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Historical Background of Merger and Acquisition in Companies

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Abstract: The terms 'mergers' and 'acquisitions' are used in a generic sense. They are used to describe nearly any business combination involving new partnerships. Mergers in a legal sense require one of the companies to sacrifice its corporate life. . In this paper will be give the overview of introduction, meaning mergers and acquisitions, Historical Background of Merger and Acquisition in Companies in India and conclusion.

Keywords: *Mergers and Acquisitions, Companies.*

Introduction

Mergers and acquisitions are important phenomena both economically and spatially. Although the target of decades of research, the motivations for mergers are not entirely understood, each firm is unique, as may be its motivations, but some generalizations regarding the behaviour and effects have been found. There is a relationship with the economic cycle, larger firms acquire more often than small firms, and mergers are spatially concentrated. Relationships between mergers and measures of firms' financial performance are as yet unresolved.[1]

Meaning of Merger

Merger means the merger of assets and liabilities of any company or companies into another existing company. Thus, merger takes place when any company transfers all its assets and liabilities to any other existing company. The transferor company is absorbed into the existing company. The transferor company loses its existence and the transferee company survives. However, all the undertaking and plants of the transferor company may continue to operate independently with the absorbing or transferee company.[2]

[1] Milford B. Green, *Mergers and Acquisitions* 32(Routledge, London and New York, 1990).
[2] Dr. R.L. Nolakha, *Company Law and Practice*286(Vikash Publishing House Pvt. Ltd., Noida, 1stedn., 2015).

Although mergers vary by type, there have been many theories put forth to explain the general nature of merger activity. When undertaking a merger search, management will consider elements of the firm. Internal factors include the general character of the firm, its size in assets or employment, the ability to generate expansion or operating capital internally, the current state of its production technology, allocation of resources among various products manufactured, and the adaptability and expandability of its organizational structure.[3]

Externally generated considerations includes: the extent of competition in various product lines, present and potential size of market demand, production processes and technologies employed by competing firms, conditions in the labour and capital markets, government legislation related to the business environment, and import tariffs and other areas of public concern.[4]

Types of Merger

A merger may be classified into the following types:

Horizontal: A merger is said to be horizontal in nature when the firms involved in the merger are engaged in the same lines of business, for example, merger of two firms producing steel represent a horizontal merger. Availing the benefit of economies of scale and restructuring the competition in an industry, are the two key benefits of such mergers.[5]

Vertical: Joining of firms engaged at different stages of production of the same product or service (having buyer and seller relation) is termed as a vertical merger. This can be forward or backward in nature. Joining of a firm with the source of raw material is backward and joining of a firm in the direction of the customer to market its product is a forward merger.[6]

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[3]A.R. Beckenstein, *Merger Activity and Merger Theories: An Empirical Investigation* 105-128 (Antitrust Bulletin, Spring, 1979).
[4]*Ibid*.
[5]ParamjeetKaur, *Mergers in India*118 (Academic Foundation, New Delhi, 1[st]edn., 2012).
[6]*Ibid*.

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Concentric: Merger of firms that are related to each other either through basic technologies or production process or markets is called a concentric merger. It, thereby leads to either product extension.[7]

Reverse: Conventionally, a healthy or a profit making company absorbs a weak company. As the name indicates, in the case of a reverse merger, a healthy company gets merged into a sick or a financially weak company. This takes place mainly to take advantage of the provision of income tax act, which permits a company to carry forward its losses to set off against its future profits.[8]

Cross-border Mergers: When the firms combining their businesses belong to different countries of the world, it is called a cross-border merger. Companies from the US, UK and Japan are very active in such mergers. After economic liberalisation, Indian firms are also active participation in the cross-border mergers.[9]

Conglomerate Mergers: Conglomerate mergers are described as diversification forays into unrelated areas in order to reduce business risks. Often, conglomerate mergers occur when diversified firms engage in the production of goods in different industries among which the technology is relatively constant.[10]

Meaning of Acquisition

Acquiring of the effective working control by one working company over another, through the purchase of controlling interest in the share capital of the latter, is termed as an acquisition or a takeover. It is important to mention that acquisition does not lead to dissolution of the company whose shares are acquired. The shares may be purchased either by means of cash or in exchange of shares of the acquiring company.[11]

If the purchase is made through the open market, which is against the wishes of the incumbent group, it is called a hostile acquisition or a hostile takeover. If the response of shareholders is

[7] *Id.* at119.
[8] *Ibid.*
[9] *Ibid.*
[10] *Supra* note 1 at20.
[11] *Supra* note 5 at119.

favourable, the acquiring firm gains control and can replace the management of the target firm. These are generally disciplinary in nature because the underlying motive is often to correct the non-value maximising practices of managers of the target firms. In this case, to avoid a takeover attempt, the target firm can adopt anti-takeover technique or offer larger cash dividends to its shareholders.[12] An acquisition may be effected by either of the following:[13]An agreement with the person holding majority interest in the company management; Purchase of new shares by private agreement; Purchase of share in the open market (open offer); Acquisition of share capital of a company by means of cash, issuance of share capital, and Making a buyout offer to general body of shareholders.[14]

Historical Background of Merger and Acquisitions in Companies

1898-1903:This period is the first merger movement. Merger activity increased following the Sherman Act in 1890. Prior to 1890, there was a predominance of the poly-poly market structure. This was reduced and partial monopolies increased. The motivations for mergers were to expand operations, achieve economies of scale and counter competition more effectively. The relaxation of corporate laws in the US helped mergers in this period. Transportation networks and national markets were developed which increased the possibility of achieving economies of size.[15]

1926-1929: The second wave witnessed greater movement of mergers. There wasmuch vertical integration through mergers. The motive behind such mergers was to achieve technical gains from integration and to avoid dependence on other firms for raw material. Mergers were also formed to consolidate sales and distribution network as well as to save advertising expenditure.[16]

[12]*Id.* at 120.
[13]GurminderKaur, *Corporate Mergers and Acquisitions*9 (Deep& Deep Publications Pvt. Ltd., New Delhi, 2005).
[14]*Ibid*.
[15]S. ShivaRamu, *Corporate Growth Through Mergers and Acquisitions*16 (Response Books, Sage Publication India Pvt Ltd, New Delhi, 1998).
[16]*Ibid*.

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1940-1947: This is the third merger movement. A study by the Federal Trade Commission indicated the disappearance of 25,000firms during this period. The growth of eight of the largest steel corporations can be credited to acquisitions.[17]

In the 1990s, scholars have classified the Merger & Acquisition movement in the US into five waves. Peel (1995) considers the M&A movements of the 1990s to be different from the earlier waves. Corporate takeovers of the 1980s were considered to constitute the fourth wave. The fifth wave started in the 1990s. The five M&A waves were liable as:

- 1890s for monopoly.
- 1920s for oligopoly.
- 1960s for conglomerate takeovers.
- 1980s for hostile bust-up takeovers.
- 1990s driven by strategic synergistic factors.[18]

In the 1980s and 1990s, companies in the US were responding to a common set of environmental/macro factors by opting for restructuring exercises. Many of these exercises were due to three macro trends: (i) globalisation of industries, (ii) deregulation of industrial sectors and (iii) increasing threat of takeover bids.[19]

Particularly since 1993, the mergers and acquisitions are largely limited to a few industries such as banking, broadcasting, communication, leisure and entertainment, insurance, health services and wholesale and distribution. These industries are responding to deregulation, technological advancement and other fundamental factors.[20]

In India Merger and Acquisitions in Companies

In pursuance of these objectives, restrictions in India were placed on the corporate sector as per the provisions of various laws and regulations like Monopolies and Restrictive Trade Practices (MRTP)

[17] *Ibid.*
[18] *Id.* at17.
[19] *Ibid.*
[20] *Ibid.*

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Act, 1969, Foreign Exchange Regulation Act (FERA), 1973, Industrial Licensing Policy, etc. The MRTP Act, 1969 regulate on the expansion of an enterprise, establishment of new enterprise, division of undertaking, consolidation of undertakings, acquisition and transfer of shares of undertakings in order to check concentration of economic power, control the growth of monopolies and prevent various restrictive trade practices likely to result from operation of economic system. The provision of FERA, 1973 placed restrictions on foreign investment in the country. [21]

The megamergers of the 1970s had their origin in long-term structural factors that predisposed profitable companies to buy totally unrelated firms. They were further encouraged by a series of changes in the business environment that made acquisitions cheaper and gave particular firms compelling reasons to merge. Once begun, the movement was pushed towards hysteria by some who proclaimed mergers as the only path to economic success, and by others who condemned mergers but became convinced that the choice was either to acquire or be acquired.[22]

The heightened number of mergers in the 1970s could be viewed as a natural response to underlying economic forces and a changing business environment. But the feverish pace at which mergers, and especially megamergers, was more than an adaptation to a new environment. The concurrence of two phenomena seems to have been responsible for this overreaction. First, the new promise of profits through mergers was accepted overenthusiastically. Second, this over activity produced waves of defensive mergers. These mergers added to the perception that mergers were profitable and that they were necessary to preserve independence. More mergers produced urgency to merge.[23]

The study of merger and acquisitions from a geographical perspective leads, by extension, to implications for regional development. Acquisitions and mergers play a major role in the growth of city system, suggesting a link between acquisition activity and urban and regional development. The process of corporate acquisition, entailing its post-acquisition organizational restructuring, undoubtedly has implications for regional development.[24]These 1970 rules prevailed for the rest of

[21]*Supra* note 1 at 1.
[22]Kenneth M. Davidson, *Megamergers* 227(Ballinger Publishing Company, Cambridge, 1985).
[23]*Id. at* 239.
[24]*Supra* note 1 at 3.

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the twentieth century, although discussion memoranda and related statements were issued periodically.[25]

Despite being tied up within the shackles of tight regulatory system wherein prior government approval for M&A was required in the pre-liberalised regime, mergers and acquisitions were not uncommon in the decade of 80s. During 1980-89, 80 amalgamation and 52 takeovers were approved by the government.[26]

Also, it was found that during 1988-92 there have been 121 takeovers and mergers and in addition 37 takeovers bids were found unsuccessful.[27] However, most of the mergers centred on takeovers of sick industrial undertaking because of staggering industrial sickness and fiscal and other incentives offered to revive the financial health of such sick industrial undertakings. Mergers between two profit-making companies which occurred simply for economic reasons were not common. Most of the mergers were largely those of sick companies with healthy one without within the same group.[28]

In the last 40 years of control, diversification was a preferred mode of growth. Indian corporate sector was full of large conglomerate firms. The regulatory framework forced firms to diversify in various unrelated sectors. In his pioneering work[29], reports the effects of the policies adopted post-independence that led to the emergence of conglomerate firms that were specific in character. Unlike Western firms[30], the Indian firms consisted of legally independent firms that diversified into various unrelated areas, but were controlled by a single central decision-making authority. It is the lacunae in the policy structure that made the expansion through separate units easier.[31]

Over a period of time, experience demonstrated that diversified companies did not perform well. It was difficult to develop managerial capabilities required to run different kinds of business. As a

[25]J. Fred Weston, Mark L. Mitchell, *et. al.*, *Takeovers, Restructuring, and Corporate Governance*70 (Pearson Education Pte. Ltd., Delhi, 2004).
[26]Ranjit Kumar Mandal, *Corporate Mergers in India: Objectives and Effectiveness* 21-22(Kanishka Publishers, New Delhi, 1995).
[27]Financial Express, Dated 8th August, 1994, New Delhi.
[28]S.R. Shinde, "Takeovers and Mergers-As means of Industrial Restructuring" *The Mangement Accountant*, July 1995.
[29]R.K. Hazari, *The Structure of the Corporate Private Sector: A Study of Concentration, Ownership and Control* 34(Asia Publishing House, London, 1966).
[30]Western firms were single business units that diversified into linked areas.
[31]Chndra (1977) provides detailed description of loopholes that led to growth of such business units.

result, even the most competent managements did not run companies efficiently. Until the MRTP Act was abolished in 1991-1992, large firms remained in the businesses they had entered into, as there were no exit provisions. Consequently, companies with underutilised capacities on one hand and companies that were expanding capacities on the other were co-existing.[32]

Though government began initiating steps towards liberalisation in the post-1985 period, the real opening up of the economy started with the Statement on Industrial Policy made on 24th June, 1991. This statement indicated continuity with change, the main thrust being on relaxation in industrial licencing, foreign investments, transfer of foreign technology and monopolies and restrictive trade practices laws. Since 1991, there have been May economic and industrial reforms which have striven to clear the obstacles to faster industrial development.[33]

Merger and acquisitions had taken place even prior to 1994, but were few and far between. The main players, such as the Murugan group and RPG, sought to build industrial empires through acquisitions. They followed the prevailing industrial structure of building a conglomerate of diverse business into one group. The recent trend is more of restructuring firm through consolidation to face the likely competition from foreign companies.[34]In India has witnessed substantial rise in merger and acquisition (M&A) activity in industrial and financial sectors of the economy. However, despite unfavourable economic environment the existed before 1991's opening up of the economy, mergers and acquisitions were not uncommon. During 1988-92, there were about 121 takeovers and mergers. In 1991, the first year of economic reform, corporate India announced 71 M&A plans. By 1994, the number swelled to 324 and by 1995, it was 412 approximately.[35]

Merger Process

The process by which a firm decides to undertake a merger is complex. The firm lives in an uncertain environment that calls its continued survival into question. The firm is connected to the outside world by a need for resources. To ensure access to resources a firm must adapt it or force others to adapt. If a merger is determined to be the preferred course of action, a search for candidates

[32] *Supra* note 5 at 202.
[33] *Supra* note 13 at 2.
[34] *Supra* note 15 at 19.
[35] *Supra* note 13 at 2.

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is undertaken. If a candidate is found, negotiations for its purchase begin. If successful, the target firm is acquired. However, not all mergers are successful in meeting the goals of the firm. If the acquisition is deemed a failure, the firm may divest itself.[36]

The earlier section discussed in detail various legislation in India that have an impact on M & A activities. While the statutory provisions relating to amalgamation of companies are contained in Sections 390 to 396 A of the Companies Act, 1956, the procedural aspects are covered by Rules 67 to 97 of the Companies (Court) Rules, 1959. In fact, merger or amalgamation under the scheme of arrangement as provided under Sections 391-394 of the Act is the most convenient and simple method of obtaining complete merger or amalgamation between the companies. There is active involvement of the court and an amalgamation is complete only after the court sanctions it under Section 394(2) and takes affect when such order of the court is field with the Registrar of Companies. The Sections 391 to 394 of the Act, along with Company (Court) Rules, 1959 serve as a complete code in themselves in respect of provisions and procedures relating to sponsoring of the scheme, the approval thereof by the creditors and the members, and the sanction by the court.[37]

Conclusion

Merger and acquisitions are accepted as effective routes to enhance corporate efficiency and shareholder wealth. Merger and acquisitions are important phenomena in companies, and acquisition control the shareholders, share capitals, stock exchange a number of steps were also taken to regularise the stock market activities, by establishing the Securities and Exchange Board of India as watching of the capital market. Companies were made free to enter the capital market and decide their own prices within the SEBI's norms for their offer documents. Indian companies were allowed to list on foreign exchanges and were permitted to raise funds from abroad through a set of guidelines. Merger and acquisition in companies are followed the rule and regulation under MRTP Act, 1969 and SEBI.

[36] *Supra* note 1 at 21.
[37] *Supra* note 13 at 69.