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# Mergers & Acquisitions in India

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**Managing Partner**

**Tokyo, Japan**

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# About Amarchand Mangaldas..... amarchand mangaldas

*TOTAL LAWYERS*  
430

*PRESENCE IN INDIA*  
*IN 5 MAJOR CITIES*

*TOTAL PARTNERS*  
40

*OVER 95 YEARS OF*  
*EXPERIENCE*

*WHO'S WHO LEGAL LAW*  
*FIRM OF THE YEAR 2007*

*ASIA PACIFIC LAW FIRM*  
*FOR THE YEAR 2004*

- India's leading and largest law firm
- Consistently voted as one of the top law firms in Asia-Pacific
- Clients include domestic and foreign commercial enterprises, financial institutions as well as state and regulatory bodies. Our client base also includes leading companies and financial institutions from Japan



Consistently been rated as the top law firm in India by various professional organizations

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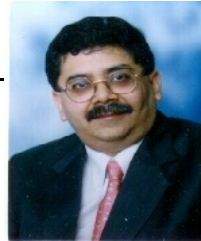


# About The Speaker

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**Name**            **CYRIL SHROFF**

**Title**            **Managing Partner**  
**Mumbai, India**



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- Experience**
- Cyril is a leading practitioner in the field of corporate and securities law and has been associated with a significant number of high-profile and complex mergers and acquisitions and securities market transactions by Indian issuers
  - Cyril has over 25 years of experience in a wide range of areas including corporate, governmental policy, infrastructure and others
  - Cyril has been a member of several governmental and other committees pertaining to law reform concerning the corporate and securities market, commercialization of infrastructure etc. and is consulted extensively on policy matters by the Government of India
  - Cyril has been consistently rated as India's leading lawyer in most practice areas by several international surveys including those conducted by International Financial Law Review (IFLR), Euromoney, Chambers Global, Asia Legal 500, Asia Law and others
  - Cyril has authored several publications on legal topics. He is a member of the Centre for Study of the Legal Profession established by the Harvard Law School (HLS)

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**Education**            L.L.B. – Admitted to the Bar in 1982  
Solicitor, Bombay High Court

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# Part I: Negotiation And Establishment Of A Newly Created Joint Venture

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# Business Operations In India

- A Foreign Company planning to set up business operations in India has the following options:
  - as an Indian company; or
  - as a Foreign company
- As an Foreign Company, business can be commenced as:
  - Liaison Office / Representative Office
  - Project Office
  - Branch Office
    - Requires RBI approval and registration with RoC
      - Restrictive in nature as no manufacturing activity can be carried out directly or indirectly



# Business Operations In India

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- Technical Collaboration: Technology payments for transfer of know-how
  - FEMA implications
- As an Indian Company, business can be commenced as:
  - Wholly-owned subsidiary
  - Joint venture

# Business Operations: Establishing A Company In India



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- Two kinds of companies: private or public
  - Requirements of a private company:
    - Minimum of two (2) shareholders
    - Minimum of two (2) directors
    - Minimum paid up capital of Rs. 0.1 million (Rs. 100,000/-)
    - Articles of Association must restrict / prohibit:
      - Transferability of shares
      - Number of members to 50
      - Invitation / Acceptance of public deposits
      - Making an invitation to the public to subscribe to shares

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# Business Operations: Establishing A Company In India



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- Requirements of a public company:
  - Minimum of seven (7) shareholders
  - Minimum of three (3) directors
  - Minimum paid up capital of Rs. 0.5 million (Rs. 500,000/-)
  - Shares must be freely transferable
  - No limit on the number of members
  - Can invite members of the public to subscribe to shares

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# Establishing A Company: Process Of Incorporation



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- Filings are done electronically
  - D.I.N./ D.S.C. are essential
- Application for D.I.N./ D.S.C.
- Determine the place of registered office
- Reserve company name
  - Done via an electronic application to the regional RoC
- Prepare and stamp the Memorandum and Articles of Association

Ministry of Corporate Affairs, Government of India: [www.mca.gov.in](http://www.mca.gov.in)

# Establishing A Company: Process Of Incorporation



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- File for registration
  - Application accompanied by registration fees, Memorandum and Articles of Association, certificate of name availability
  - Names and particulars of directors
- Obtain a Certificate of Incorporation
  - Public companies also need a certificate of Commencement of Business
- In case of non residents, documents would have to be notarised and consularised

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# Business Operations: Establishing A Company In India



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- Typically takes 33 days to set up a private company, down from 71 in 2006

Starting a Business data	Doing Business 2006	Doing Business 2007	Doing Business 2008
Rank		93	111
Procedures (number)	11	11	13
Duration (days)	71	35	33

*(Doing Business in India 2008 – World Bank report)*

- Costs
  - Registration fees
  - Stamp duty on share capital
    - Rates vary state to state
  - Registration fees for D.I.N./ D.S.C.

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# Joint Ventures

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# Joint Ventures: Overview

- Can be established by either:
  - Establishing up a JV with Indian joint venture partners; or
  - Investing in a suitable existing Indian company
- Advantages:
  - Brings visibility, distribution / marketing infrastructure, financial resources
  - Established contacts of the Indian partner cutting down the go-to-market time
  - Ease in navigating legal and regulatory channels
  - Local expertise



# Joint Ventures: Overview

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- Limitations
  - “Same field” restriction (P.N. 1/2005)
    - Existing venture as on January 12<sup>th</sup>, 2005
    - 3% or more equity stake
    - Venture not sick / defunct
  - Sector-wise caps
    - Will decide extent of participation



# Joint Ventures - Preliminary Steps

- Finding a suitable Indian JV partner
  - Can be sourced through local investment advisors e.g. Investment Banks
- Due Diligence
  - Limited DD on JV partner
  - Usually done through common, publicly available sources
  - Main factors to consider include:
    - Market presence / track record
    - Relationship with relevant regulators



# Joint Ventures - Preliminary Steps

## Signing of an MoU beforehand

- Exclusivity in negotiations
- Decisions on the extent of participation – majority / minority / 50:50 stake(s)
- Structuring
  - Tax implications e.g. Indo-Japan DTAA





# Joint Ventures - Negotiation

- Things to discuss include:
  - Shareholder and management rights – “Veto Rights”
  - Committee / Board representation- proportionate to shareholding?
  - Valuation
    - Carried out by independent valuers e.g. Chartered Accountants
    - FEMA
  - Use of Intellectual Property
    - Use of names of JV partners
    - Technology transfer
    - Royalty payments
  - “Promoter” obligations
  - Non-compete
    - In the same field as the joint venture
    - Time limits



# Joint Ventures - Negotiation

- Things to bear in mind include:
  - Several Indian companies are 'promoter' run
  - Generational dynamics at play as well
  - Family controlled / Entrepreneur driven companies – expectation of “emotional” valuation
  - Control over management restricted in certain cases
    - Telecom
    - Aviation
    - Media
  - Valuation multiples are relatively higher as expectation of growth is factored in most cases
  - Negotiations are mostly driven by the top management and represented by lawyers and accountants



# Joint Ventures - Negotiation

- Many Indian companies are not well-versed with diligence requirements unless they have prior experience – but number is increasing
- Convergence towards International M&A practice
- Regulatory experience is tedious, not sure of ‘promote’ or ‘protect’ – however regulators are opening up to foreign investment
- Listed companies – applicability of the SEBI (Prohibition of Insider Trading) Regulations 1992



# Joint Ventures - Documentation

- JV agreements are usually heavily negotiated
- Salient features of an SHA / JVA include:
  - Shareholder rights at different stakes
  - Management representation
  - Pooling of Voting Rights
  - Minority Protection
  - Transfer restrictions
    - Tag/drag rights, put/call options, rights of first refusal
  - Lock in restrictions
  - Representations and warranties
    - Indemnities
    - Disclosed liabilities are an exception – “Disclosure Letter”

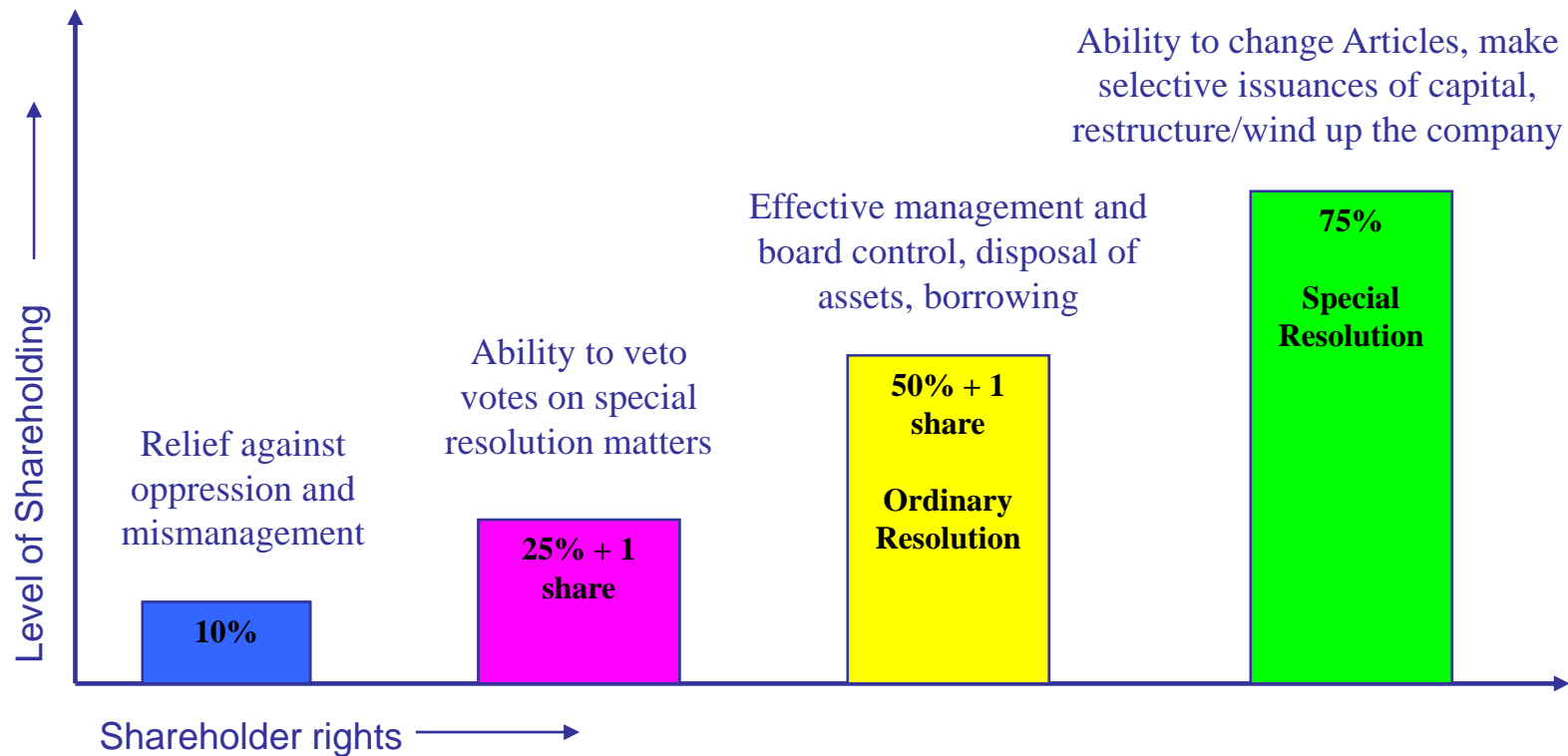


# Joint Ventures- Documentation

- Exit options
  - IPOs; sales to other investors / restrictions on sale to certain types of investors
- Dispute resolution and governing law.
  - Arbitration is usually preferred
- Implications under the Takeover Code
- Enforceability (inclusion in Articles)



# Key Shareholder Rights





# Joint Ventures - Implementation

- Typical actions at closing:
  - Issue of shares to JV partners
  - Sharing of know-how and expertise
- May be incorporated as a fully operational company
- May be incorporated as a “Shell Company”
  - Transfer of business / assets
  - Holding of investments



# Part II: Due Diligence

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# Due Diligence

- Objective:
  - Uncovering matters relating to assets, liabilities and operations
    - Impairing successful of the transaction
    - Erosion of value
  - Determination of an efficient structure
- Scope
  - May be limited or full-fledged
    - Limited DD
      - May relate only to specific aspects e.g. litigation or employment related matters
      - Faster and cheaper, and used when time is of the essence. But risks involved
    - Full-fledged DD
      - Entails a detailed and thorough review of the company
      - Typically covers everything!
      - Time consuming but thorough
      - Legal vs. other diligences e.g. financial, tax



# Conducting A Due Diligence

- Who conducts the due diligence?
  - Legal due diligence - done by local counsel
  - specific due diligence – done by specialist professionals e.g. accountants for financial due diligences; HR experts for employee related matters
- What to look for during the due diligence?
  - Corporate compliance - appropriate shareholder resolutions, timely filings
  - Articles of Association – restrictions, special promoter rights etc



# Conducting A Due Diligence

- Material contracts – consents from contracting parties, change of control restrictions
- Litigation – value of claims against the company, impact on company's ability to carry on business
- Loans and security – encumbrances on assets, total extent of liability
- Employment / labour – key employees, golden parachutes, share options and labour disputes
- Licenses and permits – existence and validity of permits, breach of conditions and change in control



# Independent Verification

- ROC search
  - Electronic filings and physical documents
    - Share capital, directors, shareholders, charges
- Title search (immoveable property)
  - Name of registered owner
  - Encumbrances
- Litigation search
  - Matters filed against the company
  - Matters filed by the company
- Trademark / Patent search
  - Name of the registered owner of the IP
  - Details of any licenses granted



# Due Diligence: Limitations

- Private / Unlisted companies that are family run or closely held:
  - Compliance with Indian corporate governance norms may not be satisfactory
  - Record keeping might not be at par with international standards
  - Books of Accounts and Financial Statements - Audit by Independent Professionals
- Certain Government records might not be well maintained or readily accessible e.g. land records
- Accessing public records may be cumbersome- yards of “Red-tape”
- Language – public records may be in vernacular languages

# Processing The Results Of The Due Diligence



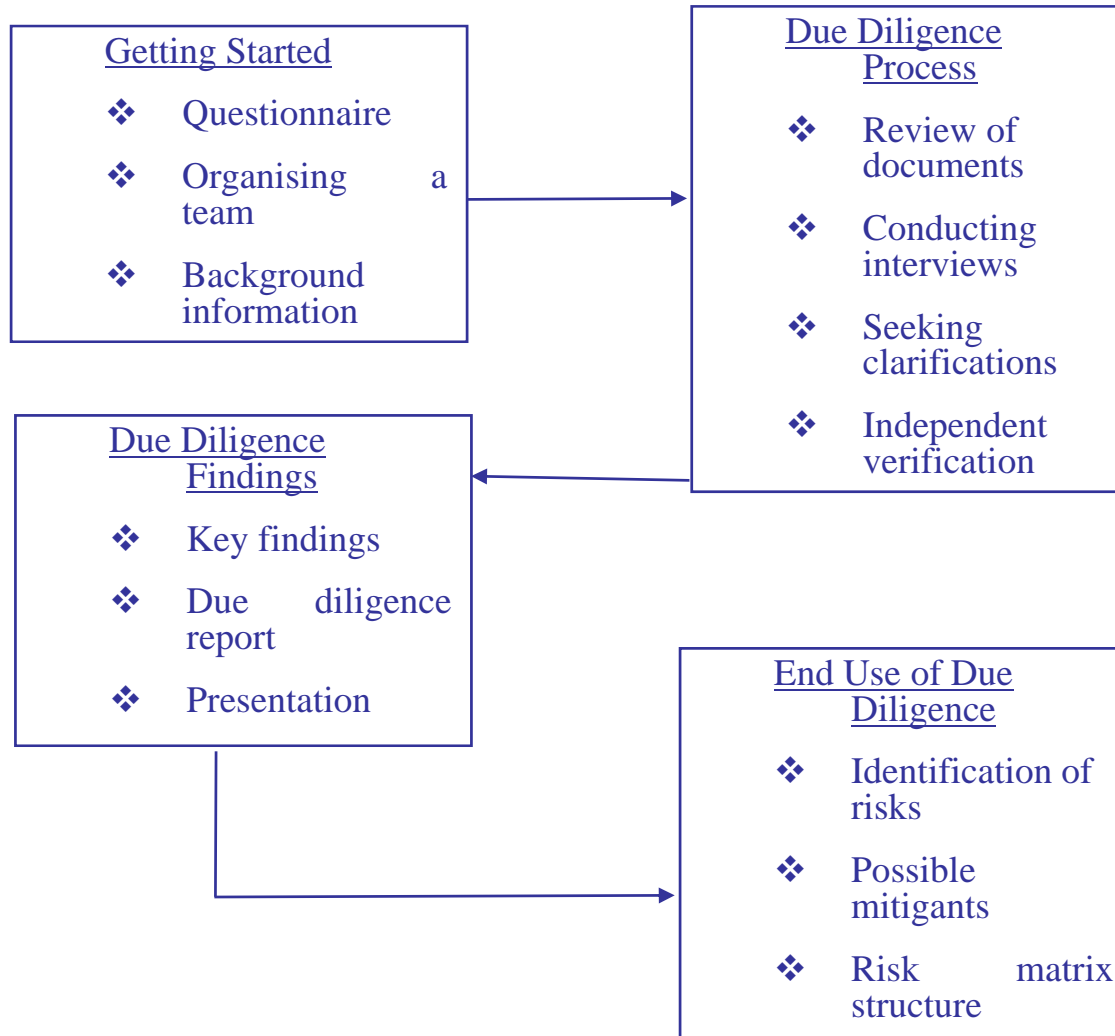
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- Deal-breakers e.g. expiry of a key lease / permit, restrictions on change of control
- Transaction structure e.g. tax focused re-structuring
- Valuation e.g. additional liabilities
- Conditions precedent e.g. securing key approvals
- Representations and warranties e.g. complete disclosure of material information; potential liabilities identified during due diligence
- Indemnity – negotiations for higher indemnity caps, longer duration of indemnity if results not satisfactory

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# Steps Involved In A Due Diligence



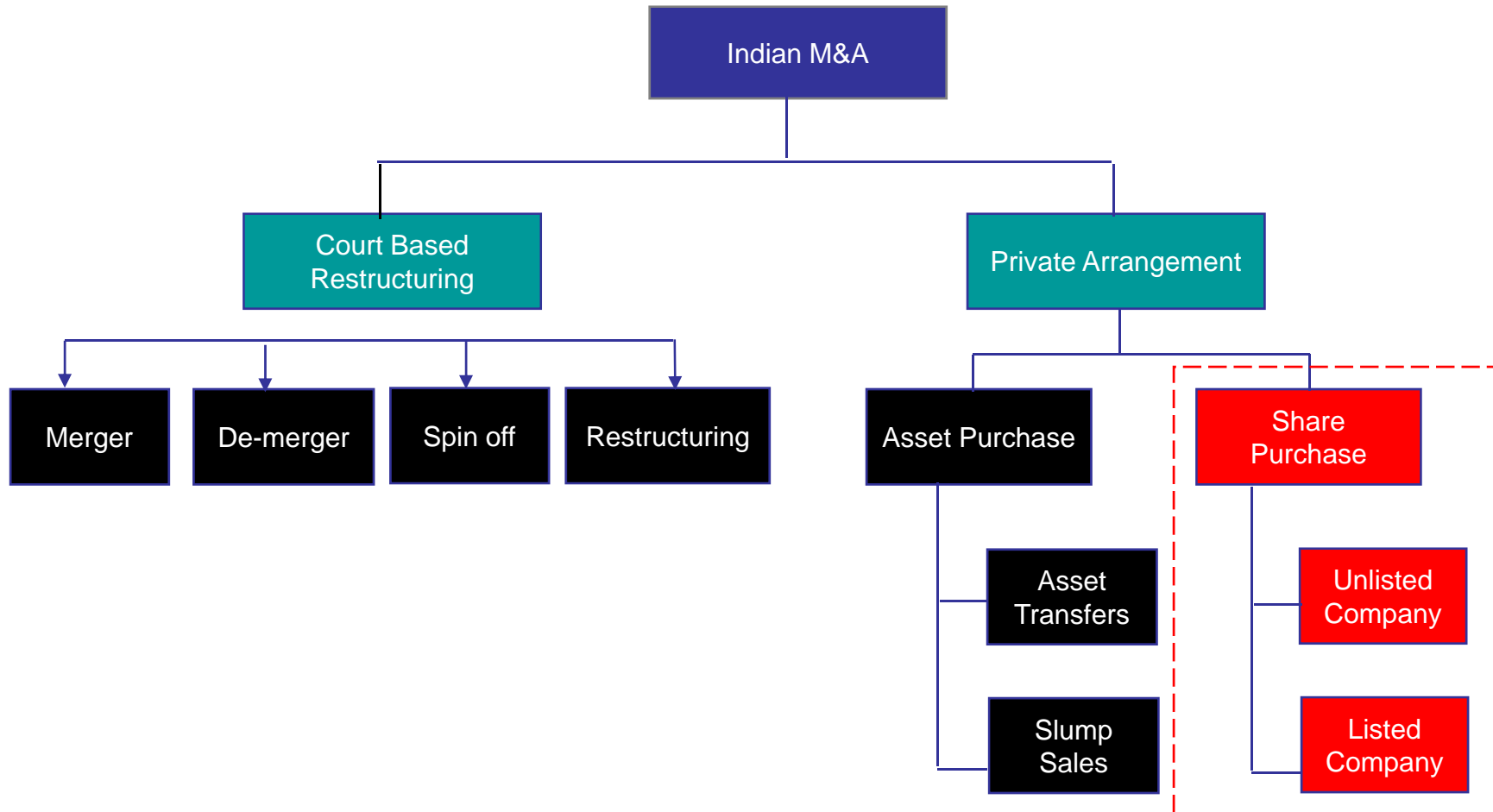


# Acquisition Of Shares / Equity Interests

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# Varieties Of M&A In India



# Share Acquisition – Investment Procedure



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Procedure differs for listed and unlisted Companies

- Unlisted companies:
  - Primary Acquisition - Preferential Allotment
    - Corporate Approvals
      - Section 81(1A) Resolution – Special Resolution required
      - For a rights issue to existing shareholders - Ordinary Resolution required
    - Price
      - Pricing Guidelines prescribed by the RBI
    - For private companies, Board approvals are adequate

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# Share Acquisition Investment Procedure



- Listed companies
  - Primary Acquisition - Preferential Allotment
    - Eligibility
    - Corporate Approvals
      - Special Resolution
    - Price
      - Not lower than the 2 weekly or 6 monthly price average on a recognised stock exchange
    - Lock In
    - Allotment
      - 15 days from Shareholders Resolution
      - Extension for Regulatory Approvals
    - Convertible Instruments
      - Pricing
      - Time Period for Conversion

<u>Date</u>	<u>Actions Required</u>
T-45	Relevant Date for the purposes of calculating the floor price for the issue of shares
Between T-45 to T- 36	Board meeting to be held to approve issue of shares
Up to T-36	Date of issue of notices to shareholders calling for EGM to approve issue of shares
T-15	Date of shareholder approval
T	Date of Allotment of shares



# Takeover Code

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# Takeover Code

- Listed company (direct / indirect)
- “Trigger”
  - Substantial acquisition of shares or voting rights of a listed company
  - Change of “control”
- Tender offer (for a minimum 20%) – Triggers
  - First trigger at 15%
  - Creeping Limit of 5% between 15% and 55%
  - Any Acquisitions between 55% and the relevant delisting threshold (75/90%)
  - “Control” (regardless of percentage)
- Disclosure thresholds at 5%, 10%, 14%, 54% & 74%
- Applies to direct or indirect acquisitions (“chain principle”) of voting rights or control

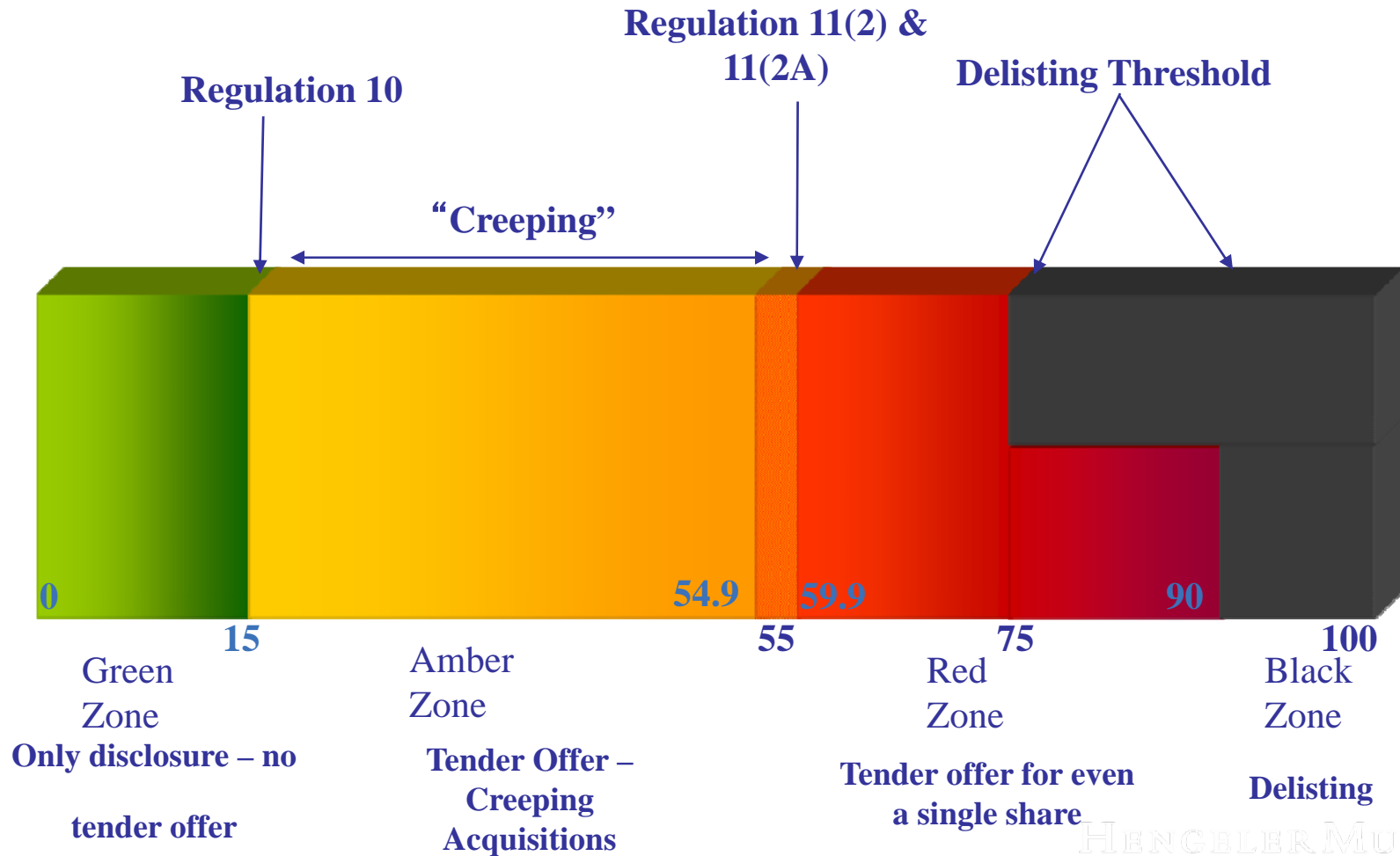


# Takeover Code

- Convertible Instruments trigger tender offer obligations at the time of conversion (“voting rights”)
- Open Offer subject to sectoral caps, investment beyond limit requires FIPB approval
- Transfers between residents and non-residents pursuant to an open offer require prior RBI approval
- Requirements of a public offer
  - Public announcement to be made within 4 days of acquiring the shares or entering into an agreement to acquire
  - Letter of Offer to be cleared by SEBI
  - Offer can be conditional upon a minimum level of acceptance which may be less than 20%, provided 50% of the cash consideration has been deposited in escrow



# Threshold And Triggers



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# Open Offer Time Line

Event	Typical Time (days)	Regulation
Public Announcement under the Code	X + 4 [Y]	Regulation 14
File for all regulatory approvals, if any required	X + 4 [Y]	Foreign Exchange Regulations
Filing draft Letter of Offer (LOO) with SEBI	Y + 14	Regulation 18(1) and Regulation 22(2)
Application to the RBI for Open Offer	Y	
Specified Date for determination of Shareholders to whom the LOO should be dispatched	Y + 30	Regulation 19
SEBI comments on the LOO	Y + 35	Regulation 18(2)
Dispatch of Final LOO to the Shareholders	Y + 37	Regulation 18(2)
Approximate date for receipt of regulatory approvals applied for	Y + 42	Foreign Exchange Regulations
LOO to reach Shareholders	Y + 44	Regulation 22(3)
Opening of Offer	Y + 55	Regulation 22(4)
Closure of Offer	Y + 75	Regulation 29
Dispatch of Payment	Y + 90	Regulation 22(12)
Merchant Banker Report	Y+ 120	Regulation 24(7)

HNCFERKVIJLBR





# Exemptions

- When is one exempted from making a tender offer?
  - Inter-se transfer amongst group companies, qualifying promoters, qualifying Indian promoters and foreign collaborators, relatives; 3 year holding requirement; price not exceeding 25% of the Reg. 20 formula
  - Allotment pursuant to a public issue
  - Under a scheme of amalgamation or reconstruction
  - Rights Issues; change in control
  - Acquisition of shares by government companies and statutory corporations
  - Banks as pledgees
  - Transfer of shares from venture capital funds or FVCI registered with SEBI to promoters of a venture capital undertaking pursuant to an agreement



# Hostile Takeovers

- Regulations envisage unsolicited offers (“hostile”)
- No regulatory restriction on a hostile takeover by a foreign investor
- Still some exception for certain sectors – financial services
- Control of the process is with the acquirer – the Target is in passive mode
- Practically and culturally however, the market is not yet inclined towards being open to hostile acquisitions and there are very limited precedents in this regard owing to:
  - Standing of Indian Promoters (and their ability to influence the regulatory mindset)
  - “Economic nationalism”
  - Business environment



# Takeover Defences

Takeover defenses available in India	Takeover defenses not available in India
<ul style="list-style-type: none"><li>• Subject to shareholders approval<ul style="list-style-type: none"><li>- “Scorched Earth” Tactics</li><li>- “Crown Jewels”</li></ul></li><li>• “White Knight”</li><li>• Lobbying to Economic Nationalism</li><li>• Embedded defenses<ul style="list-style-type: none"><li>- Change of control clauses in material contracts</li><li>- Golden (or “tin”) parachutes</li><li>- Rights incorporated in the articles</li><li>- “Brand” pill</li></ul></li></ul>	<ul style="list-style-type: none"><li>• Staggered Board</li><li>• Consolidation of promoter shareholding at a discount</li><li>• Shareholder Rights Plan</li></ul> <p style="text-align: right; font-weight: bold; font-size: 1.2em;">HENGBLER MUELLER</p>



# “Going Private” / Delisting

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# “Going Private” / Delisting

- Recommended minimum public shareholding – 25% in most cases
- In certain cases minimum public shareholding of 10% permitted
- Delisting rules to apply if
  - The delisting limit is breached at the time of takeover, or
  - Public shareholding falls below minimum limit in listing agreement
- SEBI or the stock exchange can ask the company to compulsorily delist and provide shareholders an exit option
- Public offer under the SEBI (Delisting of Securities) Guidelines, 2003 to be made – (reverse Dutch auction)

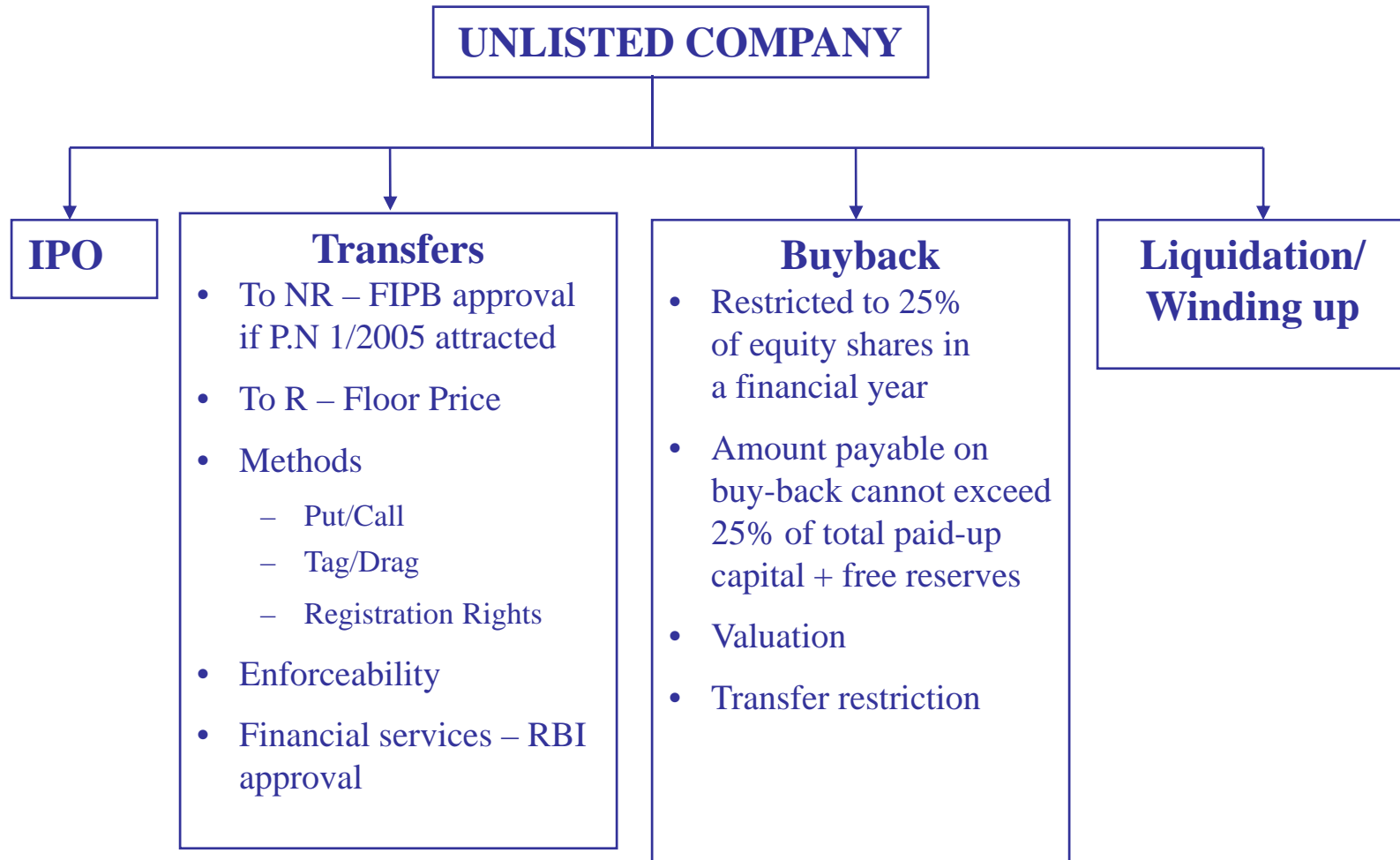


# “Going Private” / Delisting

- In case of voluntary delisting the company must approve the delisting by special resolution
- Minority Squeeze Out
  - No defined regime – not possible presently
- Shareholders might not tender into the open offer
  - Lack of awareness of delisting offer
  - Non-supportive of delisting, indicated price “not in range”
  - Unfavorable tax treatment for shares not sold through stock exchanges



# Exit Options – Unlisted Companies

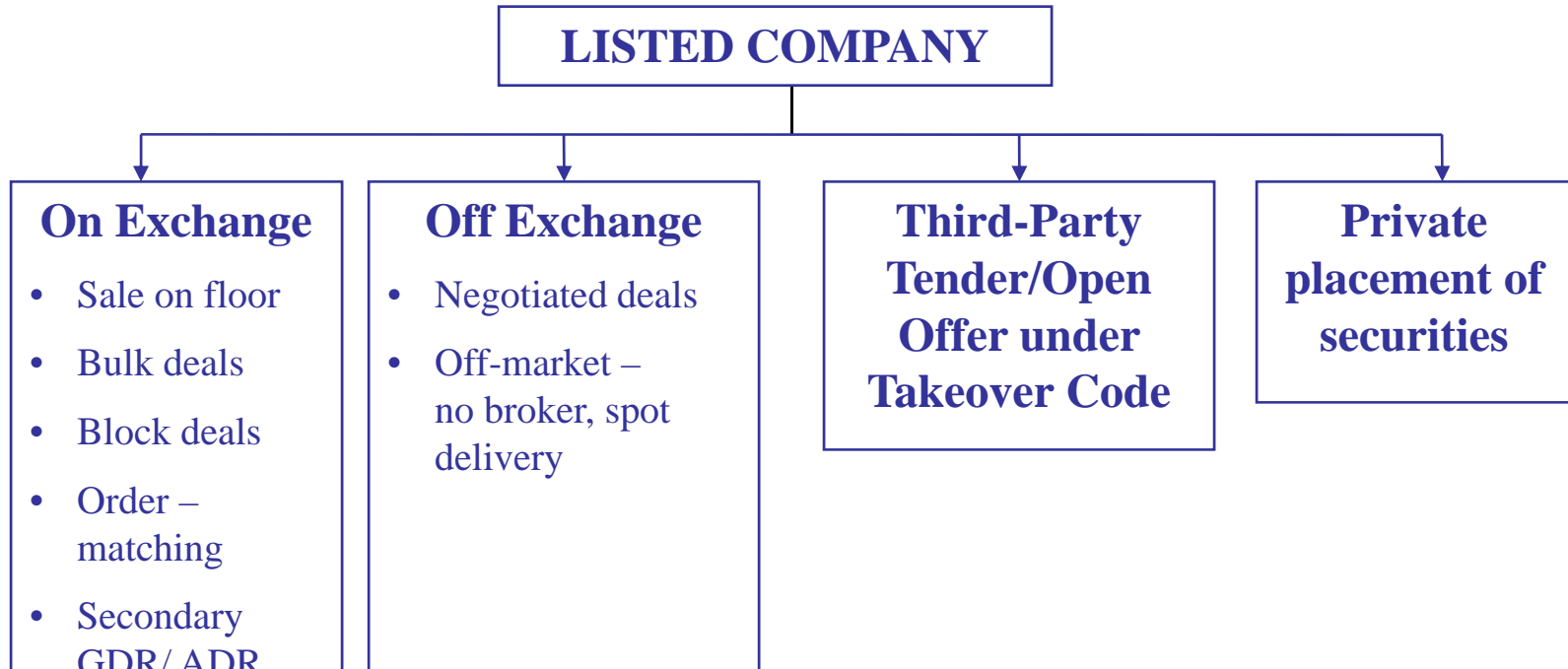


NR – Non Resident

R - Resident



# Exit Options – Listed Companies



Listed Company

- **On Exchange:** At prevailing market prices through a registered merchant banker/stock broker; or
- **Off Exchange:** Pricing formula





# Other Considerations

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# Insider Trading Regulations

- Prohibits “dealing in securities” by “insiders” based on “unpublished price sensitive information”
- No counseling or procuring any other person to deal in securities when in possession of such information
- No company to deal in the securities of another company or its associate while in possession of any unpublished price sensitive information
- Publicly available information under the Listing Agreement may not be adequate to base an investment decision



# Insider Trading Regulations - Defenses

- One option would be to make the relevant price sensitive information available to the public. This may however drive up the price of the share
- Due Diligence of Listed Companies – subject to SEBI (Prohibition of Insider Trading) Regulations
- Safe-Harbor under Regulation 3B(2) (“open offer”)
- “Chinese Walls” for financial intermediaries
- Changes on the horizon



# Competition Law – Existing Regime

- Currently governed by the combination of the MRTP Act and certain provisions (S. 108 A and 108 G) of the Companies Act, 1956
- MRTP Act, regulates restrictive and unfair trade practices – follows a “Filing Based” approach with certain agreements to be filed with MRTP Commission
- Illegality is based on possible impact on competition rather than actual impact
- Merger control is enforced under Sections 108 A to 108 G of the Companies Act, 1956



# Competition Law – Existing Regime

- Requires all acquirer of 10% or more of a public company that results in a consolidated market share of more than 25% (“dominant undertaking”) to obtain central government approval
- The MRTP Act is proposed to be replaced by a comprehensive enactment the Competition Act 2002
  - Amended in 2007 but, yet to come into force
  - Controversies surrounding the amendments in 2007 e.g. waiting period of 210 days



# Competition Act, 2002

- Modeled along the EU Competition Law and is expected to come into force latest by July 2008
- 3 substantive parts:
  - Anti- competitive agreements
  - Abuse of Dominance
  - Combinations
- Illegality based on the impact (“appreciable adverse effect”) on competition in the “relevant market” (product and geographical)
- No filing requirements pre or post, except for combinations beyond certain threshold (merger control)



# Competition Act, 2002

- Committee that has framed the law has recommended that, regulation of combinations should come into force 2 years after the other 2 parts (to give Indian industry time to consolidate)
- Penalties severe (in some cases 10% of the turnover) though financial, criminal penalties only for failure to comply with directions of the Competition Commission
- Appeal to the Competition Appellate Tribunal and then to the Supreme Court



# Corporate Governance

- India ranks 3rd in Asia (excluding Japan!) in the corporate governance scorecard\*
- Patterned on Cadbury Report, parts of Sarbanes Oxley Act with suitable Indian adaptations
- Norms introduced by amendments to the Companies Act, 1956 and Listing Agreement
- SEBI introduced clause 49 of the listing agreements with the stock exchanges mandating Indian companies to adhere to higher governance standards
  - Independent Directors and Board composition
  - Small shareholder directors
  - Audit Committees
  - Disclosures
  - Internal Standards





# QUESTIONS

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