Golden Research Thoughts
Volume 2, Issue. 7, Jan. 2013
ISSN:-2231-5063
Available online at www.aygrt.net

ORIGINAL ARTICLE

LEGAL AND ACCOUNTING ASPECTS OF M&AS

EKTA ARORA

Sr. Assistant Professor, HCTM (Haryana College of Technology & Mangement)Tech Campus, Kaithal, Haryana, India

Abstract:

Many organizations regard mergers & acquisitions as a strategic tool for increasing profitability, gaining market share and developing synergies. From banking to software , insurance to technology, companies have started entering into mergers & acquisitions to become market leaders in their respective industries. This paper discusses about the legal and accounting aspects of mergers and acquisitions. Many mergers fail because of lack of accounting information and knowledge.

INTRODUCTION ABOUT MERGERS & ACQUISITIONS:

Merger:

Merger is an arrangement whereby the assets of two or more companies become vested in or under the control of one company, which may or may not be one of the original companies merged in, which will have, as its shareholders, all or more than 90% of all the shareholders of all the original companies. Mergers in India are dealt by companies Act, 1956 (sections 390 – 390A) and to accounting part by Accounting Standard (AS) – 14.

Example of merger is a deal between Bank of Punjab and Centurion Bank and the outcome business unit is Centurian Bank of Punjab.

Acquisitions:

Acquisition simply means buying the ownership in a tangible or intangible asset. In the context of business combinations and acquisition is the purchase by one company, of controlling interest in the share capital or in the voting rights of an existing company. In India acquisitions are previewed under SEBI Takeover code – 1997, which is originated by Justice P.N. Bhagwati Committee report on Takeovers. Example is the acquisition of Associated Cements share by Holdcem.

REASONS FOR MERGERS & ACQUISITIONS:

Companies can produce goods or services more efficiently if they combine their efforts and facilities .
Collaborating or sharing expertise may achieve gains in efficiency.
Underutilized assets of the company can be used in better way.
Change in management may make the company more profitable.

Legal and Accounting aspects of M&As:

Title : LEGAL AND ACCOUNTING ASPECTS OF M&AS
Source:Golden Research Thoughts [2231-5063] EKTA ARORA yr:2013 vol:2 iss:7.

Mergers and acquisitions are strategic decisions leading to the optimization of a company's growth opportunities mergers and acquisitions aim at achieving optimum utilization of all available resources, exploitation of unutilized and under utilized assets and resources including human resources, winning over competitive forces, achieving synergies, achieving economies of scale, forming a formidable human resources base, installing an integrated research platform, capitalizing complementing opportunities, remove sickness, achieving savings in administrative costs, reducing tax burden and ultimately maximizing the interest of stakeholders.

However, sometimes it is concluded that M&As limit or restricts competition from the consumer's point of view. Further mergers and acquisitions are defined separately and with different meaning in different countries. Not only these different terms are used for mergers and acquisitions e.g. in India Amalgamation term is used for mergers and takeovers term is used for acquisitions. In India, there are different accounting procedures separately for amalgamations and takeovers. And there are different regulatory bodies to deal those type of cases.

Legal and regulatory framework for amalgamations and takeover is as follows:

1. for amalgamation:
-COMPANIES ACT, 1956 (Section 390-396A).
-Accounting standard – 14.

2.for Takeovers:
-SEBI TAKEOVERS CODE – 1997.

3.Other regulations:
-SICA, 1985 (Sections 15-18)
-INCOME TAX ACT, 1961 (Section 2 (1B), 43, 45, 47 and 72A).
-MRTP ACT, 1969 Sections 27 and 27A.
-INDUSTRIES (DEVT. & REGULATION) ACT, 1951.
-STAMP LAWS
-SALES AND LAWS
-FOREIGN EXCHANGE MANAGEMENT ACT.
Accounting Standard-14

Accounting standard – 14 is for amalgamation, which came into effect on 1 April, 1995 and is mandatory in nature. The standard deals with accounting for amalgamations with two methods (The Pooling of Interest Method, Purchase Methods) and the treatment of resultant goodwill or reserves, to safeguard the interest of public.

The standard doesn't deal with the case of acquisitions but the cases of amalgamation in the nature of merger which need to satisfy all the following conditions:

i.All the assets and liabilities of the transferor company become, after amalgamation, the assets and liabilities of the transferee company.
ii.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 therein, immediately before the amalgamation, by the transferee company or its subsidiaries or this nominees) become equity shareholders of the transferee company by virtue of the amalgamation.
iii.The consideration for the amalgamation receivable by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company is discharged by 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.
iv.The business of the transferor company is intended to be carried on, after the amalgamation by the transferee company.
v.No adjustment is intended 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.
For the purpose of Income-Tax Act, 1961, Section 2 (1B) defines Amalgamation, and stipulates three conditions:
a)and b) All the property and liabilities of amalgamating Companies should vest with the amalgamated company.

b)The shareholders holding not less than 90% in value or voting power in the amalgamating company (other than shares held by the amalgamated company or its subsidiaries) should become the shareholder of the amalgamated company. The definition given in the Income Tax Act is for the purpose of that Act only.
Transfer of Assets to the transferee company present to a scheme of amalgamation is not a transfer and doesn't attract capital gain tax. Section 47 (vi)

Approval of Central Govt. under HRTP Act no longer required for amalgamation cases, Decision under Hindustan Lever Employee's Union vs. Hindustan Lever Ltd, (1995) 83 Comp. Case 30 (1994) 15 CLA 318 (SC).

MRTP Act, 1969 Sec. 27 & 27A

Amalgamation is not defined in Companies Act. Chapter V Sec. 390 -396A of the Companies Act contains provisions on Compromises, Arrangements and Reconstructions

Amalgamation is an arrangement or reconstruction

For amalgamation, the transferee company need to take sanction from the court for such Arrangement with the set laid down procedure under section 390-396. In a well famous case of MIHEER MAFATLAL vs. MIL, SC (1996) 87, pp. 792-841 Company Case; SC gave broad guidelines for the Courts to sanction amalgamation schemes. Further, which became guidelines to the courts in such schemes.

Every Amalgamation, except those which involve sick industrial companies, requires sanction of High Court which has jurisdiction over the state/area where the registered office of a company is situated (section 391).

Amalgamation Through BIFR Under SICA

If transferor and transferee companies are under the jurisdiction of different High Court, separate approval is necessary.

1.Amalgamation may be measure for rehabilitation of a sick industrial company under SICA.
2.Section 18 of SICA envisages amalgamation of a sick company with any other company or vice versa i.e. reverse merger.
3.Section 18 (2) of SICA gives BIFR very wide powers which may be exercised by BIFR in regard to a scheme of amalgamation between a sick industrial company and healthy company.

Scheme of Amalgamation provides for transferor company's undertaking, property, assets and liabilities to be transferred by order of High Court to transferee company and dissolution of transferor company (Section 394 (1)) with the first petition in High Court, Court will convene meetings of different stakeholders i.e. AGM, Cr. Meeting Director's meeting etc. and with 2nd petition in the court the approval of the scheme and sanction of the court, the court will issue notice to central govt. to regional director, to ROC, the liquidator and will specify.

i)Effective date.
ii)Announcement date
iii)Approval date

AS-14 deals with merger and amalgamation. The merging company loses identity; hence consolidation of accounts is permanent and even minority shareholders become shareholders of the merged company. Considering the same, the standard on consolidated financial statement (AS21) is not applicable to accounting for amalgamations, accounting for the Investment in Associates for the purpose of consolidating financial account, this standard is also not applicable to accounting for amalgamations.
SEBI (Substantial Acquisition of shares of Takeover) Regulations, 1997.

Regulations regarding takeover were originally embodied in the terms of contract of listing between a public ltd. Company and the stock exchange. Although listing is not compulsory under the SCRA, under Section 73 of Companies Act, 1956, but/further companies desirous of listing their shares on the stock exchanges had to sign a listing agreement.

Section 21 of the Securities Contract Regulation Act, 1956 (SCRA) empowers the SEBI with respect to the listing of company's securities on any recognized stock exchange.

Initially there was no regulation governing the takeover of a company. Later on, in order to protect the interest of shareholders and the investing public at large; Clause 40A and 40B were incorporated in the listing agreement.

Before the Constitution of Securities and Exchange Board of India (SEBI), on approach paper was prepared for framing a comprehensive legislation for securities market and the approach paper also dealt with the deficiencies in the regulation governing takeover as contained in the listing agreement.

A statutory recognition had been accorded to the SEBI under the Securities And Exchange of India Act, 1992. Section 11 of the SEBI Act sets out the functions of the Board. One of the functions is 'to regulate substantial acquisition of shares and takeover of companies'.

Under section 30 of the SEBI Act, the SEBI has noticed on 20.2.1997, "(Substantial Acquisition of Shares and Takeover) Regulation, 1997".

CONCLUSION

Merger and Acquisitions success entirely depends on the people who drive the Business, their ability to Execute, Creativity, and Innovation. There are legal boundaries on mergers and acquisitions in India under Companies Act, 1956 and SEBI. Accounting Standard has also play a crucial role in determining the purchase price and its accounting treatment.

REFERENCES:

Agundu, P.C. & Karibo, Nelson O. (1999) "Risk Analysis in Corporate Mergers Decisions in Developing Economies." Journal of Financial Management and Analysis, July – Dec., 13-17.

Anand, Rajan ; Kumar Anil ; Kumar Gautam & Padhi Asutosh. (1998)" M&As in Asia. " The McKinsey Quarterly, No. 2, 64-75.

Bhat, Neha, (1997) "Corporate Mergers, Amalgamations and Takeovers", New Delhi Bharat Publishing House, 1997.

Bhide, A. (1989) "The Causes and Consequences of Hostile Takeovers", Journal of Applied Corporate Finance, Vol.2, 36-59.

Bhide, A. (1993) "Reversing Corporate Diversification, in The New Corporate Finance-Where Theory meets Practice", ed. D.H. Chew Jr., McGraw Hill.

Bornstein, Leopold A.; Subramanyam, K. R. & Wild, John J. (2001) "Financial Statement Analysis", 7th Edition, Tata Mc Hraw-Hill Irwin Publications, 2001.

Deng, Z. and B. Lev (1998) "The Valuation of Acquired R&D, Working Paper", New York University.

Dennis, D. and McConnell, J. (1986) "Corporate Mergers and Security Returns", Journal of Financial Economics, Vol.16, 143-188.

Gaughan, P.A. (1999) "Mergers, Acquisitions and Corporate Restructurings", John Wiley & Sons.

Hong, Hai, Robert S. Kaplan and Gershon Mandelker (1978) "Pooling Vs. Purchase: The Effects of Accounting for Mergers on Stock Prices", The Accounting Review, Vol.53, No.1, 31-47.

Iyer, L.V. (1999) "Practical Issues in Mergers and Acquisitions." Chartered Financial Analyst, June, 52-53.

Jain, N.S. ; Jain, P.K. & Yadav, S.S. (1999) "Profitability of Mergers – Some Selected Cases." The Management Accountant, July, 502-507.

Kaplan, S. and M.S. Weisbach (1992) "The Success of Acquisitions: The Evidence from Diverstitures", Journal of Finance, Vol.47, 107-138.

Kuehn, D.A. (1969) "Stock Market Valuation and Acquisition: An Empirical Test of One Component of Managerial Utility", Journal of Industrial Economics, Vol.17, No.2, 132-144.

Mc Carthy, George D. (1968) "Pre-mediated Mergers." Harvard Business Review, Sept.-Oct., 83-91.

Palepu, Krishna G. (1986) "Predicting Takeover Targets", Journal of Accounting and Economics, Vol.8, No.1, 3-35.

Pandey, Ajaj (2001) "Takeover Announcements Open Offer and Shareholders, Returns in Target Firms." Vikalpa, Vol. XXV, No. 3, 19-30.

Pawaskar, Vardhana (2001) "Effects of Mergers on Corporate Performance in India, Vikalpa", Vol. 26, No.1, 19-32.

Ramu Shiva, "Cross Border Mergers and Acquisitions", New Delhi : - Wheeler Publishing, 1998.

Ramu, Shiva, "Corporate Growth Through Mergers and Acquisitions", New Delhi : Response Books, 1998.

Rao, PVS Jagan Mohan, "Handbook on Mergers, Amalgamations and Takeover, Law and Practice", 1st Edition, New Delhi : Institute of Company Secretaries of India, 2001.

Verma, J.C. (1997), "Corporate Mergers, Amalgamations & Takeovers" 3rd Edition, Bharat Publishing House, 1997.

WEBSITES:

http://www.sebi.com
http://www.rbi.org.
http://www.indiainfoline.com
http://www.accountingweb.com