J.K. SHAH®

SUGGESTED SOLUTION

CS PROFESSIONAL

Subject – Corporate Restructuring

Topic – Part-I - Test-1 Chp-1 To 7

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Answer to Q1.A.

Regardless of their category or structure, all mergers and acquisitions have one common goal: they are all meant to create synergy that makes the value of the combined companies greater than the sum of the two parts. The success of a merger or acquisition depends on whether this synergy is achieved. Synergy takes the form of revenue enhancement and cost savings. By merging, the companies hope to benefit from the following:

- Becoming bigger: Many companies use M&A to grow in size and leapfrog their rivals. While it can take years or decades to double the size of a company through organic growth, this can be achieved much more rapidly through mergers or acquisitions.
- Preempted competition: This is a very powerful motivation for mergers and acquisitions, and is the primary reason why M&A activity occurs in distinct cycles.
- Domination: Companies also engage in M&A to dominate their sector. However, since a combination of two behemoths would result in a potential monopoly, such a transaction would have to face regulatory authorities.
- Tax benefits: Companies also use M&A for tax purposes, although this may be an implicit rather than an explicit motive.
- Economies of scale: Mergers also translate into improved economies of scale which refers to reduced costs per unit that arise from increased total output of a product.
- Acquiring new technology: To stay competitive, companies need to stay on top of technological developments and their business applications. By buying a smaller company with unique technologies, a large company can maintain or develop a competitive edge.
- Improved market reach and industry visibility: Companies buy other companies to reach new markets and grow revenues and earnings. A merger may expand two companies' marketing and distribution, giving them new sales opportunities. A merger can also improve a company's standing in the investment community: bigger firms often have an easier time raising capital than smaller ones.

(5 marks)

Answer to Q1.B.

Although open offer once made cannot be withdrawn yet Regulation 23 of SAST Regulations, 2011 provide certain exceptions.

They are as under:

(a) Statutory approvals required for the open offer or for effecting the acquisitions attracting the obligation to make an open offer have been refused subject to such requirement for approvals having been specifically disclosed in the Detailed Public Statement and the letter of offer;

(b) Any condition stipulated in the Share Purchase Agreement attracting the obligation to make the open offer is not met for reasons outside the reasonable control of the acquirer, subject to such conditions having been specifically disclosed in the Detailed Public Statement and the letter of offer;

(c) Sole acquirer being a natural person has died;

(d) Any other circumstances if SEBI merit withdrawal of open offer.

(5 marks)

Answer to Q1.C.

1. Every petition or application or reference shall be filled in form as provided in Form No. NCLT-1 with attachments thereto accompanied by Form No. NCLT-2
2. In case of an interlocutory application, the same shall be filed in Form No. NCLT-1 accompanied by such attachments thereto along with the Form No.NCLT-3.
3. Every petition or application including interlocutory application shall be verified by an affidavit in Form No.NCLT-6.
4. All advertisement and notices shall be in Form No. NCLT-4.
5. Notice to be issued by the NCLT to the opposite party shall be in Form No.NCLT-5.

(5 marks)

Answer to Q1.D.

Earning Before Merger

	Big Ltd.	Small Ltd.
Earnings After Tax	5,00,000	1,25,000
No. of Shares	2,50,000	1,25,000
Earnings Per Share (EPS) = Total Earnings/no. of Shares	2	1
Market Price Per Share (MP)	20	10
P/E Ratio =MP/EPS	10	10

(2) Exchange Ratio

Total number of shares in the post-merger Company

Total earnings after merger = 5, 00,000 + 1, 25, 000 = Rs. 6, 25,000

Pre-Merger earnings of Big Ltd. = 2

Number of share to be issued = Post - Merger Earning/ PreMerger EPS of Big Ltd.

= 6,25,000/2

= 3, 12, 500

Number of shares to be issued = 3, 12,500 - 2, 50,000 = 62,500

Number of existing share of Small Ltd. = 1, 25,000

Exchange Ratio = 62,500/1,25,000 = 0.50

Thus one share of Big Ltd. will be issued for every two shares of Small Ltd.

(5 marks)

Answer to Q2.A.

Section 66 of the Companies Act, 2013 provides that subject to confirmation by the Tribunal on an application by the company, a company limited by shares or limited by guarantee and having a share capital may, by a special resolution, reduce the share capital in any manner.

Hence we can see that section 66 of the Companies Act, 2013 is applicable to a company limited by shares or a company limited by guarantee and having share capital.

An unlimited company can reduce the share capital in the manner specified in the Articles and Memorandum of the company, as Section 66 of the Companies Act, 2013 is not applicable.

(3 marks)

Answer to Q2.B.

As per section 235 of the Companies Act, 2013, the dissenting shareholders have been put at the limit of 10% of the value of the shares of the company. In case of listed companies, SEBI takes cognizance of even a single shareholder to initiate investigation for remedial action under SEBI (SAST) Regulations, 2011. In case of all companies, if promoters resort to take over under section 235 of the Companies Act, 2013, a transferee company, which has acquired 90% shares of a transferor company, through a scheme or contract, is entitled to acquire shares of remaining 10% shareholders.

Dissenting shareholders have been provided with an opportunity to approach Tribunal. If the price fixed is not acceptable, even a single shareholder can approach National Company Law Tribunal to seek clarification and justice.

(3 marks)

Answer to Q2.C.

External Commercial Borrowings (ECB) are commercial loans raised by eligible resident entities from recognised non-resident entities confirming to parameters with minimum maturity, permitted and non-permitted end-uses, minimum all-in-cost ceiling, etc. The parameters apply in totality and not on a standalone basis.

Reserve Bank of India issued Foreign Exchange Management (Borrowing and Lending) Regulations, 2018 for borrowing and lending between a person resident in India and a person resident outside India. Minimum Average Maturity Period (MAMP) of ECB are 3/5/7/10 years. ECB framework permits resident entities to borrow from recognised non-resident entities in any form including bank loans, Securitised instruments, buyers' credit, suppliers' credit, Foreign Currency Convertible Bonds (FCCBs), Financial Leases and Foreign Currency Exchangeable Bonds (FCEBs).

(3 marks)

Answer to Q2.D.

Accounting Standard-14 (Accounting for Amalgamations) is applicable only in case of amalgamation and not in case of demerger. Accounting Standard-14 lays down the

accounting and disclosure requirements in respect of amalgamations of companies and the treatment of any resultant goodwill or reserves.

In the scheme of arrangement between Sony India Private Limited (Sony India) and Sony Software Centre Private Limited (Sony Software), the Delhi High Court, while approving scheme of arrangement between Sony India has clarified that AS-14 is applicable only to amalgamations and not to demerger. The same was also upheld by Gujarat High court in the case of Gallops Realty Private Limited.

(3 marks)

Answer to Q2.E.

The poison pill technique, sometimes also known as a shareholder rights plan, is a form of defense against a potential hostile takeover. It is a technique by which the target company seeks to make itself less desirable to potential acquirers.

A controversial but popular defense mechanism against hostile takeover bids is the creation of securities called “poison pills". These pills provide their holders with special rights exercisable only after a period of time following the occurrence of a triggering event such as a tender offer for the control or the accumulation of a specified percentage of target shares. These rights take several forms but all are difficult and costly to acquire control of the issuer, or the target firm. Poison pills are generally adopted by the Board of Directors without shareholders’ approval but the technique is vulnerable to Court review as such considered enhancing the ability of the Board of Directors to bargain for a "fair price” though takeovers cannot be prevented.

(3 marks)

Answer to Q3.A.

Any default in payment of term loan, public deposits, and debentures becomes a hurdle in buy-back of securities. However, in the instant case, the default is remedied prior to 3 years of the proposal as stated in proviso to section 70(1)(c) of the Companies Act, 2013. Buy-back is also prohibited if done through any subsidiary or further subsidiaries down the line, through any sole or group investment companies and/or if there are failures in compliance of section 92 (annual return), sections 123 or 127 (distribution of dividends) or section 129 (financial statements) of the Companies Act, 2013.

In the given case the Company has default of payment of certain installments of the Bank was made good by July, 2013, and three (3) years has been passed before the passing of resolution by Board, So Company can go ahead for the Buy-back proposal.

Further, it is necessary to ensure debt to equity ratio is at least 1:2 post buy-back and shares ascribed for buy-back are fully paid-up. Process of buy-back need to be completed within 12 months of authorization. Shares bought back need to be destroyed within seven days of the last date of completion of buy-back.

(5 marks)

Answer to Q3.B.

Leverage is an investment strategy of using borrowed money, specifically, the use of various financial instruments or borrowed capital to increase the potential return of an investment. When one refers to something (a company, a property or an investment) as “highly leveraged,” it means that item has more debt than equity.

A leveraged buyout (LBO) is the acquisition of a company in which the buyer puts up only a small amount of money and borrows the rest. The buyer can achieve this desirable result because the targeted acquisition is profitable and throws off ample cash used to repay the debt. The expectation with leveraged buyouts is that the return generated on the acquisition will more than outweigh the interest paid on the debt, hence making it a very good way to experience high returns whilst only risking a small amount of capital.

In 2000, a landmark deal was witnessed in the Indian corporate history, when Tata Tea acquired the UK brand Tetley for 271 million pounds. This deal was the largest cross border acquisition by any India Company. Apart from the size of the deal, what made it particularly special was the fact that it was the first ever leveraged buyout by any Indian company.

Structure of the deal: Tata Tea created a Special Purpose Vehicle (SPV)-christened Tata Tea (Great Britain) to acquire all the properties of Tetley. The SPV was capitalised at 70 mn pounds, of which Tata tea contributed 60 mn pounds; this included 45 mn pounds raised through a GDR issue. The US subsidiary of the company, Tata Tea Inc. had contributed the balance 10 mn pounds.

(5 marks)

Answer to Q3.C.

In brief, it can be said that there are eight stages involved in merger and amalgamation, which are listed below:

Stage1 – Drafting of the Scheme

Stage2 – Obtaining the approval of the Board of Directors of the companies involved

Stage3 – Obtaining approval of the stock exchanges in case of listed companies

Stage4 – Application / Petition for convening the meeting of members/creditors shall be filed with National Company Law Tribunal

Stage5 – Convening meetings of the Shareholders and Creditors and obtaining their consent on Scheme

Stage6 – Approvals or No objection from Regional Director / Official Liquidator

Stage7 – Filing of final petition with NCLT for approving the Scheme

Stage8 – Obtaining order for approval for scheme of merger/amalgamation from the National Company Law Tribunal.

(5 marks)