmetric as in the above example, merely that the choices which are individually optimal (and strongly dominant) result in an equilibrium which is socially inferior.