India's New Cross Border Merger Regime

As Indian companies can now merge with an overseas company, **CS Amitava Banerjee** reviews the pros and cons

Indian firms have gained significant attention over the past decade due to their overseas acquisitions. They were primarily aimed at establishing new international consumer bases; gain access to new technology and intellectual property. Hence, outbound acquisitions are a matter of significant importance for the corporate sector and the economy as well. However, it is the legal environment governing such acquisitions which determine their number, structure and the success or failure of such transactions.

Under the previous Companies, Act, 1956 (sections 391-394) it was only possible for a foreign company to merge with an Indian company. However, the reverse was not allowed. This was primarily done with the intention to ensure that the company that continues after the merger is an Indian company and can be subject to the Indian regulatory regime.

However, section 234 of the Companies, Act 2013 (2013 Act) allowed cross-border mergers both ways, subject to the fulfilment of certain conditions. Yet after almost three years of the 2013 Act coming into force, such an important enabling provision was made effective only from April 13, 2017. This paper delves into key issues which have been dealt with by the lawmaker's and those which need further clarity.

The MCA notification on April 13, 2017 has brought into effect, section 234 of the 2013 Act. Indian companies can now merge with an overseas company through a scheme sanctioned by the National Company Law Tribunal ("NCLT") in accordance with Chapter XV of the Act and the amended Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 ("Companies Rules 2016"). Further as such mergers will also be subject to the approval of the Reserve Bank of India ("RBI"), it has also come up with Foreign Exchange Management (Cross border Merger) Regulations, 2017 ("RBI Draft Regulations").

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However, before actual plans are executed for such cross-border transactions, there are some important issues that needs to be considered. They are summarised as follows:

The dilemma of notified jurisdictions

The primary reason for the delayed implementation of such an important enabling provision was the dilemma with identifying "notified jurisdictions". In a way demarcating certain territories to be destinations for mergers is in a way a restriction, however the lawmakers found substance in it as it was meant to prevent some unfavourable transactions impacting the Indian economy. There were apprehensions in the industry that the basis on which the "notified jurisdictions" will be specified were meant to exclude tax havens.

However, the Ministry of Corporate Affairs ("MCA"), notification on 13th April 2017 which brought in the Companies (Compromises, Arrangements and Amalgamations) Amendment Rules, 2017, has finally put to rest the speculations on what will be the notified jurisdictions. The Rules have now defined 'notified jurisdictions' for outbound mergers to mean the following:

(i) Jurisdictions whose securities regulator is a member of IOSCO (appendix A, signatories) or has a bilateral memorandum of understanding with SEBI,

(ii) Those whose central bank is a member of the Bank for International Settlements (BIS), and

(iii) Those who have not been identified in the public statement of the Financial Action Task Force (FATF) about to not having Anti-Money Laundering/Combating the Financing of Terrorism deficiencies or those that have made sufficient progress in addressing such deficiencies or those who made a commitment to FATF's action plan to address such deficiencies.

On a closer look, it can be found that the present signatories to Appendix A, of IOSCO's Multilateral Memorandum of Understanding include Bermuda, British Virgin Islands, Cayman Islands, Isle of Man and Mauritius among others, which are established tax havens. Further, SEBI has executed MOUs with securities regulator of Dubai, Singapore and Mauritius which are on the favoured route of investing into Indian entities.

On the other hand, the Draft Regulations by RBI requires the 'foreign company' to be incorporated in the aforesaid jurisdictions, but extends such territorial restrictions to both inbound and outbound mergers, by the explanation to regulation 2(v). This is because the same definition of 'foreign company' is used in case of both regulations 4 and 5 dealing with inbound and outbound mergers respectively. This is not in consonance with the intent of MCA under the Companies Rule, 2016 as the criteria of notified jurisdictions applies only for outbound mergers.

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Norms for valuation

Rule 25A, of Companies Rules 2016 provides that in case of an outbound merger by an Indian company, the transferee company shall ensure that valuation is conducted by values who are members of a recognised professional body in the jurisdiction of the transferee company and such valuation should be in accordance with internationally accepted principles on accounting.

The Draft Regulations, further clarifies that the valuation of the Indian company and the foreign company for cross border merger should be done as per internationally accepted pricing methodology for valuation of shares on arm's length basis which should be duly certified by a chartered accountant/ public accountant/merchant banker authorised to do so in either jurisdiction.

Applicability to demergers

Rule 25A of Companies Rules 2016, refers only to a merger. However, regulation 2 (iv) of the RBI Draft Regulations defines a 'cross border merger' to include any merger, demerger, amalgamation or arrangement between Indian

company (is) and foreign company(is) in accordance with the Companies Rules 2016. An issue that needs clarity is whether the RBI perspective of including demerger in the ambit of permissible cross border transactions is tenable, when the main Companies Rule 2016 on which the even the RBI guidelines depend, only talks specifically of merger.

Making an application with NCLT

Application for sanctioning a scheme of amalgamation is filed with the NCLT within whose jurisdiction; the registered office of the applicant is situated. In case of a merger between a foreign company and an Indian company, an issue may arise as to whether the foreign company can be mandated to file an application before the NCLT.

Under the Companies Act, 1956, in case of a merger of a foreign company (i.e. a transferor company) with an Indian company (i.e. a transferee company), there have been instances when the High Courts sanctioned the scheme on a petition filed only by the Indian company. In Re Moschip Semiconductor Technology Limited, (2004)120 CompCas 108, the Andhra Pradesh High Court held that " inasmuch as the transferee company is a company incorporated in accordance with the provisions of the Act with its registered office within the territorial jurisdiction of this Court and the transferor company, on the other hand, is a foreign company which comes within the definition of "body corporate" as can be seen from Section 2 (7) of the Act and under Sub-section (4) of Section 394 of the Act the transferor company can be a body corporate, there can be a valid scheme of arrangement for amalgamation in between them. Therefore, there is no legal bar for according the necessary sanction". Similarly, in Essar Shipping Ports and Logistics Ltd., In re [2009] 149 CompCas 417 (Guj) the Gujarat High court approved a similar Scheme of Amalgamation wherein the Transferor Company was incorporated in Mauritius without requiring it to file an application in India.

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Therefore, it may be argued that the petition seeking the necessary sanction of NCLT may be required to be filed only by the Indian company.

Applicability to LLPs

The definition of "Foreign Company" for cross border mergers, means any company or body corporate incorporated outside India whether having a place of business in India or not. Whereas the definition of "Indian Company" includes a Company incorporated under the 2013 Act or under any previous Company Law.

This means that the definition of foreign company includes Limited Liability Partnership (LLP) as well, as section 2 (d) of the LLP Act, 2008 clearly states that a body corporate includes a LLP registered under that act or incorporated outside India.

Hence, it seems that the intent of the legislators is to extend the ambit of cross border mergers to only those LLPs incorporated outside India and not to those incorporated in India. There seems to be some parity issues when it comes to treating the LLPs and needs some clarification on whether Indian LLPs can also benefit from this merger regime.

Benefit of fast track process

MNC's with wholly-owned subsidiaries in India can now benefit by making an exit from India by way of merger of their subsidiary with its parent entity without following lengthy process of liquidation. However, neither section 234 of the 2013 Act nor rule 25A of the Companies Rule, 2016, dealing with cross border merger have any reference to fast track mergers. It therefore appears that the benefit of fast track process would not be available in case of cross border merger.

Conclusion

The notification is a welcome move and a step forward towards Ease of Doing Business in India; however, the new merger regime will also require changes in existing rules and regulations of Income Tax laws and Employment / labour laws as mergers entail transfer of employees too in certain cases. Further when the RBI notifies the Regulations the issues of inconsistency will also need to be addressed. In certain sectors, a prior approval from the sectoral regulator will also be required (for e.g. Insurance Regulatory and Development Authority (IRDA) or Telecom Regulatory Authority of India (TRAI)) for undertaking a cross-border merger. Such regulators also need to formulate their own action plan and notify their regulations to facilitate such sector specific mergers. Altogether, it can be said that the process has begun but ultimate framework for cross border merger need to evolve to deliver the anticipated benefits to the commercial world. ■

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