# Restructuring of companies under the Companies Act, 2013

**This article aims to:**

- Provide an overview of the key provisions of the Companies Act, 2013 with respect to restructuring of companies (i.e. compromises, arrangements and amalgamations)
- Highlight the corresponding requirements prescribed by SEBI under the Listing Regulations.

## Introduction

Mergers and acquisitions are the common forms of restructuring and expansion exercised by the companies. The objectives of such arrangements could vary from drawing synergies, enhancing capacities, tax benefits to consolidation of operations, etc.

In India, mergers and acquisitions schemes are required to be approved by the National Company Law Tribunal (NCLT) under the provisions of the Companies Act, 2013 (2013 Act).

The 2013 Act prescribes separate procedures for following kinds of arrangements:

- Compromise or arrangement between a company and its creditors or shareholders (Section 230)
- Merger or amalgamation between companies (other than wholly-owned subsidiary and small companies) (Section 232)
- Merger or amalgamation of a company with wholly-owned subsidiary or small companies (Section 233) and
- Merger or amalgamation of a company with a foreign company (Section 234).

The Rules facilitating the provisions of the above sections i.e. Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 (Compromises Rules) came into effect from 15 December 2016.

In this article, we aim to provide an overview of the key provisions of the 2013 Act and the related Rules in relation to the restructuring of companies (i.e. compromises, arrangements and amalgamations). We also highlight the relevant requirements of the Securities and Exchange Board of India (SEBI) (Listing Obligations and Disclosure Requirements) Regulations, 2015 (Listing Regulations) that are applicable to listed companies in India.

### Arrangements with creditors or shareholders (Section 230, 231 and Section 232)

A company undertaking a scheme of arrangement is governed by the provisions of Section 230 and 232 of the 2013 Act. A company could restructure their arrangements with creditors or shareholders in a number of ways, and they are as follows:

a. Reorganisation of the company's share capital by the consolidation of shares of different classes or by the division of shares into shares of different classes, or by both of those methods

b. Reduction of share capital

c. Corporate debt restructuring[1] (consented by not less than 75 per cent of the secured creditors)

d. Buy-back of securities

e. Take-over offer[2]

f. Merger[3]/amalgamation of any two or more companies

g. Demerger/division[4] of companies.

A company that undertakes any of the above mentioned schemes of arrangement would need to comply with certain procedure. The procedure is as follows:

- **Application to the NCLT:** An application to the NCLT has be made for the proposed scheme of compromise/arrangement in Form No. NCLT-1. This application can be made by the company, creditor, member of the company, or liquidator (in case of a company being would up).

  The above application should be accompanied by appropriate disclosures (by way of an affidavit in Form No. NCLT-6) and also include:

  a. All material facts relating to the company such as the latest financial position of the company, the latest auditor's report on the accounts of the company and the pendency of any investigation or proceedings against the company

  b. Reduction of share capital, if any, included in the compromise or arrangement.

  In case of a *corporate debt restructuring* scheme, a company would have to disclose to the NCLT:

  - A creditor's responsibility statement in Form No-CAA.1
  - An auditor's report stating that the fund requirements of the company after the corporate debt restructuring (as approved by NCLT) conform to the liquidity test based upon the estimates provided to them by the Board should be furnished
  - Safeguards for the protection of other secured and unsecured creditors
  - Where the company proposes to adopt the corporate debt restructuring guidelines specified by the Reserve Bank of India (RBI), a statement to that effect
  - A valuation report in respect of the shares and the property and all assets, tangible and intangible, movable and immovable, of the company by a registered valuer.

- **Order and notice of the meeting:** On receipt of the application, the NCLT could order a meeting of the shareholders/ creditors to be held in the prescribed manner. Notice of such a meeting should be in Form No. CAA.2 and accompanied by a statement disclosing details of the compromise/arrangement including its effect on material interests of the creditors, key managerial personnel, directors or employees of the company. A copy of the valuation report, if any, should also be sent along with the notice.

  *Merger/division of companies*

  In case of a scheme that involves merger or division, merging companies or the companies (in respect of which division has been proposed) would be, *inter alia,* also required to circulate a supplementary accounting statement, if the last annual accounts of any of the merging company relate to a Financial Year (FY) ending more than six months before the first meeting of the company summoned for the purposes of approving the scheme.

- **Notice to statutory authorities:** A notice in Form No. CAA.3 along with the prescribed documents should also be given to the Central Government (CG), income-tax authorities, RBI, SEBI, Registrar of Companies (ROC), stock exchanges, official liquidator, Competition Commission of India (CCI) and other sectoral regulators/authorities which are likely to be affected by the compromise or arrangement.

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1. Scheme that restructures or varies the debt obligations of a company towards its creditors.
2. Related provisions have not been notified yet.
3. Merger includes merger by absorption or merger by formation of a new company.
   a. **Merger by absorption:** Where the undertaking, property and liabilities of one or more companies, including the company in respect of which the compromise or arrangement is proposed, are to be transferred to another existing company, it is a merger by absorption.
   b. **Merger by formation of a new company:** Where the undertaking, property and liabilities of two or more companies, including the company in respect of which the compromise or arrangement is proposed, are to be transferred to a new company, whether or not a public company, it is a merger by formation of a new company.
4. Where the undertaking, property and liabilities of the company in respect of which the compromise or arrangement is proposed are to be divided among and transferred to two or more companies each of which is either an existing company or a new company, such a scheme involves division.

A period of 30 days has been provided to the above mentioned authorities to make a representation on the proposed scheme and if no such response is received, it would be presumed that they have no representations.

Notice to statutory authorities is not required in case of merger/amalgamation between parent and its wholly-owned subsidiary or two or more small companies.

- **Exemption from meeting:** In case a scheme of compromise/arrangement has been approved by the creditors/class of creditors with at least 90 per cent value, NCLT could dispense with calling of a meeting of such creditors/class of creditors.
- **Voting on the scheme:** Person in receipt of notice can vote on a proposed scheme either in person, through proxies or through electronic means within one month from the date of receipt of notice.
- **Objection to the scheme:** An arrangement could be objected only by a person holding at least 10 per cent shareholding or 5 per cent debt as per the latest audited financial statements.
- **Auditor's certificate on compliance with AS:** A scheme would not be sanctioned unless an auditor's certificate to the effect that the accounting treatment specified in the scheme is in conformity with the prescribed Accounting Standards (AS) has been filed with the NCLT.
- **Approval of the scheme:** A scheme of compromise or arrangement approved by creditors/members representing three-fourths in value and sanctioned by the NCLT (by an order) would be binding on the company, its creditors/members, its contributories and on the liquidator (in case of winding up).
- **Order of the NCLT:** An order of the NCLT approving the scheme should, *inter alia,* provide an option to preference shareholders (where the scheme provides for conversion of preference shares into equity shares) to obtain arrears of dividend in cash or accept equity shares equal to the value of the dividend payable and exit offer to dissenting shareholders.

  Such an order should be filed with the ROC within 30 days of the receipt of the order by the company.
- **No shares in own name:** No shares should be held by the transferee companies in its own name or in the name of any trust. Any such shares, if held, should be cancelled or extinguished.
- **Amalgamation between listed and unlisted companies:** In case of amalgamation of a listed transferor company into an unlisted transferee company, unlisted transferee company should remain unlisted (unless it becomes listed) and should provide for payment of value of shares held by dissenting shareholders.
- **Order of winding up:** NCLT has the power to supervise the implementation of the approved compromise or arrangement. If it is satisfied that the scheme could not be implemented with/without modification and the company is unable to pay its debts as per the scheme, then it could order winding up of such a company.
- **Appointed date:** In case of merger/amalgamation between companies, the scheme should indicate an appointed date from which the scheme would be deemed to be effective.

  It is important to note that as per requirements of Ind AS 103, *Business Combinations,* an acquirer needs to identify the acquisition date which is the date on which it obtains control of the acquiree. Such a date is generally the closing date on which the acquirer legally transfers the consideration, acquires the assets and assumes the liabilities of the acquiree.

  However, an acquirer could obtain control on a date earlier or later than the closing date (e.g. a written agreement provides that the acquirer obtains control of the acquiree on a date before closing date).

  The Ind AS Transition Facilitation Group (ITFG) of the Institute of Chartered Accountants of India (ICAI) has issued its clarifications bulletin 12[5] on issues relating to implementation of Indian Accounting Standards (Ind AS). In the bulletin, it, *inter alia,* considered a situation where pursuant to a court scheme, a company gets merged with another company with an appointed date approved by the NCLT (as 1 April 2016) and the companies would prepare their first Ind AS financial statements for the year ending 31 March 2018.

5. ICAI - ITFG clarification bulletin 12 dated 23 October 2017.

In the above situation, ITFG clarified that if the NCLT approves the scheme with a different appointed date as compared to the acquisition date as per Ind AS 103, then the appointed date approved by the NCLT would be considered as the acquisition date for business combinations. The company would be required to provide appropriate disclosures and the auditor would need to consider the requirements of relevant AS.

The above ITFG view would be applicable both for, business combinations under common control as well as business combinations not under common control.

- **Yearly statement of compliance:** A statement (in Form No. CAA.8) confirming implementation of the scheme in accordance with the order to be submitted with the ROC within 120 days from the end of each FY until the completion of the scheme, in case of merger/amalgamation between companies.

### Merger or amalgamation of a company with a wholly-owned subsidiary or small companies[6] (Section 233)

The 2013 Act provides a simplified procedure for merger and amalgamation between:

- Holding company and its wholly-owned subsidiary
- Two or more 'small companies' or
- Such other prescribed class of companies.

Any such merger could be given effect to without the approval of the NCLT, subject to compliance with the specified procedures which, *inter alia,* includes the following:

a. Filing of a declaration of solvency with the ROC by each of the companies involved in the merger/ amalgamation in Form No. CAA.10

b. Approval of scheme by members holding at least 90 per cent of the total number of shares and by majority representing nine-tenth in value of the creditors of respective companies.

### Merger or amalgamation of a company with a foreign company (Section 234)[7]

A foreign company[8] incorporated outside India could merge with an Indian company or a company[9] could merge with a foreign company (incorporated in the specified jurisdictions) subject to the following:

- Prior approval of the RBI
- Ensure compliance with the above mentioned provisions of Sections 230 to 232 of the 2013 Act and the related Rules
- Transferee company should ensure that valuation is conducted by a registered valuer and is in accordance with internationally accepted principles on accounting and valuation. A declaration to this effect would be required to be attached with the application made to RBI for obtaining its approval.

Additionally, the terms and conditions of the scheme of merger could provide, among other things, for the payment of consideration to the shareholders of the merging company in cash, or in depository receipts, or partly in cash and partly in depository receipts, as the case may be, as per the scheme to be drawn up for the purpose.

The concerned company should file an application with the NCLT for approval of the merger after complying with the above mentioned conditions.

### Purchase of minority shareholding (Section 236)

The 2013 Act has introduced new provisions relating to buy-out of minority shareholding.

According to it, any person or group of persons holding 90 per cent of the issued equity share capital of a company by virtue of an amalgamation, share exchange, conversion of securities or for any other reason, could purchase the remaining equity shares of the company from minority shareholders at a price determined by a registered valuer in accordance with the prescribed rules.

Similarly, the minority shareholders of the company could also offer the majority shareholders to purchase the minority equity shareholding of the company.

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6. *Small company* means:
   a. A non-public company
   b. Not being a holding/subsidiary company, a company for charitable purposes or a company established under a special Act
   c. Having a paid-up share capital less than INR50 lakhs (amount can be prescribed up to INR5 crore) and turnover less than INR2 crore (amount can be prescribed up to INR20 crore).
7. Effective from 13 April 2017.
8. *Foreign company* means any company or body corporate incorporated outside India whether having a place of business in India or not.
9. Company incorporated under the 2013 Act or under any previous company law.

## Requirements of the Listing Regulations

The Listing Regulations prescribe following in relation to the schemes of arrangements undertaken by a listed company:

- **Filing of draft scheme of arrangement with the stock exchange (Regulation 37):** A listed entity that desires to undertake a scheme of arrangement (including with an unlisted entity) under the requirements of the 2013 Act is required to obtain a no objection letter or an observation letter from the stock exchange. No scheme of arrangement could be filed with the court or NCLT unless the listed entity has obtained an observation/no-objection letter from the stock exchange.

  Further, the validity of the observation/no-objection letter is six months from the date of issuance within which the draft scheme should be submitted to the court/NCLT for approval.

  The schemes of arrangement for merger of a wholly-owned subsidiary with the parent entity would not be required to be filed with SEBI (under the Listing Regulations). Such schemes should be filed with the stock exchanges for the purpose of disclosure.

- **Conditions for undertaking scheme of arrangement:** SEBI, through its various circulars, has laid down detailed requirements to be complied with by listed entities while undertaking schemes of arrangements. These, *inter alia,* includes the following:

  - **Scheme of arrangement with unlisted entities:** The percentage of shareholding of pre-scheme public shareholders of the listed entity and the Qualified Institutional Buyers (QIBs) of the unlisted entity, in the post scheme shareholding pattern of the merged entity should not be less than 25 per cent.

  - **Approval of shareholders to a scheme of arrangement:** Voting for approval of the scheme will be only through e-voting.

    Additionally, in certain cases, SEBI has mandated that a scheme of arrangement would be approved only if the votes cast by the public shareholders in favour of the proposal are more than the number of votes cast by the public shareholders against it. These, *inter alia,* includes schemes where parent listed entity has acquired equity shares of the subsidiary from shareholders of subsidiary and the subsidiary is being merged with the parent listed entity.

  - **Detailed compliance report:** Listed entities are required to submit a detailed compliance report (as per the prescribed format) confirming compliance with various regulatory requirements specified for schemes of arrangement and all AS with the stock exchange.

- **Requirements of stock exchanges to supersede the scheme (Regulation 11):** A listed entity is required to ensure that any scheme of arrangement/amalgamation/merger/reconstruction/reduction of capital, etc. presented to any court or NCLT should not violate, override or limit the provisions of securities law or requirements of the stock exchange.

  Such a provision is not applicable to the units issued by the listed mutual funds.

- **Disclosures (Regulation 30 read with Part A of Schedule III):** Every listed entity is required to disclose the scheme of arrangement (amalgamation/merger/demerger/restructuring) or any other restructuring to the stock exchange without application of the guidelines for materiality as such events are considered as deemed to be material.

### Recommendations of the Companies Law Committee (CLC) and the Companies (Amendment) Bill, 2017[11]

Sections 236 of the 2013 Act uses the term 'transferor company.' However, the term has not been defined in the Section.

Therefore, the CLC in its report dated February 2016 recommended that references to the phrase 'transferor company' in Section 236 should be modified to a 'company whose shares are being transferred' or alternatively, an explanation be provided in the provision clarifying that Section 236 only applies to the acquisition of shares.

Accordingly, the Companies (Amendment) Bill, 2017 proposed to amend Section 236 to substitute the words 'transferor company' with the words 'company whose shares are being transferred' for providing clarity.

10. SEBI circular no. CIR/CFD/CMD/16/2015 dated 30 November 2015, circular no. CFD/DIL3/CIR/2017/21 dated 10 March 2017 and circular no. CFD/DIL3/CIR/2017/105 dated 21 September 2017.

11. Passed by the Lok Sabha; assent of the Rajya Sabha is pending.

## Consider this

- No scheme of arrangement would be sanctioned unless an auditor's certificate to the effect that the accounting treatment specified in the scheme is in conformity with the prescribed AS has been filed with the NCLT.

  However, such certificate is not required in case of merger/amalgamation between parent and its wholly-owned subsidiary or two or more small companies. Approval of NCLT is also not required in such cases.

- Appointed date approved by the NCLT would be considered as the acquisition date for business combinations under Ind AS, in case NCLT approves an appointed date different from acquisition date.

- All listed entities are required to obtain observation/no-objection letter from stock exchange on the proposed scheme of arrangement before filing such scheme with the court/NCLT for approval. Guidelines issued by SEBI need to be adhered while undertaking the schemes of arrangements.

  Additionally, all schemes of arrangements should be disclosed to the stock exchanges as they are deemed to be material events/information under the Listing Regulations.