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PRIVATE MERGERS AND ACQUISITIONS

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Private mergers and acquisitions in India: overview

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CORPORATE ENTITIES AND ACQUISITION METHODS

1. What are the main corporate entities commonly involved in private acquisitions?

Private limited companies and limited liability partnerships are the main corporate entities commonly involved in private acquisitions.

2. Are there any restrictions under corporate law on the transfer of shares in a private company? Are there any restrictions on acquisitions by foreign buyers?

Restrictions under the Companies Act 2013

A private limited company is required to restrict the transferability of its shares in terms of the Companies Act 2013 (Companies Act). These restrictions are contained in the company's articles of association (the bye-laws of the company). The restrictions are generally expressed as a pre-emptive right in favour of the other shareholders. It is therefore necessary to ensure that such shareholders waive their pre-emptive rights before the share purchase transaction is completed.

Foreign ownership restrictions

Foreign ownership of Indian companies is regulated under the Foreign Exchange Management (Non-debt Instruments) Rules 2019 (Foreign Investment Regulations). The government has progressively liberalised foreign investment norms. The current Foreign Investment Regulations allow 100% foreign investment in most sectors open for private investment in India. However, there are some sectors where either prior approval from the government is necessary before a foreign investment can be made, or where foreign ownership of less than 100% is permitted. Under the current foreign investment policy, foreign investment proposals that contemplate an investment of more than INR50 billion also require prior government approval, regardless of whether the sector falls under the approval route or the automatic route.

Foreign investment in a private limited company must come through the foreign direct investment route, and not from other routes (such as foreign portfolio investment). The Foreign Investment Regulations require non-residents to meet certain requirements relating to the following:

- **Equity instruments.** An Indian company can issue equity shares, convertible securities and share warrants to a foreign investor under the automatic route. Any other type of instrument does not qualify as an equity instrument, and is considered external commercial borrowing.
- **Pricing.** The equity instruments must be issued in accordance with the applicable pricing norms of the Reserve Bank of India from time to time.
- **Reporting.** Issuance of equity instruments entails making appropriate reporting under the Foreign Exchange Management (Mode of Payment and Reporting of Non-Debt Instruments) Regulations 2019.

A non-resident investor cannot be provided an assured exit price. However, a non-resident investor can be provided the option of an assured exit (subject to the mandatory lock-in period of one year or applicable sectoral regulations, whichever is longer). The exit price should be determined in accordance with the pricing rules under the instrument of transfer.

Indirect foreign investment is also a type of foreign investment, that is, where an Indian company that is owned or controlled by non-resident investors makes a downstream investment in another Indian company. Generally, the rules applicable to foreign direct investment also apply to indirect foreign investment.

3. What are the most common ways to acquire a private company? What are the main advantages and disadvantages of a share purchase (as opposed to an asset purchase)?

The most common ways to acquire a private company are the following:

- **Acquisition of shares and assets**. There are two ways to make an acquisition of a target, that is, an asset purchase and a share purchase. An acquisition can be friendly or hostile, depending on the circumstances. Acquisition of share capital of the target can be accomplished by purchasing existing shares or by subscribing to new shares of the target. Other ways to acquire share capital (such as minority squeeze-out and capital reduction) remain extremely regulated and are subject to principles set out by the courts from time to time. Therefore, a negotiated share purchase transaction remains the best way to acquire the share capital of the target.
- In an asset purchase, specific assets of the target are acquired. Asset acquisition can be accomplished by way of a demerger, sale of business as a going concern (also known as a slump sale) or itemised sale of assets of the target. A demerger is the reverse of a merger or amalgamation, where the identified business of the target is transferred to the acquirer. A demerger can be implemented either contractually or in terms of the provisions applicable to mergers and amalgamations under the Companies Act. A slump sale involves the transfer of an undertaking for a lump sum consideration without assigning values to individual assets or liabilities, except for regulatory or accounting reasons. The transaction is implemented in terms of a business transfer agreement. An itemised sale of assets is also

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referred to as "cherry-picking assets", where the acquirer purchases only the assets that are of interest to it. Generally, no liabilities are assumed, unless this is specifically agreed to. The liabilities remain with the target.

- **Mergers and amalgamations.** This is broadly used to categorise transactions which result in the combination of two or more legal entities into one. The result is the transfer of assets and liabilities of one entity (the merging entity) into another legal entity (the merged entity). The merging entity is generally dissolved after the transaction, without having to separately comply with the legal requirements of winding up under applicable laws. The shareholders of the merging entity are allotted shares in the merged entity. The Companies Act contains detailed provisions dealing with mergers and amalgamations. Within these regulations, a party can use a variety of structures. Mergers and amalgamations require the approval of the jurisdictional National Company Law Tribunal (NCLT). This process typically takes six to eight months to complete. The Companies Act and Foreign Investment Regulations also contain necessary framework to achieve a merger or an amalgamation of an Indian company with a foreign company and vice versa.

Share purchases: advantages/asset purchases: disadvantages

The advantages of share purchases and the disadvantages of asset purchases are the following:

- **Simplicity.** A share purchase transaction is a simple and straightforward transaction structure. Approval from the NCLT is not necessary, and there is no requirement to form a separate merger subsidiary to hold the business. With respect to an asset purchase, there may be a risk of failure to purchase all the assets a business needs to operate. It may also be difficult sometimes to separate the assets and the relevant contracts from the overall business and contracts of the target in an asset purchase. In an asset purchase, there may also be confusion as to what is transferred and what is retained.
- **Stamp duty savings.** There may be significant savings on the stamp duty costs involved in a share purchase transaction, if the shares are held in dematerialised form. However, the government has recently proposed to rationalise these exemptions and is working with state governments to bring in a uniform stamp duty structure as a result of which such savings may no longer be available.
- **Not necessary to apply for business licences.** The share purchase transaction does not generally entail obtaining fresh business licences or getting prior third-party approvals for the transaction (for example, under a change of control clause). Therefore, there is minimal business interruption as a result of the transaction in a share purchase transaction.
- **Speed.** An asset purchase is more time-consuming as it involves the preparation of a detailed asset listing, determining the most efficient manner to accomplish the transfer, calculating transaction costs and obtaining a valuation for each asset.
- **Liability (from a seller's perspective).** An asset purchase is not favourable from a seller perspective, as the seller is left with potential liabilities but without the corresponding assets to discharge these liabilities.
- **Employees.** Generally, share purchase transactions do not impact employees directly. There is no interruption in their service, and employees continue to receive the same compensation and benefits. Therefore, the requirement to pay "retrenchment compensation" under the Industrial Disputes Act 1947 does not apply to share purchase transactions.

Share purchases: disadvantages/asset purchases: advantages

The advantages of asset purchases and the disadvantages of share purchases are the following:

- Asset purchase transactions are more efficient to complete if the shareholders are a heterogenous group. It avoids the requirement to engage in negotiations with multiple shareholder groups (for example, polarised groups under the control of different people/companies).
- Mergers and amalgamations do not require the unanimous approval of all the shareholders involved. It only requires the approval of shareholders holding three-quarters in value of the total paid up capital of the company. This threshold is particularly useful when anticipating challenges in getting all the shareholders on-board in a share purchase transaction. While a dissenting shareholder can challenge the merger or amalgamation before the NCLT, he/she needs to satisfy certain minimum shareholding thresholds to mount a challenge.
- The Companies Act provisions dealing with mergers and amalgamations allow great flexibility in structuring transactions. The Companies Act allows parties to incorporate capital reduction and minority squeeze-out provisions in accordance with the mergers and amalgamations provisions. The Companies Act also allows the merged entity to use the regulatory costs paid by the merging entity on its authorised share capital.
- An itemised sale of assets is a very favourable structure from a buyer's perspective. It allows the buyer to pick and choose only the assets it wants to acquire without inheriting the accompanying liabilities. In contrast, the buyer may be exposed to unknown risks in a share acquisition.

4. Are sales of companies by auction common? Briefly outline the procedure and regulations that apply.

Sale of companies by auction is quite common. A bidding process is typically organised by the investment banker. The bidding process culminates in bidders submitting a detailed bid. A bid should be clear, precise and address all aspects of the acquisition, including the source of financing. The shortlisted acquirer moves to the next stage, that is, the process of entering into exclusive negotiations with the seller to conclude the transaction. Bidders who show a clear source of funding are likely to be selected in the bidding process.

It is advisable to adopt a fair and transparent bidding process to reduce future claims.

PRELIMINARY AGREEMENTS

5. What preliminary agreements are commonly made between the buyer and the seller before contract?

Letters of intent

A letter of intent often referred to as a memorandum of understanding or term sheet) is commonly made between the buyer and the seller before a contract. These preliminary agreements are generally non-binding (except such terms that are expressly made binding).

Clauses dealing with break-up fee, exclusivity, confidentiality, governing law and dispute resolution are generally binding.

Exclusivity agreements

These agreements require parties to negotiate with each other exclusively, with a view to enter into a contract. The exclusivity is for a limited duration and the parties are free to negotiate with third parties upon expiry of the duration.

An exclusivity agreement should be stamped in terms of the stamp law.

The non-breaching party can obtain an interim injunction order from the competent forum. While this provides immediate relief to the non-breaching party, the ultimate objective is to claim damages for breach.

Non-disclosure agreements

Typically, acquisitions entail parties exchanging commercially sensitive and publicly unavailable proprietary information. It is important to ensure that the recipient of this information uses it only in relation to evaluating the proposed transaction. Therefore, parties enter into a mutual non-disclosure agreement to set out the confidentiality obligations in relation to such information. These agreements are binding and enforceable under Indian law.

For enforcement and remedies available for breach of non-disclosure agreements, see above,*Exclusivity agreements*.

ASSET SALES

6. Are any assets or liabilities automatically transferred in an asset sale that cannot be excluded from the purchase?

There is considerable flexibility in determining which assets or liabilities are excluded from the purchase. However, under the Income Tax Act 1961 (Income Tax Act), the following conditions must be met for a merger and amalgamation to qualify as an amalgamation:

- All assets and liabilities of the merging company must transfer to the merged company.
- Shareholders holding at least 75% of the value of the shares of the merging company become shareholders in the merged company.

7. Do creditors have to be notified or their consent obtained to the transfer in an asset sale?

Under the Companies Act, a copy of a proposed merger or demerger must be served on the creditors, and consent of the creditors constituting at least three-quarters in value must be obtained. Their consent needs to be obtained in a meeting of the creditors, unless the NCLT has waived the requirement to hold such a meeting. In such a case, the consents are collected in the form of an affidavit. If the meeting of the creditors is dispensed with in such a way, the threshold of approval in such cases is 90% of creditors in value.

The Companies Act does not require that consent is obtained by creditors in a slump sale or an itemised sale of assets. However, their consent is required if there are contractual provisions between the company and the creditor to that effect. Financing agreements typically require the borrower to obtain the consent of the creditors before the transfer of an asset.

A transfer of shares or fixed assets while tax proceedings are pending against the transferor company is void, unless the transferor company has obtained a no-objection certificate from the assessing officer (*section 281, Income Tax Act*). Therefore, this certificate is necessary in M&A transactions.

SHARE SALES

8. What common conditions precedent are typically included in a share sale agreement?

The following common conditions precedent are typically included in a share sale agreement:

- Completion of due diligence to the satisfaction of the acquirer.
- Obtaining the necessary regulatory and corporate approvals, including anti-trust approvals (if applicable).
- Warranties being true and correct as on the closing date.
- Obtaining a valuation certificate to show compliance with the applicable pricing norms prescribed by the Foreign Investment Regulations.
- Resolving identified diligence findings, as may be agreed between the parties.

SELLER'S TITLE AND LIABILITY

9. Are there any terms implied by law as to the seller's title to the shares in a share sale? Is any specific wording necessary and do buyers normally impose a higher standard than is implied by law?

Shares are considered goods under the Sale of Goods Act 1930 (Sale of Goods Act). Under the Sale of Goods Act, the following terms are implied by law as to the seller's title to the shares (unless the circumstances of the contract show a different intention):

- An implied condition that the seller has the right to sell the goods.
- An implied warranty that the buyer has quiet possession of the goods.
- An implied warranty that the goods are free from any undisclosed charge or encumbrance in favour of any third party.

Buyers typically ask for additional warranties in relation to title. The kind of additional warranties requested depends on the details of the transaction. These warranties are often heavily negotiated between the parties.

10. Can a seller and its advisers be liable for pre-contractual misrepresentation, misleading statements or similar matters?

There are no clear rules around this. It may be difficult to hold a seller and its advisers liable for pre-contractual misrepresentation if the transaction agreement expressly excludes liability in relation to statements made before the conclusion of such agreements. Typically, the transaction agreement contains a clause which states that the transaction agreement overrides previous communications and statements made by the seller and their advisers. However, a seller and its advisers can be held liable for fraudulent misrepresentations.

MAIN DOCUMENTS

11. What are the main documents in an acquisition and who generally prepares the first draft?

The main documents in an acquisition are as follows:

- Share purchase agreement (prepared by the buyer).
- Disclosure letter (prepared by the seller).
- Waiver letters by the existing shareholders (prepared by the seller).
- Fresh set of bye-laws (prepared by the buyer).
- Escrow agreement, if necessary (prepared by the escrow agent in conjunction with the buyer).
- Earn-out or compensation agreements with key employees of the target (prepared by the buyer).
- Business transfer or asset purchase agreement (prepared by the buyer).
- Relevant employment documents and employee consents (prepared by the buyer and seller).
- Assignment and assumption agreement, with respect to existing contracts in the case of slump sale (prepared by the buyer).
- Novation agreement, with respect to existing contracts in an asset sale (prepared by the buyer).
- A scheme of merger and amalgamation.

ACQUISITION AGREEMENTS

12. What are the main substantive clauses in an acquisition agreement?

The main substantive clauses in an acquisition agreement are as follows:

- Payment of purchase consideration and the form of payment, including purchase consideration hold-back and establishment of an escrow account.
- Conditions precedent to the acquisition.
- Closing and closing-related actions.
- Post-closing obligations.
- Representations, warranties and covenants.
- Indemnities (particularly tax indemnities).
- Governing law and dispute resolution process.
- Non-compete restrictions.
- Payment of costs and expenses.

13. Can a share purchase agreement provide for a foreign governing law? If so, are there any provisions of national law that would still automatically apply?

The basic legal principle is that Indian parties are bound by Indian law. It has been held that Indian parties contracting out of Indian law is against the public policy of India. However, an agreement can provide for a foreign governing law if the agreement is between an Indian party and a foreign party. A transaction governed by a foreign law must still comply with specific Indian requirements under (for example) the Income Tax Act, the Foreign Investment Regulations and the Competition Act 2002 (Competition Act).

India has a robust and independent arbitration system for both domestic arbitration and international commercial arbitrations. Awards of arbitrators are recognised as "decrees" of a court of law and enforced as such. India is a signatory to the New York Convention on the Enforcement of Foreign Awards. Therefore, Indian law recognises and enforces foreign seated arbitration awards.

WARRANTIES AND INDEMNITIES

14. Are seller warranties/indemnities typically included in acquisition agreements and what main areas do they cover?

Seller warranties or indemnities are typically included in an acquisition agreement. These cover areas such as the following:

- Title and marketability to/of shares, assets and properties of the target.
- Organisation of the target and the sellers.
- Capitalisation of the target.
- No conflicts or consents.
- Financial statements.
- Undisclosed liabilities.
- Absence of certain changes, events and conditions.
- Material contracts.
- Condition and sufficiency of business assets.
- Inventory.
- Accounts receivable and accounts payable.
- Customers and suppliers.
- Insurance.
- Legal proceedings and governmental orders.
- Compliance with laws, permits and so on.
- Employee-benefit plans and employee matters.
- Real property and leases.
- Taxes.
- Books and records.
- Related party transactions.
- Bank accounts and power of attorney.
- Environmental matters.

15. What are the main limitations on warranties?

Limitations on warranties

The main limitations on warranties are:

- The statute of limitations.
- Disclosed matters.
- *De minimis* thresholds for making claims.
- Transactions involving non-residents. An amount of up to 25% of the total consideration can be set aside to meet indemnity payments. However, these payments must be made by / or to

non-residents within 18 months from the date the full consideration was paid, if the total consideration has already been paid. However, the total consideration finally paid for the transfer must comply with the pricing rules under the Foreign Investment Regulations (*see Question 17, Factors in choice of consideration*).

Qualifying warranties by disclosure

Qualifying warranties by disclosure is standard and common. Unless otherwise agreed, the buyer may insist on an indemnity in certain cases even after disclosure.

16. What are the remedies for breach of a warranty? What are the time limits for bringing claims under warranties?

Remedies

There are two types of remedies that are fundamentally used in an acquisition transaction, that is:

- **Claims for (liquidated or unliquidated) damages.** Generally, the court awards damages or compensation based on directness of damages and the mitigation measures of the non-breaching party. Indian contract law does not permit the payment of indirect, special, consequential or punitive damages.
- **Indemnities.** Parties to a contract can also seek to address certain specific types of risks through an indemnity. The intention of an indemnity clause is to restore the non-breaching party to the same position as though no loss occurred. An indemnity is a contractual (and not statutory right). Therefore, it should be specifically included in the contract. The principles of remoteness of damages and the duty to mitigate (which would otherwise apply to an award of damages) do not apply to indemnities.

Indemnity payments to a foreign party should be structured as per the Foreign Investment Regulations (*see Question 2*). A payment of damages under an indemnity may require the prior approval of the Reserve Bank of India.

Warranties and indemnity insurance or representations and warranties insurance are also emerging as an option to address the risks arising from breach of warranties. Increasingly, this is a key differentiator between various bidders and the bid that offers insurance is likely to stand a better chance of qualifying.

Time limits for claims under warranties

The statute of limitation generally prescribes three years for making monetary claims, subject to certain exceptions. However, parties to the transaction generally negotiate to align the limitation period with the relevant statutes. For instance, the Income Tax Act allows an assessment officer to reopen assessment proceedings against a company up to seven years after the end of the relevant financial year. Therefore, the buyer typically asks for tax warranties for seven years from the end of the relevant financial year.

CONSIDERATION AND ACQUISITION FINANCING

17. What forms of consideration are commonly offered in a share sale?

Forms of consideration

The purchase consideration is generally discharged by payment of cash. It remains the most common way to conclude acquisitions. Non-cash consideration options can also be evaluated based on the transaction structure. For example, consideration can be discharged by a swap of shares. However, this remains a regulated activity under the Foreign Investment Regulations.

Factors in choice of consideration

Tax considerations are often the biggest factor in determining the choice of consideration.

In addition to tax considerations, Foreign Investment Regulations also play a key part. For the most part, the Foreign Investment Regulations require consideration to be discharged by payment of cash through ordinary banking channels. Non-cash consideration is only allowed in certain situations. The consideration payable in a transaction should also comply with the pricing norms under the Foreign Investment Regulations. The pricing norms are briefly explained below:

- **Transfer of a stake from a resident to a non-resident.** The price should be no less than the fair market value determined by an Indian chartered accountant applying an internationally accepted pricing methodology on an arm's length basis.
- **Transfer of a stake from a non-resident to a resident.** The price should be no more than the fair market value determined by an Indian chartered accountant applying an internationally accepted pricing methodology on an arm's length basis.

The above pricing rules also apply in the case of allotment of shares to non-residents on a private placement or a preferential allotment basis.

Deferred consideration structures or earn-outs can also be implemented under the Foreign Investment Regulations. These structures are allowed under the automatic route if the following are met:

- The deferred consideration does not exceed 25% of the total purchase consideration.
- The deferment does not extend beyond 18 months.
- The final consideration that is settled by the parties complies with the pricing norms above.

In case of allotment of securities to a non-shareholder, the Companies Act envisages a valuation undertaken by a registered valuer and allotted at fair value.

18. If a buyer listed in your jurisdiction raises cash to fund an acquisition by an issue of shares, how is the issue typically structured? What consents and regulatory approvals are likely to be required?

Structure

A buyer listed in India can raise cash to fund an acquisition through the following routes:

- Rights issue.
- Private placement.
- Follow-on public offering.
- Qualified institutional placement.

Consents and approvals

Approval of the board of directors is required in all cases. Approval of the shareholders is also required in case of a private placement of shares and public offer. The Companies Act also envisages the approval of the acquirer's shareholders by way of a special resolution if the value of the transaction exceeds either:

- 60% of the acquirer's paid-up share capital and free reserves and securities premium account.
- 100% of its securities premium account.

Other regulatory approvals may also be needed, depending on the sector of the target.

Permission from the applicable stock exchange for listing of shares must also be obtained. The target should also execute a listing agreement with the relevant stock exchange to cover the matters specified in the listing regulations.

Requirements for a prospectus

An offer document must be circulated among the potential investors. In a rights issue, this document is called a letter of offer. In all other cases, the offer document is called a prospectus. A copy of the offer document must be filed with the jurisdictional registrar of companies. The securities market regulator has prescribed detailed rules as to the content of the prospectus. Misstatements in a prospectus can result in civil liability and criminal liability, depending on the facts of each case.

19. Can a company give financial assistance to a potential buyer of shares in that company?

Restrictions

A public limited company cannot provide financial assistance to fund the acquisition of its shares. The prohibition extends to providing a loan, guarantee or security for the purpose of, or in connection with, any purchase or subscription to its shares. The above restrictions also apply to giving financial assistance to acquire shares of its holding company.

Exemptions

The Companies Act does not expressly prohibit a private limited company from giving financial assistance to a potential buyer of shares in that company.

SIGNING AND CLOSING

20. What documents are commonly produced and executed at signing and closing meetings in a private company share sale?

Signing

At signing, the following documents are typically signed or produced:

- A share purchase agreement or an asset purchase agreement.
- Relevant corporate resolutions approving the execution of the agreement and identifying authorised signatories.

Closing

At closing, the following documents are typically signed or produced:

- Relevant corporate resolutions taking on record the closing of the transaction.
- Filing of a Single Master Form under the Foreign Investment Regulations with the authorised dealer bank. Under the Foreign Investment Regulations, the Single Master Form is required to be filed within 60 days of receipt of funds or share transfer (whichever is earlier).
- Securities transfer form (SH-4, under the Companies Act) (Securities Transfer Form).
- Filing of relevant forms with the company registry.
- Resignation of the seller's nominees from the board of directors.
- Appointment of the buyer's nominees to the board of directors.
- Relevant employment agreements.
- The new bye-laws of the company.

21. Do different types of document have different legal formalities? What are the formalities for the execution of documents by companies incorporated in your jurisdiction?

Different types of documents do have different legal formalities.

Documents which qualify as an "instrument" must be stamped in accordance with the relevant stamp act. The rate of stamp duty is prescribed by the federal government (if the instrument falls under the union list). The relevant state government is entitled to prescribe the rate of stamp duty if the instrument falls under the state list. The stamp duty should be paid at (or before) the time of executing the instrument. If the instrument is executed outside India, it must be stamped within three months of its receipt in India. An instrument which is not stamped under the relevant stamp law is not admissible as evidence before a court of law or an arbitral panel. In addition, a public authority can impound such documents.

The instrument relating to a transfer of immovable property or intellectual property of a certain value must be registered with the jurisdictional sub-registrar's office. An additional levy (that is, registration fees) must be paid with respect to such instruments.

Any person authorised by the board of directors can sign a document or instrument on behalf of the company.

In some cases, the document must be stamped with the common seal of the company (if required under the bye-laws of the company).

22. What are the formalities for the execution of documents by foreign companies?

There are no special requirements for the execution of documents by foreign companies. The requirements set out in *Question 21* apply when documents are executed by foreign companies. The only additional requirement is that affirmations (such as affidavits and declarations) are apostilled in accordance with the HCCH Convention Abolishing the Requirement of Legalisation for Foreign Public Documents 1961 (Apostille Convention).

23. Are digital signatures binding and enforceable as evidence of execution?

The Information Technology Act 2000 provides the regulatory regime regarding digital signatures and electronic signatures. Under the Information Technology Act 2000, digital signatures (that is an asymmetric crypto-system and hash function) issued by recognised certifying authorities are a valid source of signature. A legal presumption exists with respect to documents that are digitally signed. Therefore, parties to an M&A transaction can use the digital signatures for executing documents.

24. What formalities are required to transfer title to shares in a private limited company?

The formalities under the articles of association and the Companies Act must be complied with. A waiver of pre-emptive rights by the other shareholders must be obtained (*see Question 2, Restrictions under the Companies Act 2013*). In addition, any contractual stipulations regarding share transfers must be complied with.

The Companies Act requires the transferor and transferee to deposit a duly executed Securities Transfer Form with the board of the target. The Securities Transfer Form must be stamped at the rate of 0.25% of the purchase consideration (including premium, if any).

This is a federal levy and must be paid to the appropriate jurisdictional officer.

The requirement for a Securities Transfer Form does not apply if the shares are held in dematerialised form. In such cases, the transferor and the transferee must give the relevant transfer instructions to the respective depository, who will carry these transfer instructions out in the electronic records maintained by it.

TAX

25. What transfer taxes are payable on a share sale and an asset sale? What are the applicable rates?

Share sale

The Securities Transfer Form is required to be stamped at 0.25% of the purchase consideration. However, this levy does not apply if the shares are held in dematerialised form (*see Question 24*). The Finance Act 2019 proposes to introduce a uniform rate of stamp duty on all share transfer transactions, regardless of whether they are dematerialised or not (*see Question 3, Share purchases: advantages/asset purchases: disadvantages*).

Stamp duty is also payable on the share purchase agreement as the agreement is treated like an instrument. This is a state levy and states set specific rates for such agreements.

Asset sale

An order of the NCLT sanctioning the scheme of merger or demerger is considered an instrument. It is therefore subject to stamp duty under the relevant state stamp act. The stamp duty is calculated as a percentage of the value of the transferor company's properties located in that state, or a percentage of the value of shares issued to the shareholders of the transferor company (whichever is higher). However, certain state stamp acts do not have a specific entry dealing with stamp duty on NCLT orders. In such states, an NCLT order is treated like a conveyance. Therefore, the stamp duty conveyance rate must be paid on the order of the NCLT.

The business transfer agreement needs to be stamped on the *ad valorem* value. The range of stamp duty is 3% to 6% of the purchase consideration (depending on the state-specific stamp legislation).

An additional levy (that is, registration fees) is payable to the sub-registrar's office if immovable property is being sold or leased. The state governments have jurisdiction to levy the registration fee.

26. What are the main transfer tax exemptions and reliefs in a share sale and an asset sale? Are there any common ways used to mitigate tax liability?

In case of a merger, amalgamation and demerger:

- A consolidated stamp duty is payable on the order of the NCLT. There is no requirement to pay stamp duty on individual assets. Some Indian states also provide a more relaxed regime in case of intra-group mergers and amalgamations with respect to stamp duty.
- The Companies Act also allows the transferee company to use the stamp duty and registration fees paid by the transferor company on its authorised share capital against future capital increases.
- Until the government amends the applicable laws, shares that are held in dematerialised form are not subject to stamp duty (*see Question 24*).

27. What corporate taxes are payable on a share sale and an asset sale? What are the applicable rates?

Share sale

Income tax is payable on the gains made by the seller. These gains are taxed as capital gains. The rate of taxation depends on the residency status of the seller and the holding period of the shares, as follows:

- Long-term capital gains (LTCG) tax is payable if the shares are held for more than 24 months. The rate of LTCG is 20% (plus the applicable surcharge and cess) in the case of a resident and it is 10% in the case of a non-resident. STCG is charged at 30% (plus applicable surcharge and levy) for residents and 40% for non-residents. While computing LTCG, indexation of the acquisition cost is allowed. This benefit is not available to non-residents while calculating taxable profits. However, the gains are computed in the applicable foreign currency denomination.
- Short-term capital gains (STCG) tax is payable if the shares are held for less than 24 months.

There is a requirement to withhold applicable taxes when making payments to non-residents. The obligation must be discharged by the buyer of shares or assets. Payments made to a resident seller are generally not subject to tax withholding obligations.

India has also introduced indirect transfer taxes in 2012, but with retrospective effect from 1961. Under these provisions, an indirect transfer of an Indian company's shares is subject to Indian income tax if both:

- The overseas assets derived their substantial value from Indian assets. "Substantial" means at least 50% of the value of assets.
- The value of the Indian assets is at least INR100 million.

Indian transfer pricing rules apply in a transfer of shares between associated enterprises under the Income Tax Act.

Asset sale

Mergers and amalgamations can result in a taxable event in India if they involve a transfer of a capital asset in India. However, certain classes of mergers, amalgamations and demergers have been specifically exempted from capital gains tax (if certain conditions under the Income Tax Act are met).

In a slump sale, the sale of an undertaking is subject to LTCG if the undertaking is held for at least 36 months. This is regardless of the holding period of individual assets. Capital gains from a slump sale is taxed at 20% (which is additional to any fees and levies) if the undertaking is held for 36 months or more and 30% (which is additional to any fees and levies) in any other case.

In an itemised sale of assets, the capital gains tax payable will depend on the holding period of the asset. Capital gains from an itemised sale of assets is taxed at 20% (exclusive of surcharge and cess) if the asset is held for 36 months or more and 30% (exclusive of surcharge and cess) in any other case.

Indirect transfer taxes also apply in an asset sale (subject to certain exemptions under the Income Tax Act).

Indian transfer pricing rules apply in a transfer of assets between associated enterprises, under the Income Tax Act.

28. What are the main corporate tax exemptions and reliefs in a share sale and an asset sale? Are there any common ways used to mitigate tax liability?

India has entered into double taxation avoidance agreements (DTAAs) with many countries. These DTAAs provide for a mechanism to deal with cross-border taxation issues. The DTAAs with certain countries like Singapore, Mauritius, The Netherlands and Cyprus provide a favourable framework for taxation of capital gains. Investments into India are generally routed through these jurisdictions under these provisions.

A merger or amalgamation can be structured in a tax-neutral manner by fulfilling the conditions under the Income Tax Act.

Resident shareholders can also avoid paying LTCG on the sale of shares by investing the gains in certain specified assets or bonds.

However, India has introduced the General Anti Avoidance Rules (with effect from 1 April 2017). This is an overarching legislative framework that impact all types of corporate restructuring activities whose primary aim is tax avoidance. These rules apply to transactions of a certain value. The Income Tax Department needs certain approvals before it can invoke the General Anti Avoidance Rules.

29. Are other taxes potentially payable on a share sale and an asset sale?

The definition of goods and services under the goods and services tax (GST) regime excludes shares and stocks from its scope. Therefore, no GST is payable on share purchase transactions.

In mergers and amalgamations and demergers, no GST is incurred as this entails a transfer of an entire business as a going concern. Again, slump sale transactions are GST-exempt.

However, GST is payable on the sale of individual assets in an itemised sale of assets' transaction. The rate of GST on such assets depends on the nature of assets transferred. The range of GST is between 5% and 28%. However, GST paid on the sale of assets may be available as an input tax credit for the buyer (if certain conditions are met).

30. Are companies in the same group able to surrender losses to each other for tax purposes? For example, can interest expenses incurred by a bid vehicle incorporated in your country be set off against profits of the target before tax?

The Income Tax Act provides that in case of a merger, amalgamation and demerger of a company that owns an industrial establishment with another company, the accumulated losses and the unabsorbed depreciation of the amalgamating company can be carried forward and set off against profits of the amalgamated company. However, this benefit is only available if certain conditions under the Income Tax Act are met.

The Income Tax Act also recognises the carry-forward of tax holidays available to the amalgamating company (if the amalgamated company meets certain conditions under the Income Tax Act).

The amalgamated entity is also allowed a deduction with respect to the expenditure incurred wholly and exclusively for the purpose of amalgamation. The same can be used over a five-year period, commencing from the year when the amalgamation takes place.

EMPLOYEES

31. Are there obligations to inform or consult employees or their representatives or obtain employee consent to a share sale or asset sale?

Indian law categorises employees as workmen or non-workmen, depending on the nature of the work they perform. Under the Industrial Disputes Act 1947, a person employed to do any manual, technical, skilled, technical or non-technical work is a workman, unless they are:

- Employed mainly in a managerial or administrative capacity.
- Employed in a supervisory capacity, drawing wages exceeding INR10,000 per month, or exercising functions that are mainly of a managerial nature.

All other categories of employees are considered as non-workmen.

Indian law does not recognise an automatic transfer of workmen during such transfer transactions. Their prior consent is required. The law does not expressly address the issue of transfer of non-workmen. However, the rules applicable to transfer of workmen are generally followed even in the case of non-workmen.

Consent of workmen or employees is not required under a share transaction, as this involves no transfer of workmen or employees. However, their consent is required in asset transactions that involve their transfer. Also, certain enterprises with trade unions enter into a settlement agreement dealing with rights of workers. The settlement agreement often deals with asset transfer situations. The settlement agreement must be complied with.

32. What protection do employees have against dismissal in the context of a share or asset sale? Are employees automatically transferred to the buyer in a business sale?

Workmen are protected against dismissal in the context of a share or asset sale. Under the Industrial Disputes Act, a workman who has been in continuous service for at least one year cannot be dismissed unless the following conditions are met:

- The workman is given one-month's notice, or salary in lieu of notice.
- The workmen are paid retrenchment compensation calculated as 15-days' average pay for every completed year of continuous service or if any part of continuous service of more than six months is paid as retrenchment compensation.
- The employer must report the dismissal to the local labour officer.

However, the above rules do not apply if it is shown that:

- The workman's services are uninterrupted despite the transfer.
- The terms of employment of the workman are no less favourable than their previous terms.
- The new employer must recognise the previous employment of the workmen for the purpose of benefits and awards.

In addition to the Industrial Disputes Act, the relevant state Shops and Establishment Act also sets out certain requirements. The Shops and Establishments Act of most states also provides the necessary legal framework regarding employee dismissals.

The legal framework described above sets the minimum compensation payable to a workman in case of dismissal. However, parties can always agree to a better severance package than the one provided under law.

The law requires prior approval from the jurisdictional labour officer if the retrenchment is proposed by a factory that has employed on average 100 or more workmen per working day for the preceding 12 months.

PENSIONS

33. Do employees commonly participate in private pension schemes established by their employer? If an employee is transferred as part of a business acquisition, is the transferee obliged to honour existing pension rights or provide equivalent rights?

Private pension schemes

Indian labour and employment law require every establishment employing 20 or more persons to make provident fund contributions. The employer and the employee contribute an equal amount to a provident fund scheme established by the government. The rate of contribution is currently fixed at 12% of the basic wages. Employees are also entitled to receive gratuity calculated as a percentage of their salary at the end of five years of continued employment with the relevant employer. This gratuity is currently capped at INR2,000,000 per employee. India has also established the Employees State Insurance scheme. This scheme requires both employers and employees to make certain contributions to a centrally administered insurance scheme. Employees or their legal heirs can rely on insurance in case of death or disablement.

Pensions on a business transfer

The acquirer must ensure continuity of service to employees (*see Question 32*). The terms of employment must not be less favourable than those offered by the previous employer. Retrenchment compensation is payable to the relevant employee if these conditions are not met. The statutory social security and pension contributions (such as provident fund, pension and gratuity) must be honoured by the new employer. These benefits are either paid out at the time of acquisition, or recorded in the books of the acquirer as payable. Most transactions record these benefits in the books of the acquirer as payable to ensure that the transfer does not result in interruption of service to employees.

COMPETITION/ANTI-TRUST ISSUES

34. Outline the regulatory competition law framework that can apply to private acquisitions.

Triggering events/thresholds

The Competition Act 2002 (Competition Act) regulates combinations. The Competition Act confers extra-territorial jurisdiction on the regulator over combinations based on assets in India and turnover from India. Any enterprise intending to enter a combination must notify the Competition Commission of India (CCI) and seek its permission for consummating the combination.

A transaction is a combination if any of the following are met:

- If the acquisition (of shares, control, voting rights or assets) of the target results in the:
  - acquirer and target having assets of more than IN20 billion in India or turnover of more than INR60 billion in India;
  - acquirer's group and the target having assets of more than USD1 billion in value globally (with at least INR10 billion of assets in India) or turnover of more than USD3 billion globally (with at least INR30 billion of turnover from India);
  - acquirer's group having assets of more than INR80 billion in India or turnover of more than INR240 billion in India; or
  - acquirer's group having assets of more than USD4 billion globally (with at least INR10 billion of assets in India), or turnover of more than USD12 billion globally (with at least INR30 billion of turnover from India).
- Acquisition of control over an enterprise when the acquirer already has control over another enterprise engaged in distribution, production or trading of a similar or identical or substitutable goods or provision of a similar or identical or substitutable service where:
  - the enterprise over which the acquirer has control, along with the target in India, has assets of more than INR20 billion, or turnover of more than INR60 billion in India;
  - if the acquirer and target have more than USD1 billion in assets globally (with at least INR10 billion of assets in India), or turnover of more than USD3 billion globally (with at least INR30 billion turnover from India);
  - the acquirer's group has assets of more than INR80 billion, or turnover of more than INR240 billion; or
  - the acquirer's group has assets of more than USD4 billion globally (with at least INR10 billion of assets in India), or turnover of more than USD12 billion globally (with at least INR30 billion of turnover from India).
- Any merger or acquisition in which:
  - the remaining entity or amalgamated entity has assets of more than INR20 billion in India, or turnover of more than INR60 billion in India;
  - the assets of the remaining entity or the amalgamated entity are more than USD1 billion globally (with at least INR10 billion of assets in India); or the turnover is more than USD3 billion globally (with at least INR30 billion of turnover from India);
  - the acquirer's group has more than INR80 billion of assets in India, or its turnover from India exceeds INR240 billion; or
  - the assets of the remaining entity or the amalgamated entity are more than USD4 billion globally (with at least INR10 billion of assets in India), or turnover is more than USD12 billion globally (with at least INR30 billion of turnover from India).

A combination that causes or is likely to cause an appreciable adverse effect on competition is prohibited and is void.

De-minimis exemption/small-target exemption. This is available where the value of assets being acquired, taken control of, merged or amalgamated does not exceed INR3.5 billion in India, or the turnover from India is not more than INR10 billion. This exemption is available for five years from 27 March 2017.

Exceptions to the approval requirement. The CCI regulations also exempt certain categories of combinations that are ordinarily not expected to have an appreciable adverse effect on competition.

Timeframe for approving combinations. The CCI must make a decision regarding the combinations within 210 days of its notification to it. However, as per the relevant combination regulations, the CCI must formulate a prima-facie view about the combination within 30 days of notification of the combination. Generally, the CCI keeps to this time period.

ENVIRONMENT

35. Who is liable for clean-up of contaminated land? In what circumstances can a buyer inherit and a seller retain liability in an asset sale and a share sale?

India has a range of umbrella legislation, such as the:

- Environment (Protection) Act 1986.
- Air (Prevention and Control of Pollution) Act 1981.
- Water (Prevention and Control of Pollution) Act 1974.
- National Green Tribunal Act 2000.

The broad principle under these statutes is that the occupier of the land is liable for contaminated land. However, government has endeavoured to hold the perpetrator of the contamination liable. For example, under the Guidelines on Implementing Liability for Environmental Damage due to Handling and Disposal of Hazardous Waste and Penalties, the occupier may be excluded from liability if he/she proves that the contamination was caused by the previous occupier or owner.

In a share sale, the buyer acquires all the liabilities, including environmental liabilities. Environmental liabilities may be excluded in asset acquisitions, depending on the transaction structure. However, given the risk of liability attaching to the occupier, it may be best to have robust environmental warranties.

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