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"Striking A Balance: Regulatory Compliance And Corporate Governance In Cross-Border Mergers"

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Abstract

The rise in cross-border mergers and acquisitions (M&A) has significantly altered the global economic environment, with serious consequences for India's economy. This research study looks on the legal elements of cross-border M&A transactions and their impact on the Indian economy.

The essential legal elements of cross-border M&A transactions are discussed, including regulatory approvals, competition law compliance, intellectual property rights, and tax implications. The paper investigates the difficulties and complexity of navigating numerous legal systems across jurisdictions, highlighting the importance of extensive due diligence and strategic preparation.

Furthermore, the study paper examines the influence of cross-border mergers and acquisitions on the Indian economy. It balances the potential benefits, such as access to new markets, technology transfer, and greater competitiveness, against the challenges, which include regulatory scrutiny, cultural integration, and post-merger integration concerns. Case studies and statistics are utilised to show the real-world effects of cross-border mergers and acquisitions on the Indian economy. The article examines significant mergers and acquisitions involving Indian firms, concentrating on the results and lessons learned.

Introduction

- In developed economies, mergers and acquisitions have been popular for a long time, but in India, mergers and acquisitions have recovered after the Indian government launched the liberalization policy in 1991. Thus, in 2013 passed a more modern, simplified, and nationalized legislative company law to align our company law with global best practices. The New Law of 2013 introduced pragmatic reforms for mergers and acquisitions, which made the process easier, faster, and cleaner.

- Cross-border mergers and acquisitions are deals involving two or more firms from separate countries; they are also known as offshore merger-related acquisitions. In a cross-border purchase, control of assets and activities is transferred from a domestic to a foreign firm, with the former becoming an affiliate of the latter. Cross-border M&A has been supported by technological advancements, low-cost financing arrangements, and strong market conditions, which have given dealmakers more confidence and creativity in their expansion strategy.

- The Companies Act of 1956 confined cross-border mergers to inbound mergers resulting in an Indian firm. However, the recently amended Companies Act of 2013 expanded the scope of cross-border mergers to include outbound mergers as well. As a result, the Companies (Compromise, Arrangement, and Amalgamation) Rules, 2016 were created to make it easier to file inward and outbound mergers and other arrangements with the NCLT.

- To address particular difficulties of cross-border mergers, the RBI enacted the Foreign Exchange Management (Cross Border Merger) Regulations, 2018 (CMR). The regulations were developed to align the scope of cross-border mergers with India's exchange control legislation. According to Section 234 of the Act, Transferee firms can only be foreign firms from specified countries that the Indian government has notified.

- Definitions:
  Mergers: A merger occurs when two or more firms combine their assets and liabilities through amalgamation, absorption, or creation of a new organisation.
  Types of Mergers:
  i. Horizontal mergers include merging firms with comparable products and services to expand their offerings. For example, Meta or Facebook purchasing Instagram and WhatsApp. This form of merger and acquisition is used to reduce market competition and tilt the market in favour of monopolies.
  ii. Vertical mergers occur when organisations or businesses in the same industry merge at various levels of production and supply chain. It occurs when one company purchases or sells any product or service from or to another firm. A well-known example of this merger is the combination of Pixar and Disney.
  iii. Conglomerate Mergers: This sort of merger involves two corporations or enterprises that do not have any common business sectors and belong to distinct industries. The major goal of a conglomerate merger and acquisition is to diversify their product and service offerings while also expanding their market size. For example, a watch manufacturer may acquire a cement producing firm.
  iv. Concentric mergers occur when two firms offer distinct products or services yet share a consumer base. For example, when a UPS manufacturer and a computer system manufacturer collaborate to create any combination. They are also known as "congeneric mergers and acquisitions."

  Acquisitions: Acquisitions occur when a corporation buys out the ownership of another company (target company). Acquisition, sometimes known as takeover, is carried out with the goal of achieving market dominance.

Nature of Acquisitions:

Acquisitions or takeover may be friendly or hostile.

- In a friendly acquisition or takeover, the acquiring business assumes ownership of the target company's management with board consent.
- In hostile acquisitions or takeovers, the acquiring corporation takes control of the target business's management without board permission.

❖ Difference between mergers and acquisition:

- A merger occurs when two separate companies or businesses combine to establish a new company or business in which both parties have equal control. The scale of these businesses is often comparable. Acquisition, on the other hand, refers to the circumstance in which a purchasing firm purchases another company. Typically, larger corporations acquire smaller corporations.
- The merging of two firms results in the establishment of a new company, while the old companies are dissolved. In contrast, an acquisition does not result in the establishment of a new business; the acquiring firm and the target company remain different organisations, with the purchasing company relinquishing control of the latter.
- Mergers entail at least two firms pooling their assets and liabilities and transforming them into a new company. However, this is not the case in acquisitions. In an acquisition, only the acquiring corporation assumes control of the business's management.

Regulatory Framework of Cross-Border Mergers in India

Laws governing Cross-Border M&A Transactions in India:

1) Laws Applicable for Listed Companies:
    - Indian Contract Act,1872
    - Securities and Exchange Boad of India Act, 1992 (SEBI)
    - SEBI Regulations, 2009 (Issue of Capital and Disclosure Requirements)
    - SEBI (Securities Acquisition of Shares and Takeovers) Regulations, 2011
    - SEBI Regulations, 2015 (Listing Obligations and Disclosure Requirements)
2) Laws Applicable for Foreign Companies or non-resident companies:
    - Foreign Exchange Management Act, 1999 and all the relevant rules made under this act.
    - Government of India's policy of Foreign Investment
3) Laws Applicable in case the acquisition is done through debt:
    - Transfer of Property Act, 1882
    - Securitisation and Reconstruction of Financial Assets and Enforcement of Security Act, 2002 (SARFESI Act)
    - Recovery of Debts due to Banks and Financial Institutions Act,1993
    - Companies Act, 1956
    - Companies Act, 2013
    - Income Tax Act, 1961

Parties Involved in Cross-Border Transactions

Cross-border mergers and acquisitions in India include a diverse group of parties, all of whom contribute to the transaction's success and execution. While investments in India, including FDI and local investments, provide the basis for M&A activity, investments from India in other countries enable Indian firms to expand internationally and capitalise on new possibilities.

Furthermore, foreign venture capital investors, portfolio investors, NBFCs, and corporations that subscribe to NCDs all play important roles in providing financing, finance, and financial help to acquiring companies.

Their participation boosts capital market liquidity, promotes innovation, and facilitates company expansion. The parties that are engaged in the process of cross-border mergers and acquisitions are listed below:

1) Investment in India: Domestic as well as foreign direct investments (FDI) are included while considering overall investments in India. Domestic investments are capital inflows from within India, which include Indian businesses, individuals, and institutional investors. These investments have a significant influence on the M&A landscape, particularly domestic mergers and acquisitions in which Indian businesses consolidate market positions, diversify portfolios, or expand into new markets.
   Examples:
   Tata Motors, an Indian multinational automobile manufacturing firm, acquired Jaguar Land Rover, a well-known British luxury car manufacturer, in 2008. Tata Group's acquisition constituted a substantial local investment, helping it to improve its position in the worldwide automobile industry.
   Adani Group Acquires Airports the Adani Group, an Indian multinational firm, has made large domestic investments in the aviation sector by acquiring various airports around India. This strategic choice aimed to improve the Group's infrastructure portfolio while also contributing to India's aviation sector growth.
2) Investments from India (Overseas Direct Investments): Indian firms and investors make direct investments in international markets. These investments enable Indian companies to expand their global footprint, penetrate new markets, acquire cutting-edge technology, and diversify their operations.
   Examples:
   Tech Mahindra's acquisition of Target Group, a UK-based financial services business, in 2016. This foreign purchase allowed Tech Mahindra to expand its financial services capabilities while also establishing a footprint in the European market.
   - Reliance Industries' Investments in Jio Platforms: India's largest conglomerate, Reliance Industries, has made considerable investments in Jio Platforms, a well-known digital services provider. This investment surge featured cooperation with global IT heavyweights such as Facebook and Google, highlighting India's outward digital investments.
3) Other significant participants in mergers and acquisitions include organisations with different roles and affects, as well as direct stockholders. These stakeholders include overseas venture capitalists.
   a) Venture Capitalists: Foreign investors provide crucial early-stage funding for innovative and fast-growing companies. Their investments typically expedite a company's development and expansion, helping it to scale operations, develop new products, and penetrate new markets.
      For example, Sequoia Capital invested in Byju's: Sequoia Capital, a leading worldwide venture capital company, has made significant investments in Byju's, an Indian educational technology business. This flood of international venture capital was key to Byju's rapid growth and emergence as India's leading edtech unicorn.
   b) Foreign Institutional Investors FPIs, or, include pension funds, sovereign wealth funds, and asset management organisations that invest in Indian markets. These investors provide significant capital inflows, benefiting Indian investors by enhancing market liquidity, capital formation, and portfolio diversification.
      For example: BlackRock invests in Indian equities:
      BlackRock, one of the world's largest asset managers, has made considerable investments in Indian stocks through the FPI method. These investments have had a huge influence on India's capital markets, driving up valuations and strengthening investor confidence.
   c) Non-Bank Financial Companies (NBFCs) provide banking services without a licence. They play a crucial role in financing mergers and acquisitions by offering purchasing companies with other sources of funding, such as loans.
      For example, take L&T Finance Holdings' funding of infrastructure projects.
      L&T Finance Holdings, an Indian NBFC, has played a significant role in funding infrastructure projects and acquisitions in India. Their financial help has allowed infrastructure companies to accomplish large-scale projects, contributing to India's economic progress.

d) d. Debt funds and mutual funds typically invest in Non-Convertible Debentures (NCDs) issued by Indian firms. These investments offer a steady stream of loan financing to support mergers and acquisitions, with attractive returns for investors.
For example, Franklin Templeton, a worldwide investment management business, invested in Non-Convertible Debentures (NCDs) issued by Indian firms during mergers and acquisitions. These investments help firms fund their expansion plans and strategic acquisitions.

Procedure of Cross-Border M&A in India

- According to the Companies Act of 2013, cross-border mergers and acquisitions occur when two or more companies from different countries merge or acquire each other to enter a new market or expand their business. However, the phrase merger is distinct from acquisition. The phrase merger refers to a circumstance in which two or more companies unite to form a single business. Acquisition, on the other hand, occurs when one firm acquires a percentage ownership in another company that is located in a different nation.
- Cross-border M&A activity has recently increased dramatically, with larger and more frequent transactions. These mergers, which may include acquisitions or amalgamations, bring together Indian and international corporations under the corporations (CA&A) Rules, 2016. The Companies Act of 2013 provided this framework, which fuels Indian enterprises' global expansion.
- To strengthen India's presence on the global commercial stage, a strong legislative environment for cross-border mergers is required. This is exactly why Section 234 was enacted. Cross-border mergers are necessary to drive economic growth and efficiency improvements (economies of scale). Section 234, enacted by the Ministry of Corporate Affairs, establishes the legal framework for such mergers in India. Cross-border mergers became a reality after they were implemented in April 2017.
- Section 234 of the Companies Act of 2013 governs the merger or amalgamation of a company with a foreign corporation.
  - The provisions of this Chapter apply to combinations and mergers between companies registered under this Act and companies established in the jurisdictions notified by the Central Government, unless otherwise specified by other laws. The Central Government may, in consultation with the Reserve Bank of India, enact mergers and acquisitions regulations.
  - With prior authorization from the Reserve Bank of India, a foreign firm may merge with a company created under this act, subject to any other applicable laws. Provided that the merging businesses give information on how shareholders got or will receive their payments, which may be in cash, depository receipts, or a mix of both.
- Explanation: In sub-section (2), a "foreign company" is defined as any corporation or body corporate formed outside India, regardless of its presence in India.

- Section 234 of the Companies Act of 2013, revised in December 2017, contains provisions for both inbound and outbound mergers. It enables the Central Government, in collaboration with the RBI, to develop cross-border merger legislation. In line with this, the Foreign Exchange Management (Cross Border Merger) Regulations, 2018 (Merger Regulations 2018) have been published and will go into effect on March 20, 2018, as described in Annexure A.
- Mergers that comply with the Merger Regulations are believed to be automatically authorised by the RBI and do not require further approval. The Merger Regulations include a comprehensive set of rules governing cross-border mergers.
- Cross-border mergers are defined in the Merger Regulations as any merger, arrangement, or amalgamation that complies with the Companies (Compromises, Arrangements, and Amalgamations) Rules 2016 ("Companies Amalgamation Rules"), which were notified under the Companies Act of 2013.
- According to the Merger Regulations, a foreign firm is one that is not formed in India. Similarly, an Indian company is one that is incorporated in India. Outbound investment is only permitted for firms formed in the countries mentioned in Annexure B of the firms Amalgamation Rules. The 'Resultant

Company' is the company that acquires the assets and liabilities of the cross-border merger partners. A Resultant Company might be either Indian or international.

Determining Jurisdiction as per Indian Laws:

According to Rule 25A of the Companies Amalgamation Rules, a foreign corporation can combine or amalgamate with a firm, and vice versa.

(1) To merge with an Indian business, a foreign company founded outside India must obtain prior authorization from the Reserve Bank of India and follow the Companies Act, 2013 (sections 230-232) and related guidelines.
(2) This sub-section states the following:
  (a) A firm can combine with a foreign company from any of the jurisdictions indicated in Annexure B with previous Reserve Bank of India authorization and compliance with sections 230 to 232 of the Act and these regulations.
  (b) The transferee company must guarantee that the valuation is performed by valuers who are members of a recognised professional body in the transferee company's jurisdiction and follows globally accepted accounting and valuation standards. A declaration to this effect must be included to the application submitted to the Reserve Bank of India for approval under clause (a) of this subrule.

(3) The corporation must submit an application to the Tribunal in accordance with sections 230 to 232 of the Act and these rules, after acquiring the necessary permissions under sub-rules (1) and (2).

Explanation 1: For the purposes of this regulation, the word "company" means a company as defined in clause (20) of section 2 of the Act, and the term "foreign company" means a company or body corporate constituted outside India, regardless of whether it has a place of business in India.

Explanation 2: It is stressed that no changes to this regulation will be made without the approval of the Reserve Bank of India.

The Companies Amalgamation Rules, 2016:

Under Rule 25A of the Companies Amalgamation Rules, a foreign firm is defined as one founded outside of India. Foreign firms may merge with Indian companies under the firms Amalgamation Rules, with prior approval from the Reserve Bank of India and adherence to sections 230-232 of the Act and Rules. The Companies Amalgamation Rules, 2016 further require that the valuation be completed by valuers who are members of a recognised professional group and adhere to internationally accepted criteria.

Furthermore, the following requirements must be completed before merging with or acquiring any foreign company:

- Mergers between Indian corporations are only permitted with multinational companies based in certain countries.
- The foreign firm is responsible for ensuring that valuations are conducted by a member of a reputable professional body in their country and adhere to internationally accepted accounting and valuation procedures.

The jurisdictions named in clause (a) of sub-rule (2) of rule 25A [Annexure-B] are:

a) Securities market regulators who have signed the International Organisation of Securities Commission's Multilateral Memorandum of Understanding (Appendix A Signatories) or a bilateral Memorandum of Understanding with SEBI.
b) Countries having central banks that belong to the Bank of International Settlements (BIS).
c) A jurisdiction not identified in the Financial Action Task Force (FATF) public statement as:
   - having strategic Anti-Money Laundering or Combating the Financing of Terrorism deficiencies requiring countermeasures, or
   - a jurisdiction that has not made sufficient progress or committed to an action plan to address these deficiencies.

Concept of Inbound and Outbound Mergers as per Indian Legal Framework

In Section 234 of the Companies Act of 2013 the idea of inbound and outbound mergers was introduced through an amendment.

Inbound Merger.

An inbound merger occurs when a foreign firm merges with an Indian company, creating an Indian corporation. The following are the essential regulations that must be observed during an incoming merger.

- Transfer of Securities: Typically, the cross-border merger resultant company may transfer any security, including a foreign security, to a person resident outside India in accordance with the provisions of the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations of 2017. However, if the foreign firm is a joint venture or totally owned subsidiary of an Indian company, it must comply with the rules of the Foreign Exchange Management (ODI Regulations) Regulations, 2004 (ODI Regulations).
- Branch/Office Outside India According to the Foreign Exchange Management (Foreign Currency Accounts by a Person Resident in India) Regulations, 2015, a foreign company's office/branch outside India is considered the resultant company's office outside India. In the event of a securities transfer, both the buyer and the target can use the services of a Tripartite, whose role it is to have securities in the books and to do all back-office procedures (including securities valuation).
- Borrowings: The transferor company's borrowings would become those of the resultant company. The Merger Regulations provide for a two-year period to comply with the External Commercial Borrowings (ECB) regime. The end-use limitations do not apply here. Hedging of External Commercial Borrowings (ECB) is also required for cross-border mergers. External Commercial Borrowings (ECB) are arrangements between an Indian buyer and a foreign bank in which the foreign bank funds an Indian corporate through a foreign currency loan with a defined amount and term. FEMA allows hedging of loans received from outside banks in Indian books.
- Transfer of Assets: Assets acquired by the resulting business may be transferred in compliance with the Companies Act of 2013 or any regulations enacted under it. If an asset is not permitted to be bought, it must be sold within two years after the National Company Law Tribunal (NCLT)'s sanction. The earnings of such a transaction shall be returned to India. Opening of overseas bank accounts for the resultant company the resultant firm may open a bank account in foreign currency in the overseas jurisdiction for a maximum of two years in order to conduct cross-border merger-related operations.
- Bank Account: the resulting business is permitted to open up a bank account in the foreign jurisdiction for a period of 2 years and not more than that. During this period the resultant business may carry out the transactions related to cross-border mergers and acquisitions.

Outbound Mergers

An outbound merger occurs when an Indian firm merges with a foreign company to form a new overseas company. The following are the primary rules that govern an outbound merger:

Issue of Securities: Securities issued by a foreign corporation to an Indian entity can be issued to both Indian and non-Indian residents. The acquisition of securities supplied to persons resident in India must comply with the ODI regulations. Securities in the resulting firm may be acquired if their fair market value is within the limits set by the Liberalised Remittance Scheme.

Branch Office: An Indian company's office in India may be classified as the resultant company's branch office in India under the Foreign Exchange Management (Establishment in India of a branch office, liaison office, project office, or any other place of business) Regulations, 2016.

Bank Account: The resultant foreign business can now register a special non-resident rupee account under the FEMA (Deposit) Regulation, 2016 for a maximum of two years to assist outbound mergers and acquisitions activities.

Other modifications.

a) The resulting company's borrowings should be repaid according to the approved programme.
b) The resultant company must sell assets that cannot be purchased or held within two years of the scheme's authorization date.
c) The foreign business can open a Special Non-Resident Rupee Account under the FEMA (Deposit) Regulations, 2016 for two years to aid the outbound merger.

Navigating the regulatory landscape is critical in outbound mergers and acquisitions (M&A), which occur when an Indian firm (the Resident firm or RC) purchases a foreign entity. Compliance with the Foreign Exchange Management Act (FEMA), the Companies Act of 2013, and other relevant legislation is vital for ensuring a seamless and lawful merger process.

Conclusion

Synthesis of the Paper:

- The current regulatory environment, while changing, can be complex and time-consuming for cross-border M&A transactions. Streamlining procedures and establishing clearer standards will considerably increase India's appeal to foreign investors.
- Competition, intellectual property rights, and dispute resolution issues must be carefully considered during cross-border mergers and acquisitions to ensure fair competition, innovation protection, and efficient conflict resolution.
- Cross-border mergers and acquisitions can bring considerable economic benefits to India, such as job creation, access to innovative technologies, and increased market competitiveness. However, potential negative consequences such as job displacement in specific industries and foreign company dominance demand a balanced response.
- It is critical to strengthen the legal environment to protect Indian enterprises' and stakeholders' interests during cross-border mergers and acquisitions. This may include guaranteeing transparency, creating an equal playing field, and limiting any risks linked with intellectual property and capital flight.

Suggestions: For a cross-border transaction to be effective and sustainable, leaders must plan carefully, do thorough due diligence, and execute meticulously before and after the transaction. The following are some of the factors that executives and transaction participants should consider during a cross-border merger and acquisition:

- Make sure the transaction research and objectives guide throughout the process of M&A.
- To prevent global challenges, adapt the negotiation technique and playbook as needed.
- Preventing handoff errors by combining pre-deal due diligence with pre-close preparation activities.
- The agreement arrangement should be such that it meets the essential objectives.
- Mention the whole integration scope, method, and plan for achieving both the start and end-state goals openly.
- Create a global integration programme that includes representatives from both the target and the acquirer for key work streams, regions, and nations.
- Pay particular attention to detail-oriented pre- and post-close integration planning, with dependencies and critical paths clearly described.

Recommendations For Future:

- Digitalization of the legal framework: Streamlining approval processes, establishing clearer competition and intellectual property laws, and promoting compliance with international standards can all help to attract more foreign investment.
- Capacity building: Providing regulatory bodies and legal professionals with experience handling complicated cross-border transactions can help ensure that deals are executed efficiently and transparently.
- Promoting transparency and predictability: Clear and predictable regulations will boost international investor trust and encourage them to engage in the Indian mergers and acquisitions market.
- Fostering innovation: The legal environment should facilitate cross-border mergers and acquisitions that promote innovation and technology transfer for long-term economic growth.