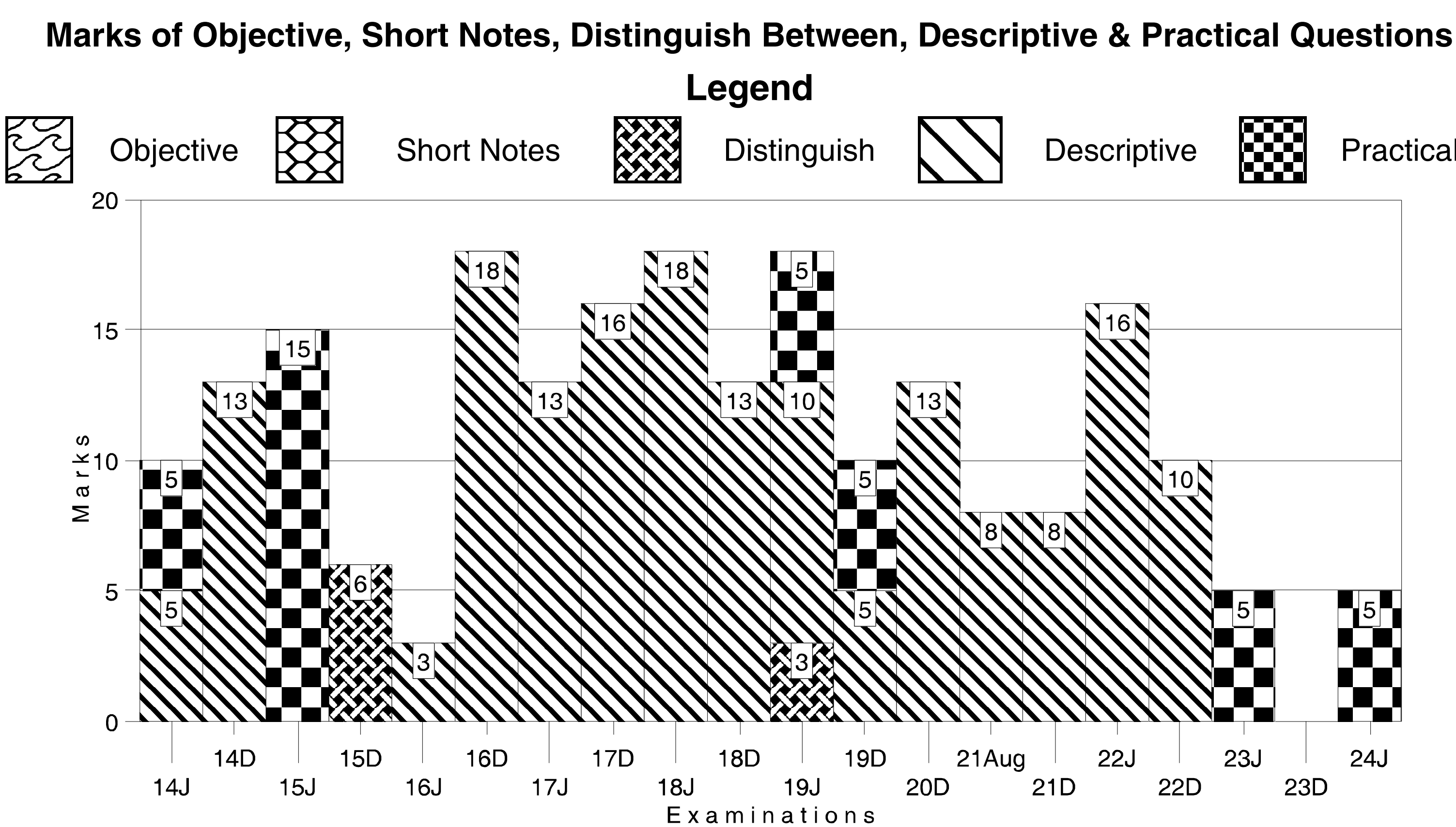

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1 TYPES OF CORPORATE RESTRUCTURING

THIS CHAPTER INCLUDES

1. Meaning of Corporate Restructuring
2. Historical Background
3. Need and Scope of Corporate Restructuring
4. Various Modes of Restructuring
5. Commonly applied tools of Corporate Restructuring
6. Planning, formulation and execution of various Restructuring Strategies
7. Financial Restructuring
8. Reduction of capital
9. Buy-Back

CHAPTER AT A GLANCE

Corporate Restructuring

Corporate restructuring is the process of significantly changing a company's business model, management team or financial structure to address challenges and increase shareholder value.

Corporate restructuring is an inorganic growth strategy.

Need and scope of Corporate restructuring

- To enhance shareholders value
- Orderly redirection of the firms activities
- Deploying surplus cash from one business to finance profitable growth in another
- Exploiting inter-dependence among present or prospective businesses
- Risk reduction
- Development of core-competencies
- To obtain tax advantages by merging a loss-making company with a profit-making company

- To have access to better technology
- To become globally competitive
- To increase the market share

Motives behind Corporate Restructuring

Financial:

- To reduce risk
- To increase operating efficiency
- To improve access to financial markets
- To obtain tax benefits

Others:

- To expand marketing and management capabilities
- To allow new products development
- To provide synergistic benefits
- To revive a sick company

Types of Restructuring

- **Financial restructuring -** Financial restructuring deals with restructuring of capital base and raising finance for new projects. Financial restructuring helps a firm to revive from the situation of financial distress without going into liquidation.
- **Market and Technological Restructuring -** Market Restructuring involves decisions with respect to the product market segments where the company plans to operate on its core competencies and technological restructuring occurs when a new technology is developed that changes the way an industry operates. Joint Venture, Strategic Alliances, Franchising are some of the examples of market and technological restructuring
- **Organisational Restructuring -** Organizational Restructuring involves establishing internal structures and procedures for improving the capability of the personnel in the organization to respond to changes.

Commonly applied tools of Corporate Restructuring
1. Mergers 2. Acquisitions 3. Amalgamation 4. Consolidations 5. Tender offers 6. Purchase of assets
Merger
A merger is a legal consolidation of two entities into one entity which can be merged together either by way of amalgamation or absorption or by formation of a new company. 'Merger' is the fusion of two or more companies, whereby the identity of one or more is lost resulting in a single company whereas 'Amalgamation' signifies the blending of two or more undertaking into one undertaking, blending enterprises loses its identity forming themselves into a separate legal identity.
Types of merger
Horizontal Merger - Horizontal Merger is a merger between companies selling similar products in the same market and in direct competition and share the same product lines and markets. It decreases competition in the market. The main objectives of horizontal merger are to benefit from economies of scale, reduce competition, achieving monopoly status and control of the market. **Vertical Merger -** Vertical Merger is a merger between companies in the same industry, but at different stages of production process. In another words, it occurs between companies where one buys or sells something from or to the other. **Conglomerate Merger -** Conglomerate merger is a merger between two companies that have no common business areas. It refers to the combination of two firms operating in industries unrelated to each other.

Congeneric Merger - Congeneric merger is a merger between two or more businesses which are related to each other in terms of customer groups, functions or technology e.g., combination of a computer system manufacturer with a UPS manufacturer.

Acquisition

Acquisition occurs when one entity takes ownership of another entity's stock, equity interests or assets. It is the purchase by one company of controlling interest in the share capital of another existing company. Even after the takeover, although there is a change in the management of both the firms, companies retain their separate legal identity. The companies remain independent and separate; there is only a change in control of the companies. When an acquisition is 'forced' or 'unwilling', it is called a takeover.

Difference between a Merger and an Acquisition

A merger occurs when two separate entities, usually of comparable size, combine forces to create a new, joint organization in which both are equal partners whereas an acquisition refers to the purchase of one entity by another (usually, a smaller firm by a larger one)

In Merger old company cease to exist and a new company emerges whereas in acquisition a new company does not emerge Merger requires two companies to consolidate into a new entity with a new ownership and management Structure whereas acquisition occurs when one company takes over all of the operational management decisions of another If the takeover is friendly, it is called merger. If the takeover is hostile, it is called as an acquisition

Amalgamation

Amalgamation is defined as the combination of one or more companies into a new entity. It includes:

(i) Two or more companies join to form a new company

(ii) Absorption or blending of one by the other

Consolidation
A consolidation creates a new company. Stockholders of both companies approve the consolidation, and subsequent to the approval, receive common equity shares in the new firm.
Tender Offer
One company offers to purchase the outstanding stock of the other firm at a specific price.
Acquisition of Assets
In a purchase of assets, one company acquires the assets of another company.
Management Buyout
A management buyout (MBO) is a transaction where a company's management team purchases the assets and operations of the business they manage.
Demerger
It is a business strategy in which a single business is broken into components, either to operate on their own, to be sold or to be dissolved. A demerger allows a large company, such as a conglomerate, to split off its various brands to invite or prevent an acquisition, to raise capital by selling off components that are no longer part of the business's core product line, or to create separate legal entities to handle different operations. Demerger is an arrangement whereby some part / undertaking of one company is transferred to another company which operates completely separate from the original company. Shareholders of the original company are usually given an equivalent stake of ownership in the new company.

Types of Demerger

Divestiture - Divestiture means selling or disposal of assets of the company or any of its business undertakings/divisions, usually for cash

Spin-offs - The shares of the new entity are distributed to the shareholders of the parent company on a pro-rata basis.

Splits/divisions - Splits involve dividing the company into two or more parts with an aim to maximize profitability by removing stagnant units from the mainstream business. Splits can be of two types, Split-ups and Split-offs.

Equity Carve-Outs - Equity carve-outs are referred to a percentage of shares of the subsidiary company being issued to the public.

Slump Sale

The transfer of the undertaking concerned as going concern is called "Slump sale". Slump sale is one of the methods that are widely used in India for corporate restructuring where the company sells its undertaking.

The main reasons of slump sale are generally undertaken in India due to following reasons:

- It helps the business to improve its poor performance.
- It helps to strengthen financial position of the company.
- It eliminates the negative synergy and facilitates strategic investment.
- It helps to seek tax and regulatory advantage associated with it.

Business Sale / Divestiture

Divestiture means selling or disposal of assets of the company or any of its business undertakings/ divisions, usually for cash (or for a combination of cash and debt) and not against equity shares to achieve a desired objective, such as greater liquidity or reduced debt burden. Divestiture is normally used to mobilize resources for core business or businesses of the company by realizing value of non-core business assets.

Joint Venture

A joint venture (JV) is a business or contractual arrangement between two or more parties which agree to pool resources for the purpose of accomplishing a specific task may be a new project or any other business

activity. In a joint venture (JV), each of the participants is responsible for profits, losses and costs associated with it. Company enters into a joint venture when it lacks required knowledge, human capital, technology or access to a specific market that is necessary to be successful in pursuing the project on its own. **Equity-** based joint ventures is a type of joint venture in which two or more parties set-up a separate legal company to act as the vehicle for carrying out the project. **Non-equity** joint ventures also known as cooperative agreements, seek technical service arrangements, franchise, brand use agreements, management contracts, rental agreements, or one-time contracts, e.g., for construction projects, non-equity arrangements in which some companies are in need of technical services or technological expertise than capital.
Strategic Alliance
Strategic alliance is an arrangement between two companies that have decided to share resources to undertake a specific, mutually beneficial project. It is an excellent vehicle for two companies to work together profitably. It can help companies develop and exploit the unique strengths. Organizations get an opportunity to widen customer base or utilize the surplus capacity.
Reverse Merger
A reverse merger is a merger in which a private company becomes a public company by acquiring it. It saves a private company from the complicated process and expensive compliance of becoming a public company. Instead, it acquires a public company as an investment and converts itself into a public company. However, there is another angle to the concept of a reverse merger. When a weaker or smaller company acquires a bigger company, it is a reverse merger. In addition, when a parent company merges into its subsidiary or a loss-making company acquires a profit-making company, it is also termed as a reverse merger.

The reason for reverse merger are: • To carry forward tax losses of the smaller firm, this allows the combined entity to pay lower taxes. Tax savings under Income Tax Act, 1961. • Economies of scale of production • Marketing network • To protect the trademark rights, licence agreements, assets of small/loss making company
Financial Restructuring
Corporate financial restructuring is any substantial change in a company's financial structure, or ownership or control, or business portfolio, designed to increase the value of the firm, i.e., debt and equity restructuring. Internal reconstruction of a company is the simplest form of financial restructuring.
Debt Restructuring
It involves a reduction of debt and an extension of payment terms or change in terms and conditions, which is less expensive. It is nothing but negotiating with bankers, creditors, vendors. It is the process of reorganizing the whole debt capital of the company. It involves the reshuffling of the balance sheet items as it contains the debt obligation of the company. Debt capital of the company includes secured long term borrowing, unsecured long-term borrowing, and short term borrowings.
Equity Restructuring
It is a process of reorganizing the equity capital. It includes a reshuffling of the shareholders capital and the reserves that are appearing on the balance sheet. Restructuring equity means changing how the firm's residual cash flows are divided and distributed among the firms shareholders, with the goal of increasing the overall market value of the firms common stock. The following comes under equity restructuring: • Alteration of share capital • Reduction of share capital • Buy-back of shares

Alteration of Share capital
Alteration of share capital means increase or decrease in or rearrangement of share capital as permitted in Articles of Association. Five ways of alteration of share capital: • increase its authorised share capital by such amount as it thinks expedient • consolidate and divide all or any of its share capital into shares of a larger amount than its existing shares • convert all or any of its fully paid-up shares into stock, and reconvert that stock into fully paid-up shares of any denomination • sub-divide its shares, or any of them, into shares of smaller amount • cancel shares which, at the date of the passing of the resolution in that behalf, have not been taken or agreed to be taken by any person
Reduction of Share Capital
Capital Reduction is the process of decreasing a company's shareholder's equity through share cancellations and share repurchases. The reduction of share capital means reduction of issued, subscribed and paid up share capital of the company.
Modes of Reduction of Capital
A company limited by shares or a company limited by guarantee and having a share capital may, if authorised by its articles, by special resolution, and subject to its confirmation by the Tribunal on petition, reduce its share capital in any way and in particular: (a) extinguish or reduce the liability on any of its shares in respect of the share capital not paid-up; or (b) either with or without extinguishing or reducing liability on any of its shares,— (i) cancel any paid-up share capital which is lost or is unrepresented by available assets; or (ii) pay off any paid-up share capital which is in excess of the wants of the company, Reduction of capital without sanction of the Tribunal

The following are cases which amount to reduction of share capital but where no confirmation by the Tribunal is necessary: 1. **Surrender of shares –** "Surrender of shares" means the surrender of shares already issued, to the company, by the registered holder of shares. 2. **Forfeiture of shares –** A company may if authorised by its articles, forfeit shares for non-payment of calls and the same will not require confirmation of the Court. 3. **Diminution of capital –** Where the company cancels shares which have not been taken or agreed to be taken by any person . 4. Redemption of redeemable preference shares. 5. Buy-back of its own shares. **Creditors' right to object to reduction -** The creditors having a debt or claim admissible in winding-up are entitled to object. To enable them to do so, the Tribunal will settle a list of creditors entitled to object. **Confirmation and registration -** Section 66(3) of the Companies Act, 2013 states that if the Tribunal is satisfied that either the creditors entitled to object have consented to the reduction, or that their debts have been determined, discharged, paid or secured, it may confirm the reduction of share capital on such terms and conditions as it deems fit.
Conclusiveness of certificate for reduction of capital - Where the Registrar had issued his certificate confirming the reduction, the same was held to be conclusive although it was discovered later that the company had no authority under its articles to reduce capital [Re Walkar & Smith Ltd., (1903) 88 LT 792 (Ch D)]. Similarly, in a case where the special resolution for reduction was an invalid one, but the company had gone through with the reduction, the reduction was not allowed to be upset [Ladies's Dress Assn. v. Pulbrook, (1900) 2 QB 376].
Buy-Back
According to Section 68(1) of the Companies Act, 2013, a company whether public or private, may purchase its own shares or other specified securities (hereinafter referred to as "buy-back") out of:

(i) its free reserves; or (ii) the securities premium account; or (iii) the proceeds of any shares or other specified securities.
Modes of Buy-Back
Tender Offer In tender offer, the company makes an offer to buy a certain number of shares/securities at a specific price directly from security holders on proportionate basis. **Open Market Purchase** In open market purchase, the company acquires a certain number of shares. Fixes a price cap and buy for any price up to the upper limit.
Advantages of buy-back
• It is an alternative mode of reduction in capital without requiring approval of the National Company Law Tribunal • To improve the earnings per share • To improve return on capital, return on net worth and to enhance the long-term shareholders value • To provide an additional exit route to shareholders when shares are undervalued or thinly traded • To enhance consolidation of stake in the company • To prevent unwelcome takeover bids • To return surplus cash to shareholders • To achieve optimum capital structure • To support share price during periods of sluggish market condition • To serve the equity more efficiently.
Legal provisions for Buy-Back
• The primary requirement is that the articles of association of the company should authorise buy-back. • Board of directors can approve buy-back up to 10% of the total paid-up equity capital and free reserves of the company and such buyback has to be authorized by the board by means of are solution passed at the meeting.

- Shareholders by a special resolution can approve buy-back up to 25% of the total paid-up capital and free reserves of the company. In respect of any financial year, the shareholders can approve by special resolution up to 25% of total equity capital in that year.
- The ratio of the aggregate of secured and unsecured debts owed by the company after buy-back should not be more than twice the paid-up capital and its free reserves i.e. the ratio shall not exceed 2:1.
- No offer of buy-back under this sub-section shall be made within a period of one year reckoned from the date of the closure of the preceding offer of buy-back, if any.
- The notice of the meeting at which the special resolution is proposed to be passed shall be accompanied by an explanatory statement stating full and complete disclosure of all material facts
- Filing Declaration of Solvency with SEBI/ROC
- The offer for buy-back shall remain open for a period of not less than15 days and not exceeding 30 days from the date of dispatch of the letter of offer
- Payment of consideration/returning of share certificates – within 7 days
- Every buy-back shall be completed within a period of one year from the date of passing of the special resolution, or as the case may be, the resolution passed by the Board.
- When a company completes a buy-back of its shares or other specified securities it shall not make a further issue of the same kind of shares or other securities including allotment of new shares under clause (a) of sub-section (1) of Section 62 or other specified securities within a period of six months except by way of a bonus issue or in the discharge of subsisting obligations such as conversion of warrants, stock option schemes, sweat equity or conversion of preference shares or debentures into equity shares.
- A company shall, after the completion of the buy-back under this section, file with the Registrar and the Securities and Exchange Board (incase of listed companies) a return containing such particulars relating to the buy-back within thirty days

Circumstances prohibiting buy back
Under Section 70 of the Companies Act, 2013, no company shall directly or indirectly purchase its own shares or other specified securities— (i) through any subsidiary company including its own subsidiary companies; (ii) through any investment company or group of investment companies; or (iii) if a default, is made by the company, in the repayment of deposits accepted either before or after the commencement of this Act. However, the buy-back is not prohibited, if the default is remedied and a period of three years has lapsed after such default ceased to subsist.
Income tax Aspect on buy back
Section 46A of the Income-tax Act,1961 provides that any consideration received by a security holder from any company on buy back shall be chargeable to tax on the difference between the cost of acquisition and the value of consideration received by the security holder as capital gains.
Buy-Back procedure for Listed Securities
All the listed companies are required to comply with SEBI (Buy Back of Securities) Regulations, 2018, in addition to the provisions of the Companies Act, 2013. These regulations broadly cover the following aspects: 1. Special resolution and its additional disclosure requirements. 2. Methods of buy back including buy back through reverse book building, from existing shareholders through tender offer, etc. 3. Filing of offer documents, public announcement requirements. 4. Offer procedure/opening of escrow account, etc. 5. General obligations of company, merchant banker, etc.
Methods of Buy-Back
According to Regulation 4 of the Regulations, a company may buy back its own shares or other specified securities by any one of the following methods:

(a) from the existing shareholders or other specified securities holders on a proportionate basis through the tender offer; (b) from the open market through: (i) book-building process (ii) stock exchange (c) from odd-lot holders.
Escrow account for Buy-Back
(a) the company shall, as and by way of security for performance of its obligations under the Regulations, on or before the opening of the offer, deposit in an escrow account the sum as specified in clause (b) (b) the escrow amount shall be payable in the following manner: (i) if the consideration payable does not exceed ₹100 crores —25 per cent of the consideration payable; (ii) if the consideration payable exceeds ₹100 crores —25 percent upto ₹100 crores and10 percent there after;
Extinguishing of bought-back securities (Regulation11)
The company shall extinguish and physically destroy the security certificates so bought back in the presence of a Registrar to issue or the Merchant Banker and the Statutory Auditor within fifteen days of the date of acceptance of the shares or other specified securities. The company shall also ensure that all the securities bought-back are extinguished within seven days of expiry of buy-back period.

DISTINGUISH BETWEEN

2015 - Dec [3] (b) Distinguish between 'demerger' and 'slump sale'.

(6 marks)

Answer:

Demerger: As per the Rules made under the Companies Act, 'demerger' in relation to companies means transfer, pursuant to scheme of arrangement by a 'demerged company' of its one or more undertakings to any 'resulting company' in such a manner as provided in Section 2(19AA) of the Income Tax Act, 1961, subject to the shares being allotted by the 'resulting company' to the shareholders of the 'demerged company' against the transfer of assets and liabilities. Section 232 deals with mergers and amalgamation including demergers.

Slump Sale: Slump sale means the transfer of one or more undertaking as a result of the sale for a *lump sum* consideration without value being assigned to the individual assets and liabilities in such sales.

Both demerger and slump sale results in having of a division or undertaking, but there are various differences which are as follows:

1. In case of slump sale, values are not assigned to individual assets and liabilities and the sale, of undertaking is for a *lump sum* consideration. Whereas in demerger, valuation of individual assets and liabilities are mandatory.
2. In case of demerger, the resulting company have to continue the business of transferred undertaking of demerged company, while it is not so in the case of slump sale.
3. Demerger unlike slump sale results into reorganization of capital.
4. In case of demerger, the shareholders of demerged company have to be issued shares of resulting company whereas in case of slump sale, the issue of shares does not take place.
5. In slump sale through amalgamation and merger, Ind AS 103 will be applicable.

2019 - June [3] (b) Distinguish between merger and an acquisition (any *three* points). **(3 marks)**

Answer:

Merger	Acquisition
1. A merger occurs when two separate entities combine forces to create a new joint organization in which both are equal partners.	An acquisition refers to the purchase of one entity by another.

2. Old company cease to exist and a new company emerges.	A new company does not emerge.
3. It requires two companies to consolidate into a new entity with a new ownership and management structure.	It occurs when one company takes over all of the operational management decisions of another.
4. A transaction legally structured as a merger may give each party's shareholders partial ownership and control of combined enterprise.	A transaction legally structured as an acquisition may have the effect of placing one party's business under the indirect ownership of the other party's shareholders.

DESCRIPTIVE QUESTIONS

2012 - June [1] (b) What is meant by 'strategic alliance' and what are its features?

(c) "A conglomerate merger is neither a type of horizontal merger nor a vertical merger." Discuss. **(5 marks each)**

Answer:

(b) Strategic alliance is a relationship between two or more parties to pursue a set of agreed upon goals or to meet a critical businesses need while continuing to remain independent organisation.

Some of the features of strategic alliance are as follows:-

(i) It aims for a synergy where each partner hopes that the benefits from the alliance will be greater than those from individual efforts.

(ii) Alliance often involves technology transfer, economic specialisation, shared expenses, reduction in cost, etc.

(iii) It is gaining importance in infrastructure sectors.

(iv) Strategic alliance aims at pooling the resources and facilitating innovative ideas and techniques while implementing large projects.

(v) It could help company to develop a more effective process, expand into a new market or develop an advantage over a competitor, among other possibilities.

(c)
- Conglomerate merger is a merger between firms that are involved in totally unrelated business activities.
- The companies, which are merged are neither competitors nor complementaries.
- The business of these companies are neither horizontally nor vertically related to each other.
- Merging companies operate in unrelated markets.
- Conglomerate mergers are merger of different kinds of businesses under one flagship company.
- Thus conglomerate merger is neither a type of horizontal merger nor a vertical merger.

2012 - Dec [1] (c) As per the provisions of the Companies Act, 2013 and the Income-tax Act, 1961 there is no difference between de-merger and slump sale; though it results in separation of a division or unit of an existing company to a potential buyer. But in common parlance, it means rightward and leftward, *i.e.*, totally different approach from one to another. The first requires no payment but second requires down payment. But the ultimate objective is to hive off some business which is not compatible with the core business competency of the main company.
Discuss the eventuality in conjunction with the provisions of the Income-tax Act, 1961. **(5 marks)**

Answer:

Demerger:

Section 2(19AA) prescribes certain conditions to be fulfilled, for demerger, which are as below :

(i) all the property of the undertaking, being transferred by the demerged company, immediately before the demerger, becomes the property of the resulting company by virtue of the demerger;

(ii) all the liabilities relatable to the undertaking, being transferred by the demerged company, immediately before the demerger, become the liabilities of the resulting company by virtue of the demerger;

(iii) the property and the liabilities of the undertaking or undertakings being transferred by the demerged company are transferred at values appearing in its books of account immediately before the demerger;

(iv) the resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged company on a proportionate basis except where the resulting company itself is a shareholder of the demerged company;

(v) the shareholders holding not less than three-fourths in value of the shares in the demerged company (other than shares already held therein immediately before the demerger, or by a nominee for, the resulting company or, its subsidiary) become share-holders of the resulting company or companies by virtue of the demerger, otherwise than as a result of the acquisition of the property or assets of the demerged company or any undertaking thereof by the resulting company;

(vi) the transfer of the undertaking is on a going concern basis;

(vii) the demerger is in accordance with the conditions, if any, notified under sub-section (5) of section 72A by the Central Government in this behalf.

Slump Sale:

Slump sale means the transfer of one or more undertaking as a result of the sale for a *lump sum* consideration without values being assigned to the individual assets and liabilities in such sales.

Both demerger and slump sale results in hiving off a division or undertaking, but there are various differences which are as follows:

1. In case of slump sale, values are not assigned to individual assets and liabilities and the sale, of undertaking is for a *lump sum* consideration. Whereas in demerger, valuation of individual assets and liabilities are mandatory.
2. In case of demerger, the resulting company have to continue the business of transferred undertaking of demerged company, while it is not so in the case of slump sale.
3. Demerger unlike slump sale results into reorganization of capital.
4. In case of demerger, the shareholders of demerged company has to be issued shares of resulting company and in case of slump sale, the issue of shares does not take place.

2013 - June [1] (a) "Corporate restructuring aims to achieve certain predetermined objectives at corporate level." Comment and explain how corporate restructuring would help bringing an edge over competitors.

(b) "In the modern business world, the strategic alliance and joint venture both have the same objective and end result, i.e., pooling of resources, technologies and expertise, etc. to increase the market share, to enter into a new business and so on." Comment on this statement highlighting the basic differences between the two. **(5 marks each)**

Answer:

(a)
- 'Corporate Restructuring' is a term of wider importance and covers, in its ambit, the restructuring or reorganizing or financial restructuring of any organisation done in order to operate more effectively and efficiently.
- **Objective of corporate restructuring:**
  - Re - direction of the company and activities.
  - Risk reduction.
  - Deploying surplus cash from one business to another business.
  - Development of core-competencies.
- Corporate restructuring helps in bringing an edge over competitor. It aims at exploiting the strategic assets accumulated by a business i.e. natural monopolies, goodwill, etc.
- In order to drive a competitive force, corporate restructuring strategies such as merger and acquisitions exercise could be taken up that would bring an edge over competitors.

(b) Strategic Alliance:
- Alliance means an agreement between two or more organisation to cooperate with each other to accomplish their common goals and to strive for the benefits of both of them.
- It is an understanding between firms whereby resources capabilities and core competencies are combined to pursue mutual interests.

Joint Venture:
- Joint venture is a venture in which an enterprise is formed with participation in the ownership, control and management of minimum of two parties.

- In joint venture, a business enterprise is formed for profit in which parties of joint venture share responsibilities in an agreed manner, by providing risk capital, technology, trade mark & access to market, etc.

2013 - Dec [4] (a) Explain the provisions of buy-back under the Companies Act, 2013 with reference to Board resolution and shareholders' resolution. What is the maximum quantum of buy-back allowed under the Act?

(9 marks)

Answer:

Board Resolution for Buy-Back of Shares:

Section 68(2) of Companies Act, 2013 specifically provides the maximum quantum of the buy back of securities through board resolution and special resolution.

- The board can authorise the buy-back of securities not exceeding 10% of the total paid-up equity capital and free reserves of the company.
- The resolution authorising buy-back should be passed at a meeting of the Board.
- Such resolution can not be passed by circulation or at a meeting of a committee of the Board.

Shareholders Resolution for Buy-Back of Shares:

- Special resolution is required to be passed by the shareholders.
- By passing special resolution, the shareholders can authorize the buy-back of securities not exceeding 25% of the total paid-up capital and free reserves of the company in that financial year.
- Unlisted company should obtain shareholder's approval by passing the special resolution only at a duly convened general meeting.
- Listed company should obtain approval by postal ballot.

Maximum quantum of buy-back.

The following points are important for understanding the maximum quantum of buy-back:

- A company cannot buy-back more than 25% of its total paid-up capital and free reserves.
- Buy-back of equity shares in any financial year should not exceed 25% of the total paid-up equity capital of the company.

- By passing a board resolution, the Board can authorize the buy-back of securities not exceeding 10% the total paid-up equity capital and free reserves of the company.

Note:
- *The aforesaid limit is to be applied not to the number of securities to be bought back but to the amount required for buy-back of such securities.*
- *A company may buy-back its entire (i.e. 100%) securities other than equity shares, viz. preference shares and any other securities as may be notified by the Central Government from time to time, in a financial year, subject to the overall limit of 25% of the total paid-up capital and free reserves of the company.*

2014 - June [2A] (Or) (i) What is the legal protection available to creditors for protecting their interest in case of reduction of capital proposed by the company? **(5 marks)**

Answer:
- After passing the special resolution for the reduction of capital, the company is required to apply to the Tribunal by way of petition for the confirmation of the resolution.
- Where the proposed reduction of share capital involves either (i) diminution of liability in respect of unpaid share capital, or (ii) the payment to any shareholder of any paid-up share capital, or (iii) in any other case, if the Tribunal so directs, the following provisions shall have effect:

  The creditors having a debt or claim admissible in winding up are entitled to object. To enable them to do so, the Tribunal will settle a list of creditors entitled to object. If any creditor objects, then either his consent to the proposed reduction should be obtained or he should be paid off or his payment be secured. The Tribunal, in deciding whether or not to confirm the reduction will take into consideration the minority shareholders and creditors.

2014 - Dec [2] (a) ABC Ltd. has completed buy-back of equity shares on 30^{th} April, 2014. The company desires to make further issue of equity shares on 31^{st} August, 2014. Can the company proceed and allot further equity shares on 31^{st} August, 2014 assuming that all other requirements are complied with or will be complied with?
Will your answer be different, if the company desires to issue and allot on the very same day (i.e., 31^{st} August, 2014), preference shares instead of equity shares assuming that all other requirements are complied with or will be complied with? **(5 marks)**

Answer:

- In the given case, ABC Ltd. has completed buy-back of equity shares on 30^{th} April, 2014.
- The company desires to make further issue of equity shares on 31^{st} August, 2014.
- According to the provisions of Section 68(8) of Companies Act, when a company completes a buy-back of its shares or other specified securities it shall not make a further issue of the same kind of shares or other securities including allotment of new shares within a period of six months except by way of a bonus issue or in the discharge of subsisting obligations such as conversion of warrants, stock option schemes, sweat equity or conversion of preference shares or debentures into equity shares.
- As the six months is not over from the date of completion of buy-back, it cannot proceed and allot further equity shares on 31^{st} August, 2014.

Here the words "kind" and "Other" are very important, Kind must be understood as per **Section 43. Section 43** says a company can have two kinds of shares (a) Equity shares (b) Preference shares. So company can issue preference shares on 31^{st} August, 2014 being not the same kind of shares.

2014 - Dec [2A] (Or) (iii) Explain the concept of 'vertical merger' and differentiate between 'forward integration' and 'backward integration'.
(5 marks)

Answer:

Vertical Merger:

- Vertical Merger is one of the types of Merger.
- It is a merger which takes place upon the combination of two companies which are operating in the same industry but at different stages of production or distribution system.
- Vertical merger provides a way for total integration to those firms which are striving for owning of all phases of the production schedule together with the marketing network.

Forward Integration:

Forward integration may result if a company decides to take over the retailer or Customer Company.

Backward Integration:

If a company takes over its supplier/producers of raw material, then it may result in backward integration of its activities.

2014 - Dec [3] (d) Good Earth Pvt. Ltd. wants to become a public listed company without opting for initial public offer (IPO). What is the best strategy available for the company? Distinguish the same from 'strategic alliance'. **(3 marks)**

Answer:

Reverse merger is the opportunity for the unlisted companies to become public listed company, without opting for Initial Public offer (IPO). In this process the private company acquires the majority shares of public company, with its own name.

Strategic Alliance: Any agreement between two or more parties to collaborate with each other, in order to achieve certain objectives while continuing to remain independent organizations is called strategic alliance.

2016 - June [1] (b) Comment on the following:

(i) No offer of buy-back shall be made within a period of 180 days from the date of Board Meeting or meeting of shareholders, as the case may be, in respect of the preceding offer of buy-back. **(3 marks)**

Answer:

As per Section 68(2) of the Companies Act, 2013 no offer of buy-back under this sub section shall be made within a period of one year reckoned from the date of the closure of the preceding offer of buy-back, if any.

So period to be calculated from the date of the closure of the preceding offer of buy-back.

2016 - Dec [1] (a) "Corporate restructuring aims at different things at different times for different companies but the single common objective in every restructuring exercise is to eliminate the disadvantages and combine the advantages." Comment on the statement highlighting various needs for undertaking corporate restructuring. **(5 marks)**

(b) What do you understand by 'over- capitalised' company? Discuss the corrective measures required to be undertaken by an over-capitalised company. **(5 marks)**

Answer:

(a) The various needs for undertaking a Corporate Restructuring exercise are as follows:

(i) To focus on core strengths, operational synergy and efficient allocation of managerial capabilities and infrastructure.

(ii) Consolidation and economies of scale by expansion and diversion to exploit extended domestic and global markets.

(iii) Revival and rehabilitation of a sick unit by adjusting losses of the sick unit with profits of a healthy company.

(iv) Acquiring constant supply of raw materials and access to scientific research and technological developments.

(v) Capital restructuring by appropriate mix of loan and equity funds to reduce the cost of servicing and improve return on capital employed.

(vi) Improve corporate performance to bring it at par with competitors by adopting the radical changes brought out by information technology.

(b) A company is said to be over-capitalized, if its earnings are not sufficient to justify a fair return on the amount for share capital and debentures that have been issued. Otherwise, it is said to be over capitalized when total of owned and borrowed capital exceeds its fixed and current assets i.e. when it shows accumulated losses on the assets side of the balance sheet.

Steps of restructuring by over-capitalised company

- Buy-back of shares by a company as per the provisions of **Companies Act, 2013.**
- Paying back surplus share capital to shareholders.
- Repayment of loans.
- Repayment of fixed deposits.
- Redemption of debentures

2016 - Dec [2] (b) Elucidate the obligations of a merchant banker as per Regulation 25 of SEBI (Buy - back of Securities) Regulations, 2018.

(5 marks)

Answer:

Regulation 20 provides that the merchant banker should ensure that:

(a) the company is able to implement the offer;

(b) the provision relating to escrow account has been made;

(c) firm arrangements for monies for payment to fulfil the obligations under the offer are in place;

(d) the public announcement of buy-back is made and the letter of offer has been filed in terms of the Regulations;

(e) the merchant banker should furnish to SEBI, a due diligence certificate which should accompany the draft letter of offer;

(f) the merchant banker should ensure that the contents of the public announcement of offer as well as the letter of offer are true, fair and adequate and quoting the source wherever necessary;

(g) the merchant banker should ensure with compliance **Section 68 of Companies Act, 2013,** and **Section 70 of Companies Act, 2013** and any other applicable laws or rules in this regard;

(h) upon fulfillment of all obligations by the company under the Regulations, the merchant banker should inform the bank with whom the escrow or special amount has been deposited to release the balance amount to the company and send a final report to SEBI in the specified form, within 15 days from the date of closure of the buy-back offer.

2016 - Dec [3] Comment on the following:

(b) Circumstances which prohibit buy-back of shares or other specified securities under the Companies Act, 2013. **(3 marks)**

Answer:

Under Section 70 of the Companies Act, 2013, no company shall directly or indirectly purchase its own shares or other Securities:

- through any subsidiary company including its own subsidiary companies;
- through any investment company or group of investment companies.
- if a default, is made by the company, in repayment of deposits accepted either before or after the commencement of the Act, interest payment thereon to any financial institution or banking company. However, the buy-back is not prohibited, if the default is remedied and a period of three years has lapsed-after such default ceased to subsist.
- No company shall, directly or indirectly, purchase its own shares or other specified securities in case such company has not complied with the provision of **Section 92** (Annual Return), **123** (Declaration of Dividend), **127** (Punishment for failure to distribute dividend) and **Section 129** (Financial Statement).

2017 - June [1] (a) "Measuring the shareholders' value" is the objective of Good Corporate Governance. Comment on the statement, how buy back of shares achieves it. **(5 marks)**

(c) Discuss "Strategic Alliance" and "Joint Venture" as corporate restructuring strategies. **(5 marks)**

Answer:

(a)
- Corporate Governance is the application of best management practices, compliance of law in true letter and spirit and adherence to ethical standards for effective management and distribution of wealth and discharge of social responsibility for sustainable development of all stakeholders.
- Shareholder value is the value delivered to shareholders because of management's ability to grow sales, earnings and free cash flow over time and which depended upon good strategic decisions by the board of the directors of the company that invest the shareholders money into profitable projects that creates healthy returns.

- If this value is created over the long term, the share price increases and the company can pay larger cash dividends to shareholders.
- But this is possible when there is effective and good corporate governance in the company.
- Thus the main objective of good corporate governance is always to measure and increase the ultimate shareholder's value.
- Buy back of securities is governed by **Sec. 68 of Companies Act, 2013** and is one kind of a measure in which the capital of a overcapitalized company can be restructured.
- Buy back of securities increases the EPS and RoE and also enable the shareholders to sell their securities at good price when the market prices of the securities are low. Buy back of securities enhances the reputation of the company and gives a message to all the stakeholders that company is enjoying rich amount of funds.
- Thus a good corporate through buy back of securities by complying of the provisions of the companies act as well as SEBI BUY BACK REGULATIONS not only help the over capitalized companies to restructure its capital but also it increases the shareholders' value too.

(c) ***Please refer 2013 - June [1] {C} (b) on page no. 34***

2017 - June [3] Examine and explain the following statement citing relevant provisions of laws:

(a) The reduction of share capital can result in extinguishment of class of shares. **(3 marks)**

Answer:

- Reduction of capital means reduction of issued, subscribed and paid-up capital of the company.
- The need for reduction of capital may arise in various situations such as:
  - trading losses
  - heavy capital expenses and assets of reduced or doubtful value
  - original capital may either have become lost or a company may find that it has more resources than it can profitably employ
  - to adjust the relation between capital and assets.

- As per **Sec. 66 of Companies Act, 2013**, A company limited by shares or a company limited by guarantee and having a share capital may, if authorised by its articles, by special resolution, and subject to its confirmation by the tribunal on petition, reduce its share capital in any way and in particular:
  - extinguish or reduce the liability on any of its shares in respect of the share capital not paid-up; or
  - either with or without extinguishing or reducing liability on any of its shares,:
    - cancel any paid-up share capital which is lost or is unrepresented by available assets; or
    - pay off any paid-up share capital which is in excess of the wants of the company, alter its memorandum by reducing the amount of its share capital and of its shares accordingly.

  In ***Seil Ltd., Re. (2008) 144 Com Cases 469: (2009) 89 SCL 434 (Del),*** a scheme of amalgamation and arrangement involved reduction of share capital by extinguishment of shares of a particular class. The reduction was approved by the majority of shareholders and creditors of the transferee company. The NCLT approved the reduction and extinguishment of a portion of share capital was held to be permissible as no one was prejudicially affected.

2017 - Dec [1] (a) “Corporate Restructuring aims at significant change in a Company’s business model, management team or financial structure to address challenges and increase shareholders’ value.” Elucidate the statement with relevance to business strategy. **(5 marks)**

(b) “Restructuring is resorted to in various forms with objectives such as profitability improvement, augmenting more resources, relief from competition and methods take the forms like acquisition, merger, takeover, leveraged buy outs, slump sale, overseas acquisitions etc.” Illustrate certain instances that have happened in India setting examples of benefits in Corporate Restructuring. **(5 marks)**

Answer:

(a) • Corporate Restructuring is the process of significantly changing a company's business model, management team or financial structure to address challenges and increase shareholder value.

- Restructuring may involve major layoffs or bankruptcy, though restructuring is usually designed to minimize the impact on employees, if possible.
- Restructuring may involve the company's sale or a merger with another company.
- Companies use restructuring as a business strategy to ensure their long-term viability.
- Shareholders or creditors might force a restructuring if they observe the company's current business strategies as insufficient to prevent a loss on their investments.
- The nature of these threats can vary, but common catalysts for restructuring involve a loss of market share, the reduction of profit margins or declines in the power of their corporate brand.

(b) Corporate restructuring is a process in which a company changes the organizational structure and processes of the business. The most common form of corporate restructuring are mergers/amalgamations, acquisitions/takeovers, financial restructuring, divestitures/ demergers and buyouts. Corporate Restructuring can also be resorted in any of the forms like slump sale, leveraged buy-out or even circumventing the restriction imposed under statutes or by regulators.

As a case of demerger the Cement division of L&T Ltd. resulted to Ultratech Cement Co. Ltd. that resulted in economies of scale and overall competitiveness, multifunctional synergies, combined resource pool, cross leverage financial strengths and increased capacity. Tata Steel Ltd. acquired overseas Corus Group Plc. that improved the synergies to Tata Steel Ltd. that marshalled the resources for both, utilization of wide retail and distribution network, technology transfer and enhanced R&D capabilities. Transfer of undertaking for a lump sum consideration by Piramal Healthcare Ltd. to Abbott Healthcare Pvt. Ltd. with a non-compete clause is slump sale in terms of the **Income-tax Act, 1961**. Capital gains arising therefrom is taxed as long term if held for more than 3 years prior to transfer or as short term if held for less than 3 years. Bharti Airtel Ltd. explored the strategy of leveraged buyout in acquiring Zain Africa International BV majorly financed through borrowed funds. For this purpose, special purpose vehicles are formed. Bharti Airtel structured acquisition through special purpose vehicles thus keeping its financials intact. However, as a guarantor for special purpose vehicles, Bharti Airtel assumes full responsibility.

2017 - Dec [3] (a) "Optimum capitalization is desired to maintain robust financial health of an enterprise." Identify the symptoms of over capitalization or under capitalization. **(3 marks)**
(b) "Reduction of capital requires the approval of National Company Law Tribunal (NCLT) is a general perception." Elucidate. **(3 marks)**

Answer:

(a)
- A company is said to be over-capitalized, if its earnings are not sufficient to justify a fair return on the amount of share capital and debentures that have been issued. Otherwise, it is said to be over capitalized when total of owned and borrowed capital exceeds its fixed and current assets i.e. when it shows accumulated losses on the assets side of the balance sheet.
- If the owned capital of the business is much less than the total borrowed capital than it is said to be under capitalization. In other words the owned capital of the company is disproportionate to the scale of its operation and the business is dependent more upon borrowed capital.
- Under capitalization may be the result of excess volume of trading and over capitalization may be due to insufficient volume of trading.

(b) As per section 66 of the Companies Act, 2013, sanction of the NCLT is required for effecting resolution for extinguishment or reduction of any paid-up share capital yet there are circumstances and provisions to reduce paid-up capital without necessity of approval by the Tribunal. Section 61 enables cancelling the unsubscribed shares without leave of the Tribunal. Also, surrender of shares by a shareholder, forfeiture of shares for non-payment of unpaid calls, redemption of preference shares and buy-back of shares in accordance with section 68 of the Act do not require sanction by Tribunal.

2018 - June [1] (a) "Global competition drives enterprises to become globally fit to face global challenges prompting them for corporate restructuring". Elucidate. **(5 marks)**

(b) "Inorganic growth provides an organisation with an avenue for attaining accelerated growth as compared to the organic growth in general". Comment on the statement. **(5 marks)**

(d) "Inability to pay debts was generally a ground for moving an application for winding up of a Company under the Companies Act, 1956. But such a ground no longer exists under the Companies Act, 2013". State the circumstances which compel a company to be wound up under the Companies Act, 2013. **(5 marks)**

Answer:

(a)
- Corporate restructuring activities such as merger, acquisitions, takeovers, demergers, hive off etc. enables an enterprise to achieve economies of scale, global competitiveness, right size, and a host of other benefit including reduction of cost of operations and administration.
- A merger or amalgamation is capable of offering various financial synergies and benefits such as eliminating financial constraints, deployment of surplus cash, enhancing debt capacity and lowering the cost of financing.
- Thus, global competition drives enterprises to become globally fit to face global challenges prompting them for corporate restructuring.

(b)
- Inorganic growth provides an organization with an avenue for attaining accelerated growth enabling it to skip few steps on the growth ladder. Restructuring through mergers, amalgamations etc., constitute one of the most important methods for securing inorganic growth.
- Inorganic growth is the rate of growth of business by increasing output and business reach by acquiring new businesses by way of mergers, acquisitions and take-overs and other corporate restructuring strategies that may create a change in the corporate entity.

- Inorganic growth strategies like mergers, acquisitions, takeovers and spinoffs are regarded as important engines that help companies to enter new markets, expand customer base, cut competition, consolidate and grow in size quickly, employ new technology with respect to products, people and processes. Thus, the inorganic growth strategies are regarded as fast track corporate restructuring strategies for growth.

(d) Inability to pay debts: Insolvency and Bankruptcy Code, 2016 has substituted section 271 of the Companies Act, 2013. Section 271 of the Companies Act, 2013, before its substitution by the Insolvency and Bankruptcy Code, 2016, provided the seven grounds for winding up by Tribunal. Now two ground have been deleted as below:

- if the company is unable to pay its debts
- if the Tribunal has ordered the winding up of the company under Chapter XIX.

Circumstances in which Company may be Wound up by Tribunal

- if the company has, by special resolution, resolved that the company be wound up by the Tribunal
- if the company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality
- if on an application made by the Registrar or any other person authorised by the Central Government by notification under this Act, the Tribunal is of the opinion that the affairs of the company have been conducted in a fraudulent manner or the company was formed for fraudulent and unlawful purpose or the persons concerned in the formation or management of its affairs have been guilty of fraud, misfeasance or misconduct in connection therewith and that it is proper that the company be wound up
- if the company has made a default in filing with the Registrar its financial statements or annual returns for immediately preceding five consecutive financial years
- if the Tribunal is of the opinion that it is just and equitable that the company should be wound up.

2018 - June [3] (a) What corrective measures a Company can take to restructure its internal finance having noticed symptoms of either under capitalization or over capitalization? **(3 marks)**

Answer:

Some of the corrective measures for over capitalization includes the following:

(a) Buy back of its own shares.
(b) Paying back surplus share capital to shareholders.
(c) Repaying of loans to Financial Institutions, Banks, Fixed deposit of public if any.
(d) Redemption of debentures, bonds etc.
(e) Redemption of preference shares, if any.

An under-capitalized company may restructure its capital by taking one or more of the following corrective steps:

(i) Injecting more capital whenever required either by resorting to rights issue/preferential issue or additional public issue.
(ii) Resorting to additional borrowings from financial institutions, banks, other companies etc.
(iii) Issuing debentures, bonds, etc. or
(iv) Inviting and accepting fixed deposits from directors, their relatives, business associates and public.

2018 - Dec [1] (a) "Corporate Restructuring is an inorganic growth strategy that significantly changes a company's business model, management team or financial structure to address challenges and increase shareholders' value". Elucidate the statement with different options of Corporate Restructuring. **(5 marks)**

Answer:

- Inorganic growth provides an organization with an avenue for attaining accelerated growth enabling it to skip few steps on the growth ladder. Restructuring through mergers, amalgamations etc., constitute one of the most important methods for securing inorganic growth.
- Inorganic growth is the rate of growth of business by increasing output and business reach by acquiring new businesses by way of mergers, acquisitions and take-overs and other corporate restructuring strategies that may create a change in the corporate entity.

- Inorganic growth strategies like mergers, acquisitions, takeovers and spinoffs are regarded as important engines that help companies to enter new markets, expand customer base, cut competition, consolidate and grow in size quickly, employ new technology with respect to products, people and processes.
- Thus, the inorganic growth strategies are regarded as fast track corporate restructuring strategies for growth.

2018 - Dec [2] (a) The unpalatable or inevitable recession can also be a key factor to trigger Mergers/Takeovers – how far is it proved true? **(5 marks)**

Answer:

- Acquisition and Mergers were identified as one of the key factor to overcome economic recession. conducted a research on corporates during world economic recession as to how they adopt strategies to survive during the recession and to succeed subsequently.
- This research focused primarily on 13 companies that were established members of the Global Fortune 500 index. They were the examples of organisations that have adapted, survived, and prospered during recessionary periods. All of the companies studied achieved dramatic increases in growth and profitability during the period of economic downturn or in the following recovery period. These companies were chosen because they exhibit characteristics and strategies that enabled them to achieve success from difficult economic periods. The study has identified seven key factors to have greatest impact on firms' ability to emerge strongly from recessionary periods.
- Among other key factors, they have identified acquisitions and strategic alliances as a key factor to overcome economic recession to strengthen, re-focus, and position the company for increased growth and profitability.
- The study identified that companies also made acquisitions to access new markets, products, technologies, customers and talent at an accelerated pace.

2018 - Dec [3] (c) Enumerate certain circumstances that necessitates financial restructuring, being part of Internal Corporate Restructuring. **(3 marks)**

Answer:

A company is required to balance between its debt and equity in its capital structure and the funding of the resulting deficit.

When, during the life time of a company, any of the following situations arise, the Board of Directors of a company is compelled to think and decide on the company's restructuring:

(i) necessity for injecting more working capital to meet the market demand for the company's products or services;

(ii) when the company is unable to meet its current commitments;

(iii) when the company is unable to obtain further credit from suppliers of raw materials, consumable stores, bought-out components etc. and from other parties like those doing job work for the company.

(iv) when the company is unable to utilise its full production capacity for lack of liquid funds.

Financial restructuring of a company involves rearrangement of its financial structure so as to make the company's finances more balanced.

2019 - June [1] (c) "Circumstances or reasons that prompt or motivate Management to resort to Corporate Restructuring" - Briefly analyse the phrase giving or citing certain noted mergers or demergers during the last couple of years. **(5 marks)**

Answer:

Broadly speaking, management is prompted to resort to corporate restructuring either for financial or other reasons. Financial reasons could be to reduce risk; increase operating efficiency; improve access to financial market; or to avail tax benefits. Other reasons could be to expand marketing and management capabilities; explore new products for development; avail synergistic benefits; or revive a sick company. Insolvency and Bankruptcy Code, 2016 has created one more window to submit resolution plan in a Corporate Insolvency Resolution Process.

Restructuring aims at improving the competitive position of an individual business and maximizing its contribution to corporate objectives. It also aims at exploiting the strategic assets accumulated by a business i.e., monopolies, goodwill, exclusivity through licensing, etc. to enhance the competitiveness advantages. Thus, restructuring helps in bringing an edge over competitors.

Prominent mergers/demergers or acquisitions that took place recently are Flipkart acquiring Myntra, Asian Paints acquiring Ess Ess Bathroom products, RIL acquiring Network 18, Merck acquiring Sigma, Sun Pharma absorbing Ranbaxy; Tata Power acquiring PT Arutimin Indonesia, Reliance Industries demerger, Whitbread plc. demerged Costa Coffee and Sintex demerger.

2019 - June [1] (d) Mergers and acquisitions have one common goal of creating synergy that makes the value of the combined companies greater than the sum of the parts - Analyse briefly to focus on the visible benefits of such combinations. **(5 marks)**

Answer:

All mergers and acquisitions (M&A) have one common goal, i.e., they are all meant to create synergy that makes the value of the combined companies greater than the sum of the two parts. The success of a merger or acquisition depends on whether this synergy is achieved or not. Synergy may be in the form of revenue enhancement and cost savings. By merger, the companies expect to reap the following benefits:

1. **Becoming bigger:** Many companies use M&A to grow in size and leapfrog their rivals. While it can take years or decades to double the size of a company through organic growth, this can be achieved much more rapidly through mergers or acquisitions, i.e., through inorganic growth.
2. **Domination:** Companies also engage in M&A to dominate their respective sector/industry. However, since a combination of two behemoths may result in a potential monopoly, such a transaction may have to face regulatory challenges.
3. **Tax benefits:** Companies also use M&A for tax purposes, although this may be an implicit rather than an explicit motive.
4. **Economies of scale:** Mergers also translate into improved economies of scale which refers to reduced costs per unit that arise from increased total output of a product.

5. **Acquiring new technology:** To stay competitive, companies need to stay on top of technological developments and their business applications. By buying a smaller company with unique technologies, a large company can maintain or develop a competitive edge.
6. **Improved market reach and industry visibility:** Companies buy other companies to reach new markets and increase their revenues and earnings. A merger may expand two companies' marketing and distribution channels thereby giving new sales opportunities. A merger can also improve a company's standing in the investment community, i.e., bigger firms often have an easier time raising capital than smaller ones.

2019 - Dec [2A] (Or) (iii) You are the Company Secretary of PQR Ltd. The Board of the company is opting for reduction in the share capital of the company without seeking the approval of the Tribunal. How would you advise the Board? **(5 marks)**

Answer:

Cases which amount to reduction of share capital but where no approval/confirmation by the Tribunal is necessary:

(a) **Surrender of shares:** 'Surrender of shares' means the surrender of shares already issued, to the company, by the registered holder of shares. Where shares are surrendered to the company, whether by way of settlement of a dispute or for any other reason, it will have the same effect as a transfer in favour of the company and amount to a reduction of capital. But if, under any arrangement, such shares, instead of being surrendered to the company, are transferred to a nominee of the company then there will be no reduction of capital *[Collector of Moradabad v. Equity Insurance Co. Ltd., (1948) 18 Com Cases 309: AIR 1948 Oudh 197]*. Surrender may be accepted by the company under the same circumstances where forfeiture is justified. It has the effect of releasing the shareholder whose surrender is accepted for further liability on shares.

The Companies Act, 2013 contains no provision for surrender of shares. Thus, surrender of shares is valid only when Articles of Association provide for the same and:

(i) where forfeiture of such shares is justified; or
(ii) when shares are surrendered in exchange for new shares of same nominal value. Both forfeiture and surrender lead to termination of membership. However, in the case of forfeiture, it is at the initiative of company and in the case of surrender it is at the initiative of member or shareholder.

(b) **Forfeiture of shares:** A company may if authorised by its articles, forfeit shares for non-payment of calls and the same will not require confirmation/approval of the Tribunal.
(c) **Diminution of capital:** Where the company cancels shares which have not been taken or agreed to be taken by any person.
(d) Redemption of redeemable preference shares.
(e) Buy-back of its own shares.

2020 - Dec [1] (b) It is said that 'corporate restructuring' always has motives. Elaborate on the 'financial motives' that are prevalent? **(5 marks)**

Answer:

Financial Motives behind Corporate Restructuring include the following:

- To reduce risk
- To increase operating efficiency
- To improve access to financial markets
- To obtain tax benefits.
- For a manufacturing unit the operating efficiency is of utmost importance but for lenders like Banks, Financial Institutions and NBFCs, the disbursement risk is the greatest as a wrong judgment shall create a Non-performing asset. Risk has many forms and any one can be a cause for concern for the lenders.
- For newly set-up companies desiring to expand, modernize and grow, the access to financial markets is essential and for this the generation of ideas is important which in future should be able to generate and sustain revenue. Tax savings is the target for all corporate entities.

2020 - Dec [2] (b) 'Buy-back strategy' is nowadays being adopted by leading corporate bodies. Mention one case that has happened recently specifying the benefits of buy-back? **(5 marks)**

Answer:

Corporate giants like Infosys Ltd, Wipro, TCS etc., also resorted to buy-back of securities:

Advantages of buy-back

- It is an alternative mode of reduction in capital without requiring approval of the National Company Law Tribunal
- To improve the earnings per share
- To improve return on capital, return on net worth and to enhance the long-term shareholders value
- To provide an additional exit route to shareholders when shares are undervalued or thinly traded
- To enhance consolidation of stake in the company
- To prevent unwelcome takeover bids
- To return surplus cash to shareholders
- To achieve optimum capital structure
- To support share price during periods of sluggish market condition
- To serve the equity more efficiently.

2020 - Dec [3] (b) Is External Reconstruction superior to Internal Reconstruction? **(3 marks)**

Answer:

- In 'Internal Reconstruction', the assets are re-valued, liabilities are negotiated, and losses suffered are written-off by reducing the paid-up value of shares and/ or varying the rights attached to different classes of shares.
- Internal Reconstruction (IR) is considered to be superior to External Reconstruction(ER) since the exercises undertaken in IR requires an in-depth analysis and remedies instead of giving up in ER in the form of merger or acquisition and losing identity.
- In many a case, Internal Reconstruction does not require approvals from Courts or tribunals that may require conducting meetings of classes of shareholders and creditors, except in a case of reduction of paid up capital.

2021 - Aug [1] (d) "Safeguarding the interest of creditors is considered while sanctioning reduction of capital under Section 66 of the Companies Act, 2013". Comment and analyse briefly. **(5 marks)**

Answer:

In case the proposed reduction of capital involves diminution of liability in respect of unpaid capital or payment of any paid-up capital to any shareholder or in any other case, the Tribunal permits the creditors to object to such proposal.

The Tribunal while granting sanction of the proposed reduction will take into consideration interest of creditors and minority shareholders. In the process, notices will be given to the Government, Registrar of Companies, Securities and Exchange Board of India (in case of listed companies) and the creditors within three months of the application.

There is no limitation on the power of the Court to confirm the reduction except that it must first be satisfied that all the creditors entitled to object to the reduction have either consented or been paid or secured [British and American Trustee and Finance Corpn. v. Couper, (1894) AC 399, 403 : (1991-4) All ER Rep 667].

2021 - Aug [3] (e) HIJ Entertainment LLP desires to amalgamate as transferor with LMN Exhibitors Ltd. Is it permissible? **(3 marks)**

Answer:

Yes, it is permissible as was held in the Matter of Scheme of Amalgamation between Real Image LLP v. Qube Cinema Technologies Private Limited.

The National Company Law Tribunal, Chennai Bench in the order dated 11.06.2018 held that,

"…the legislative intent behind enacting both the LLP Act, 2008 and the Companies Act, 2013 is to facilitate the ease of doing business and create a desirable business atmosphere for companies and...

"For this purpose, both the Acts have provided provisions for merger or amalgamation of two or more LLPs and companies," noted the NCLT bench.

"If the intention of Parliament is to permit a foreign LLP to merge with an Indian company, then it would be wrong to presume that the Act prohibits a merger of an Indian LLP with an Indian company.

"Thus, there does not appear any express legal bar to allow/ sanction merger of an Indian LLP with an Indian company,"

National Company Law Tribunal, Chennai Bench taking such view decided by order dated 11th June 2018. The counsels submitted that Sections 60 to 62 of LLP Act and Sections 230 to 234 of the Companies Act, empowers National Company Law Tribunal to sanction a scheme put by the applicant entities. The Bench noted that there is no express legal bar to permit or sanction merger of Indian LLP with an Indian Company.

2021 - Dec [1] (b) 'Divestiture is normally used to mobilize resources for core business or businesses of the company by realizing value of non-core business assets'. Explain the statement with reasons for Divestitures. Also state one example. **(5 marks)**

Answer:

Divestiture means selling or disposal of assets of the company or any of its business undertakings/ divisions, usually for cash (or for a combination of cash and debt) and not against equity shares to achieve a desired objective, such as greater liquidity or reduced debt burden. Divestiture is normally used to mobilize resources for core business or businesses of the company by realizing value of non-core business assets.

For example: XYZ Ltd. is the parent of a food company, a car company, and a clothing company. If XYZ Ltd. wishes to go out of the car business, it may divest the business by selling it to another company, exchanging it for another asset, or closing down the car company.

Reasons for Divestitures

1. Huge divisional losses
2. Continuous negative cash flows from a particular division
3 Difficulty in integrating the business within the company
4. Unable to meet the competition
5. Better alternatives of investment
6. Lack of technological upgradations due to non-affordability
7. Lack of integration between the divisions
8. Legal pressures

E.g. Nestle is selling its US chocolate business, which includes brands such as BabyRuth, Butterfinger, and Crunch to Ferrero for US$2.8 billion. The deal is part of Nestle's strategy to sell underperforming brands and refocus on healthier products and fast-growing markets.

2021 - Dec [3] (e) Discuss Split-ups and Split-offs in corporate restructuring. **(3 marks)**

Answer:

Splits involve dividing the company into two or more parts with an aim to maximize profitability by removing stagnant units from the mainstream business. Splits can be of two types, Split-ups and Split-offs.

Split-ups : It is a process of reorganizing a corporate structure whereby all the capital stock and assets are exchanged for those of two or more newly established companies resulting in the liquidation of the parent corporation.

Split-offs : It is a process of reorganizing a corporate structure whereby the capital stock of a division or subsidiary of corporation or of a newly affiliated company is transferred to the stakeholders of the parent corporation in exchange for part of the stock of the latter. Some of the shareholders in the parent company are given shares in a division of the parent company which is split off in exchange for their shares in the parent company.

2022 - June [1] (a) "One of the ways of Corporate Restructuring is through market restructuring." Explain with some recent corporate examples as to how this type of restructuring is undertaken. **(5 marks)**

Answer:

Corporate restructuring is an action taken by the corporate entity to modify its capital structure or its operations significantly. To improve the operations of a corporate entity, market restructuring is indispensable. Market restructuring involves decisions with respect to the product market segments where company plans to operate on its corecompetencies. This type of restructuring usually affects employees, and tends to lead to new training initiatives along with some layoffs as the company improves efficiency. This type of restructuring also involves alliances with third parties that have technical knowledge and resources, Indian technology major Tata Consultancy Services Ltd., has embarked upon the marketing capacity and on the process of restructuring and focusing on the three core areas like cloud, agile and automation. The restructuring plan focuses on the manufacturing capacity and on the product, technical, financial, employment, organization, processing and management restructuring activities. Disney is another example where market and technological restructuring has been restructured to, that has helped the company reach more long term technology goals.

Similarly, Tata Steel Ltd. acquired overseas Corus Group Plc. that drastically improved the production synergies for Tata Steel Ltd. Through the acquisition, Tata Steel Ltd. could combine its low-cost production with the high quality of Corus. It resulted utilization of wide retail and distribution network, technology transfer and enhanced R&D capabilities.

2022 - June [2A] (Or) (ii) "An unlimited company can reduce the share capital of the company in a manner specified in the Article of Association of the company without confirmation of NCLT." Comment. List out certain situations where no confirmation of Tribunal is necessary for reduction of capital. **(5 marks)**

Answer:

According to Section 2(92) of the Companies Act, 2013, unlimited company means a company not having any limit on the liability on the members.

The member's liability is unlimited. The unlimited company can reduce the share capital of the Company in a manner specified in the Articles of Association of the Company without confirmation of NCLT.

The following are cases which amount to reduction of share capital but where no confirmation of the Tribunal is necessary:

(a) Surrender of shares.
(b) Forfeiture of shares.
(c) Diminution of capital.
(d) Redemption of redeemable preference shares.
(e) Buy-back of its own shares.

2022 - June [3] (b) Constitution of National Company Law Tribunal (NCLT) and National Company Law Appellate Tribunal (NCLAT) has provided various new opportunities for Practicing Company Secretaries (PCS) which were not available earlier. Briefly enumerate the scope of services for PCS under NCLT and NCLAT regime. **(3 marks)**

Answer:

With establishment of National Company Law Tribunal (NCLT) and National Company Law Tribunal (NCLAT) opportunities for Company Secretaries has increased. Under section 432 of the Companies Act, 2013, Company Secretaries have been authorized to appear before the Tribunal/ Appellate Tribunal. Before setting - up of the Tribunal, the matters dealt by the Tribunal what dealt by the High Court and so the appearances were taken by only advocates.

Areas of increased scope are as under:

1. Merger/ Amalgamation/Compromise
2. Revival of Companies
3. Winding up
4. Reduction of Capital
5. Oppression and Mismanagement
6. Insolvency and Bankruptcy cases.

2022 - June [3] (c) What are "Equity Carve-Outs"? Explain with suitable examples. **(3 marks)**

Answer:

Equity carve-outs are referred to a percentage of shares of the subsidiary company being issued to the public. This method leads to a separation of the assets of the parent company and the subsidiary entity. Equity carve-outs result in publicly trading the shares of the subsidiary entity. In other words, a company takes out one of the businesses and creates a separate company to handle that part of the business.

1. India's largest engineering and Construction Company Larsen and Tourbo (L&T) adopted "asset-lights strategy" by separating business units into independent subsidiaries by selling a stake in business. The Company, which is considered a corporate proxy for the broader economy, divested its assets as a way to generate capital for investing in fresh projects.

2. In 2017, the Government of India divested 10 per cent stake in Coal India Limited through the Offer-For-Sale (OFS) route at ₹ 358 per share and brought its holding to 79.65 per cent.

2022 - Dec [1] (b) Discuss the obligations of Merchant Banker under SEBI (Buy-back of Securities) Regulations, 2018. **(5 marks)**

Answer:

As per Regulation 25 of SEBI (Buy-Back of Securities) Regulations, 2018, the obligations of Merchant Banker include ensuing the following:

a. the company is able to implement the offer
b. the provision relating to escrow account has been complied with
c. firm arrangements for monies for payment to fulfil the obligations under the offer are in place
d. the public announcement of buy-back is made and the letter of offer has been filed in terms of the Regulations.
e. the merchant banker should furnish to SEBI, a due diligence certificate which should accompany the draft letter of offer
f. the merchant banker should ensure that the contents of the public announcement of offer as well as the letter of offer are true fair and adequate and quoting the source wherever necessary
g. the merchant banker should ensure compliance of Section 68,69 and 70 of the Companies Act. and any other applicable laws or rules in this regard has been made
h. upon fulfilment of all obligations by the company under the Regulations, the merchant banker should inform the bank with whom the escrow or special amount has been deposited to release the balance amount to the company and send a final report to SEBI in the specified form, within 15 days from the date of expiry of the buy-back period.

2022 - Dec [1] (c) Regardless of their category of structure, all mergers and acquisitions have one common goal - "they are all meant to create synergy that makes the value of the combined companies greater than the sum of the two parts'. Comment. **(5 marks)**

Answer:

Mergers and acquisitions can have multifarious goals however arriving at a synergy that makes the combined value of the merged entity much higher those of individual entities is always a target. The success of a merger or acquisition depends on whether the planned synergy is achieved or not. Synergy may take the form of revenue enhancement or cost savings or some other form which benefits the companies. By merging, the companies hope to benefit from the following:

1. **Becoming bigger:** Many companies use M&A to grow in size and compete their rivals. While it can take years or decades to double the size of a company through organic growth, this can be achieved much more rapidly through mergers or acquisitions.
2. **Pre-empted competition:** This is a very powerful motivation for mergers and acquisitions, and is the primary reason why M&A activity occurs in distinct cycles.
3. **Domination:** Companies also engage in M&A to dominate their sector. However, since a combination of two behemoths would result in a potential monopoly, such a transaction would have to face regulatory authorities.
4. **Tax benefits:** Companies also use M&A for tax purposes, although this may be an implicit rather than an explicit motive.
5. **Economies of scale:** Mergers also translate into improved economies of scale which refers to reduced costs per unit that arise from increased total output of a product.
6. **Acquiring new technology:** To stay competitive, companies need to stay on top of technological developments and their business applications. By buying a smaller company with unique technologies, a large company can maintain or develop a competitive edge.
7. **Improved market reach and industry visibility:** Companies buy other companies to reach new markets and grow revenues and earnings. A merger may expand two companies' marketing and distribution, giving them new sales opportunities. A merger can also improve a company's standing in the investment community: bigger firms often have an easier time raising capital than smaller ones.

PRACTICAL QUESTIONS

2014 - June [2A] (Or) (ii) X Ltd. is a listed company and holds 100% equity of Y Ltd. Y Ltd. holds 15% equity in Z Inc., USA as on 31st March, 2014. Due to the poor performance of Z Inc., USA, Boards of directors of X Ltd. and Z Inc., USA in their meeting held on 20th May, 2014 approved merger of Z Inc., USA with X Ltd. with effect from 1st April, 2014. The scheme of merger was filed with the Hon'ble High Court of Delhi pursuant to **sections 230-232.** The Registrar of Companies (ROC) has raised objections that sanction of the scheme of merger would result in the buy back by the X Ltd. of shares of its subsidiary Z Inc., USA and would thereby violate the provisions of Section 19 and Section 68 of Companies Act, 2013. Comment whether the objection raised by the ROC is sustainable in the Tribunal of law. **(5 marks)**

Answer:

This case is similar to that of *Himachal Telematics Ltd. v. Himachal Futuristic Communications Ltd. (1996) 86 Comp Cas 325 (Del)* in which a scheme of amalgamation was to be undertaken. However, the transferee company had a subsidiary which was holding shares of the transferor company. An objection was raised that the sanction of the scheme of amalgamation would result in the buying back by the transferee company of shares of its subsidiary and would thereby violate the provisions of **Section 19 and 68 of the Companies Act, 2013.** Dealing with the argument regarding violation of **Section 68 of Companies Act, 2013**, it was held that no violation would result as a consequence of sanctioning the scheme of amalgamation as the transferee company was not buying any of its own shares.

2015 - June [1] (c) Brown Ltd. committed certain defaults in repayment of deposits. Subsequently, the said defaults were remedied and a period of 30 months has lapsed after such defaults ceased to subsist.

Brown Ltd. desires to purchase its own shares. Do you think Brown Ltd. is entitled to proceed with the proposed buy-back of shares?

Give reasons for your answer quoting the relevant provisions applicable to the issue under consideration. **(5 marks)**

(d) The paid-up capital of Cool Ltd. as on 31st March, 2014 is ₹ 10 crore and its free reserves as on the same date was ₹ 10 crore. Cool Ltd. proposes to buy-back its shares for a value upto 15% of its paid-up capital.
State whether the Board of Cool Ltd. can approve buy-back of company's shares upto 15% of the paid-up capital under the provisions of the Companies Act, 2013. **(5 marks)**

Answer:

(c)
- In the given case, Brown Ltd. committed certain defaults in repayment of deposits.
- Subsequently, the said defaults were remedied and a period of 30 months has elapsed after such defaults ceased to subsist.
- Under **Section 70 of the Companies Act, 2013**, no company shall directly or indirectly purchase its own shares or other specified securities if a default is made by the company, in the repayment of deposits, interest payment thereon. However, the buy-back is not prohibited, if the default is remedied and a period of three years has lapsed after such default ceased to subsist.
- In the above case, since three years has not lapsed after default ceased to subsist, Brown Ltd. is not entitled to proceed with the proposed buy-back of shares.

(d)
- Board of Directors can approve buy-back up to 10% of the total paid-up equity capital and free reserves of the company.
- Shareholders by a special resolution can approve buy-back up to 25% of the total paid-up capital and free reserves of the company.
- In the given case, Cool Ltd. proposes to buy-back its shares for a value upto 15% of its paid-up capital.
- Paid-up capital of Cool Ltd. is ₹ 10 crore
- Free reserves of Cool Ltd. is ₹ 10 crore
- Cool Ltd. proposes to buy-back its shares for a value upto 15% of its paid-up capital. (i.e. 15% of 10 crore = 1.5 crore) which is very well within the limits of Board of Directors approval which is 10% of paid-up equity capital and free reserves (i.e. 10% of 20 crore = 2 crore).
- Hence, Board of Directors of Cool Ltd. can approve the buy-back of shares.

2015 - June [3] (c) Hardnut Ltd. wants to buy-back its equity shares. The company has equity share capital of ₹ 100 crore (face value of ₹ 10 fully paid-up) and free reserves of ₹ 200 crore. Partly paid equity shares are ₹ 60 crore. Preference share capital of face value ₹ 100 fully paid is ₹ 40 crore. The company seeks your opinion about the quantum of shares that can be bought back. **(5 marks)**

Answer:

Equity Shares	: ₹ 100 crore
Free Reserves	: ₹ 200 crore
Partly paid equity shares	: ₹ 60 crore
Preference shares capital	: ₹ 40 crore

Maximum amount upto which board can approve buy-back of shares is 10% of total paid up equity capital & free reserves of the company.

In this case matrix Ltd. has a paid up equity capital = ₹ 160 crore and Free Reserves = ₹ 200 crore ,Total = ₹ 360 crore.

Maximum amount board can approve buy-back of shares

= 10% of ₹ 360 crore

= ₹ 36 crore

Maximum amount upto which the shareholders can approve buy-back of shares is 25% of paid up capital & free reserves.

In this case, total paid up capital & free reserves

= (₹ 100 crore + ₹ 60 crore + ₹ 40 crore + ₹ 200 crore)

= ₹ 400 crore

Shareholders can approve upto 25% of ₹ 400 crore = ₹ 100 crore

Buy-back of equity shares should not exceed 25% of total paid up equity capital of the company in any financial year.

So, equity shares can be bought back maximum to the extent of 25% of (₹ 100 crore – ₹ 60 crore) = ₹ 40 crore

2019 - June [1] (a) XYZ Ltd. is going for reduction of capital, but the Board of directors of the company expects objection from some of the creditors of the company. The Board seeks your opinion as a company secretary with respect to this matter. Express your opinion in light of the provisions of Companies Act, 2013. **(5 marks)**

Answer:

After passing the special resolution for the reduction of capital, XYZ Ltd. has to apply to the National Company Law Tribunal (NCLT) for the confirmation of resolution under Section 66 of the Companies Act, 2013. Where the proposed reduction of share capital involves either (i) diminution of liability in respect of unpaid share capital, or (ii) the payment to any shareholder of any paid-up share capital, or (iii) in any other case, if the Tribunal so directs, the following provisions shall have effect:

The creditors having a debt or claim admissible in winding-up are entitled to object. To enable them to do so, the Tribunal will settle a list of creditors entitled to object. If any creditor objects, then either his consent to the proposed reduction should be obtained or he should be paid off or his payment be secured. The Tribunal, in deciding whether or not to confirm the reduction will take into consideration the rights of the creditors.

The Tribunal shall give notice of every application made to it to the Central Government, Registrar of Companies and to the Securities and Exchange Board of India, in the case of listed companies, and the creditors of the company and shall take into consideration the representations, if any, made to it by Central Government, Registrar, the Securities and Exchange Board and the creditors within a period of three months from the date of receipt of the notice.

If no representation has been received from them within the said period, it shall be presumed that they have no objection to the reduction.

Provided that no application for reduction of share capital shall be sanctioned by the Tribunal unless the accounting treatment, proposed by the company for such reduction is in conformity with the accounting standards specified in Section 133 of the Companies Act, 2013 or any other provision of the Act and a certificate to that effect by the company's auditor has been filed with the Tribunal.

There is no limitation on the power of the Tribunal to confirm the reduction except that it must first be satisfied that all the creditors entitled to object to the reduction have either consented or been paid or secured [British and American Trustee and Finance Corporation v. Couper (1894)].

When exercising its discretion, the Tribunal must ensure that the reduction is fair and equitable.

2019 - Dec [2] (c) XYZ Ltd. is a company listed on the National Stock Exchange. The latest audited financial position of XYZ Ltd. is as under :

	(Amount in ₹ crore)
Paid up equity capital	442
Free Reserves	20,347
Total secured and unsecured debts	1,275

The company intends to buy-back its fully paid up equity shares of ₹ 5 each not exceeding 2,05,85,000 equity shares at ₹ 950 per equity share payable in cash for aggregate consideration not exceeding ₹ 1,955.57 crore.

Examine whether the above buy-back offer through tender route can be approved by the Board of Directors, keeping in view the provisions of the relevant SEBI Regulations and Companies Act, 2013. **(5 marks)**

Answer:

Quantum of Buy-back (Section 68 of the Companies Act, 2013)

(a) Board of directors can approve buy-back up to 10% of the total paid-up equity capital and free reserves of the company and such buy-back has to be authorized by the board by means of a resolution passed at the meeting.

(b) Shareholders by a special resolution can approve buy-back up to 25% of the total paid-up capital and free reserves of the company. In respect of any financial year, the shareholders can approve by special resolution up to 25% of total equity capital in that year.

The ratio of the aggregate of secured and unsecured debts owed by the company after buy-back should not be more than twice the paid-up capital and its free reserves i.e. the ratio shall not exceed 2:1.

In the instant case, since the paid-up equity capital and free reserves is ₹20,789 crore as per the latest audited financials, the Board can authorize through a resolution passed at its meeting the buy-back of shares totaling ₹1,955.57 crore, which is less than the prescribed 10% limit.

After the buy-back scheme for ₹ 1955.57 crore has been fully completed, the company's reserves would drop to ₹ 18401.72 crore and its paid-up equity capital would drop by ₹ 10.29 crore to ₹ 431.71 crore. Hence, its paid up capital and free reserves after buy-back would drop to ₹ 18833.43 crore.

Thus, the debt-equity ratio after buy-back scheme has been fully completed would be 0.068, which is less than the stipulated 2:1.

Hence, XYZ Ltd. can proceed with the proposed buy-back scheme by passing a resolution passed at the Board meeting.

2022 - Dec [1] (a) A Ltd. is engaged in the business of manufacturing designer clothes. Due to lower demand during the COVID-19 period, the company started facing financial difficulties. The company has a consortium of 9 lenders out of which 5 lenders have provided term loan and remaining lenders have provided working capital loan. The operating margin of the company is continuously shrinking and the collections from the debtors are also not within the due dates. The company is facing severe financial crisis and finding it difficult to honour its debt commitments.
Explain the restructuring options available with the company to deal with the situation. **(5 marks)**

Answer:

In the given situation, the company is faced with financial crisis and is looking for options for Corporate Restructuring. Corporate financial restructuring is any substantial change in a company's financial structure, or ownership or control, or business portfolio designed to increase the value of the firm i.e., debt and equity restructuring.

Internal reconstruction of a company is the simplest form of financial restructuring. Under this various liabilities are reduced after negotiating with various stakeholders such as banks, financial institutions, creditors, debenture holders and shareholders. It deals with the restructuring of capital base and raising finance for new projects.

One of the options available with the company is debt restructuring.

Debt Restructuring

It involves reduction of debt and an extension of payment terms or change in terms and conditions, which is less expensive. It is nothing but negotiating with bankers, creditors, vendors. It is the process of reorganizing the whole debt capital of the company. It involves the reshuffling of the balance sheet items as it contains the debt obligation of the company. Debt restructuring can be achieved in the following ways:

(1) Restructuring of the secured long-term borrowing for improving liquidity and increasing the cash flows for a sick company and reducing the cost of capital for healthy companies. Restructuring of the unsecured long-term borrowings.
(2) Restructuring of the long-term unsecured borrowings can be in form of public deposits and/or private loans (unsecured) and privately placed, unsecured bonds or debentures.
(3) Restructuring of other short-term borrowings; the borrowings that very short in nature arc generally not restructured these can indeed be renegotiated with new terms. These types of short-term borrowings include inter-corporate deposits clean bills & clean overdraft.
(4) Best method for corporate debt restructuring is Debt-equity swap. In the case of a debt-equity swap, specified shareholders have right to exchange stock for a predetermined amount of debt (i.e. bonds) in the same company. In debt-equity swap debt/bonds are exchanged with shares/stock of the company.

Considering the above, debt restructuring is a viable options that the company may pursue.

2023 - June [1] (d) PQR Ltd. is a company listed on the Bombay Stock Exchange. The latest audited financial position of PQR Ltd. is as under:

	Amount (₹ in crore)
Paid up equity capital	884
Free Reserves	40,694
Total secured and unsecured debts	2,550

The company intends to buy-back its fully paid up equity shares of ₹ 10 each not exceeding 20,585,000 equity shares at ₹ 1900 per equity share payable in cash for aggregate consideration not exceeding ₹ 3,911.15 crore. Examine whether the above buy-back offer through tender route can be approved by the Board of directors, keeping in view the legal framework for buy-back of securities. **(5 marks)**

Answer:

Board of directors can approve buy-back up to 10% of the total paid-up equity capital and free reserves of the company and such buyback has to be authorized by the board by means of a resolution passed at the meeting.

Shareholders by a special resolution can approve buy-back up to 25% of the total paid-up capital and free reserves of the company. In respect of any financial year, the shareholders can approve by special resolution up to 25% of total equity capital in that year.

The ratio of the aggregate of secured and unsecured debts owed by the company after buy-back should not be more than twice that paid-up capital and its free reserves i.e., the ratio shall not exceed 2:1.

In the present case, since the paid-up equity capital and free reserves is ₹ 41,578 crores as per the latest audited financial statement, the Board can authorise through a resolution passed at a meeting the buyback of shares totalling ₹ 3911.15 crore, which is less than the prescribed 10% limit (i.e., ₹ 4157.80 crore).

After the completion of the buyback scheme for ₹ 3,911.15 crore, the company's paid up capital and free reserve would drop to ₹ 37,666.85 crore (₹ 41578 crores minus ₹ 3911.15 crore) and total secured and unsecured debts is ₹ 2550 crore. Thus, the debt equity ratio is after by back scheme has been fully completed would be 0.068, which is less than than the stipulated 2:1.

Hence, PQR Limited can proceed with the proposed buy back scheme by passing a resolution passed at the meeting of its Board of Director.

2024 - June [2] (a) PQR Ltd. is a company listed on the National Stock Exchange. The latest audited financial position of PQR Ltd. is as under:

Paid up equity Capital	₹ 780 Crore
Free Reserves	₹ 39,564 Crore
Share Premium	₹ 1,456 Crore

Total secured and unsecured debts ₹ 1,867 Crore.

The company intends to buy-back its fully paid-up equity shares of ₹ 10 each not exceeding 2,16,17,000 equity shares at ₹ 1,945 per equity share payable in cash for aggregate consideration not exceeding ₹ 4,204.51 crore. Examine whether the above buy-back offer through tender route can be approved by the Board of Directors for all 2,16,17,000 equity shares,keeping in view the legal framework for buy-back of securities? **(5 marks)**

TOPICS NOT YET ASKED BUT EQUALLY IMPORTANT FOR EXAMINATIONS

Q.1. Reliance Industries Ltd. announced the demerger of its financial services arm Reliance Strategic Investments, which would be renamed later on as Jio Financial Services Ltd. (JFSL). Explain the key aspects of demerger scheme and rational for demerger?

Answer:

Key Aspects of Demerger:

Reliance announced the demerger of its financial services arm Reliance Strategic Investments Limited as part of its group restructuring. The Scheme of Arrangement provides for:

(a) demerger, transfer and vesting of the Demerged Undertaking from the Reliance Industries Limited (RIL) into the Reliance Strategic Investments Limited (RSIL) on a going concern basis, and issue of 1 (One) fully paid-up equity share of the Reliance Strategic Investments Limited (RSIL) having face value of Rs 10 (Rupees Ten) each for every 1 (One) fully paid-up equity share of Rs 10 (Rupees Ten) each of the Reliance Industries Limited (RIL), in consideration thereof, in accordance with the provisions of Section 2(19AA) of the Income Tax Act; and

(b) reduction and cancellation of the entire pre-Scheme share capital of the Reliance Strategic Investments Limited (RSIL).

Rational of Demerged Scheme:

(i) The Demerged Company is India's biggest conglomerate with interests in multiple businesses. One amongst the multiple businesses carried on by the Demerged Company is the Financial Services Business which is carried on by the Demerged Company directly and through its subsidiaries and joint ventures.

(ii) Further growth and expansion of the Financial Services Business would require differentiated strategy aligned to its industry specific risks, market dynamics and growth trajectory.

(iii) The nature and competition involved in the financial services business is distinct from the other businesses and it is capable of attracting a different set of investors, strategic partners, lenders and other stakeholders.

Q. 2. Explain the key aspects of HDFC Limited and HDFC Bank merger

Answer:

A. Brief about the Companies:

- HDFC Investments Limited (Transferor Company No.1) is a Systemically Important NonDeposit Taking Non-Banking Financial Company registered with the Reserve Bank of India (RBI) and is primarily engaged in the business of making investments in equity shares, preference shares, venture funds, mutual funds and other securities.
- HDFC Holdings Limited (Transferor Company No.2) is also a Systemically Important NonDeposit Taking Non-Banking Financial Company registered with the RBI and is primarily engaged in the business of making investments in equity shares, preference shares, venture funds, mutual funds and other securities.
- Housing Development Finance Corporation Limited (Transferee Company/ Amalgamating Company) is principally engaged in the business of providing finance to individuals, corporates and developers for the purchase, construction, development and repair of houses, apartment and commercial properties in India through its branches in India and overseas offices supported by network of agents for sourcing loans as well as deposits.
- HDFC Bank Limited (Amalgamated Company) is registered with RBI as a banking company under the provisions of the Banking Regulation Act, 1949.

Transferor Companies are wholly-owned subsidiaries of the Transferee Company/ Amalgamating Company and that the entire paid-up share capital of the respective Transferor Companies are held by the Transferee Company/ Amalgamating Company.

Transferor Companies and Transferee Company/ Amalgamating Company are promoter companies of the Amalgamated Company. Transferee Company/ Amalgamating Company and the Amalgamated Company are both listed on BSE Limited (“BSE”) and National Stock Exchange Limited (“NSE”)

Composite Scheme of Amalgamation:

Sanction of Composite Scheme of Amalgamation among Transferor Companies, Transferee Company and Amalgamated Company sought before the Hon'ble NCLT under Sections 230 to 232 and other applicable provisions of the Companies Act, 2013 and in compliance with the provisions of the Income Tax Act.

The Scheme, inter alia, provides for the:

(a) Amalgamation of the Transferor Company No. 1 and the Transferor Company No. 2 (together referred to as the "Transferor Companies") with and into the Transferee Company/Amalgamating Company, with effect from the Appointed Date and the consequent dissolution of the Transferor Companies without being wound up; and

(b) Amalgamation of the Transferee Company/Amalgamating Company with and into the Amalgamated Company, with effect from the Appointed Date and the consequent dissolution of the Transferee Company/Amalgamating Company without being wound up, and the issuance of the New Equity Shares (as defined in the Scheme) to the equity shareholders of the Transferee Company/Amalgamating Company as on the Record Date (as defined in the Scheme) in accordance with the Share Exchange Ratio.

Some of the Rationale and Benefits of the Scheme:

- the Amalgamation, through the Scheme, shall enable the Amalgamated Company to build its housing loan portfolio and enhance its existing customer base;
- the Amalgamation is based on leveraging the significant complementarities that exist amongst the parties to the Scheme. The Amalgamation would create meaningful value for various stakeholders including respective shareholders, customers, employees, as the combined business would benefit from increased scale, comprehensive product offering, balance sheet resiliency and the ability to drive synergies across revenue opportunities, operating efficiencies and underwriting efficiencies, amongst others;

- the Amalgamated Company is a private sector bank and has a large base of over 6.8 Crore customers. The bank platform will provide a well-diversified low cost funding base for growing the long tenor loan book acquired by the Amalgamated Company pursuant to the Amalgamation;
- the Amalgamated Company is a banking company with a large distribution network that offers product offerings in the retail and wholesale segments. The Amalgamating Company is a premier housing finance company in India and provides housing loans to individuals as well as loans to corporates, undertakes lease rental discounting and construction finance apart from being a financial conglomerate. A combination of the Amalgamating Company and the Amalgamated Company is entirely complementary to, and enhances the value proposition of, the Amalgamated Company;
- the Amalgamated Company would benefit from a larger balance sheet and networth which would allow underwriting of larger ticket loans and also enable a greater flow of credit into the Indian economy;
- the Amalgamating Company has invested capital and developed skills and has set up approximately 464 (Four Hundred and Sixty Four) offices across the country. These offices can be used to sell the entire product suite of both the Amalgamating Company and the Amalgamated Company;
- the loan book of the Amalgamating Company is diversified having cumulatively financed over 90 lakh dwelling units. With the Amalgamating Company's leadership in the home loan arena, developed over the past 45 years, the Amalgamated Company would be able to provide to customers flexible mortgage offerings in a cost-effective and efficient manner;
- the Amalgamated Company has access to funds at lower costs due to its high level of current and savings accounts deposits (CASA). With the amalgamation of the Amalgamating Company with the Amalgamated Company, the Amalgamated Company will be able to offer more competitive housing products;

➢ the Amalgamating Company's rural housing network and affordable housing lending is likely to qualify for Amalgamated Company as priority sector lending and will also enable a higher flow of credit into priority sector lending, including agriculture.

Repeatedly Asked Questions		
No.	**Question**	**Frequency**
1.	Discuss "Strategic Alliance" and "Joint Venture" as corporate restructuring strategies. 13 - June [1] {C} (b), 17 - June [1] (c)	2 Times