allow the negative adjustment to the book profits for purposes of MAT. Subject to the facts of a case, it may be possible to contest the denial of the adjustment on merits.

Return of Income for the year of merger

In case the approval for the merger is not granted by the jurisdictional High Court by the date of filling of the Returns of income of amalgamating and the amalgamated company, both the companies would need to file their Returns of Income as if the amalgamation has not taken place.

Due disclosure by way of note should be made in the return of income stating that the return shall be appropriately revise after the approval of the Scheme of Merger is obtained from the High Court.

Taxability of bad debts of the amalgamating (target) Companies in the hands of the amalgamated company

Debts provided for and considered in computing Income of the amalgamating predecessor company, may be claimed as a deduction by the amalgamated company if the same become irrecoverable subsequently.

Continuing benefits in respect of certain expenses in the hands of the amalgamated company:

Expenses related benefits

Specified expenses are eligible for amortization over a prescribed period and deductible accordingly from the taxable income.

The amalgamated company is entitled to continue to claim the benefit of the unamortized expenses of the amalgamating company over
the unexpired period in respect of Preliminary Expenses; expenditure on Scientific Research; Capital expenditure on family planning.

The unamortized expenditure on acquisition of patent or copy rights or know-how would be eligible as a deduction to the amalgamating company. Where, however, the expenditure is incurred after March 31, 1998, the same shall be regarded as intangible assets eligible for depreciation accordingly.

Income related benefits

As per the law on date, the Act permits the amalgamated /resulting company (in case demerger) to continue to avail the tax holiday of the amalgamating company (or de-merged undertaking) for the unexpired period of the holiday.

The finance Bill, 2007 proposes to altogether withdraw the continuity of the unexpired tax holiday for specified undertaking in the hands of the amalgamated/ resulting neutrality of corporate re-structuring. There is no similar amendment proposed for purpose of specified industrial undertaking and it may therefore be assumed that such amalgamated/ resulting companies may continue to enjoy the unexpired tax holiday post amalgamation/de-merger of such specified industrial undertakings.

Other than the above proposed withdrawal, the existing provisions of the Act do not expressly permit the amalgamating/de-merger company to claim the tax holiday for the year in which the amalgamation/ de-merger takes place. Also, there is no provision that entitle the amalgamated/resulting company to claim the same in the year of the amalgamation/de-merger. To this extent, the tax holiday for the
year of amalgamation/demerger is lost. It may be recalled that for purpose of depreciation claims for the year in which the Merger/De-merger takes place, both the amalgamating and the amalgamated companies can claim depreciation on a proportionate basis for the number of days of use of the assets.

Share Buyout

Acquisition by purchase of shares is the simplest form of re-organization. If involves take-over without following the Court procedure under section 391-394 of the Companies Act. The shares are sold and registered in “the name of the purchasing company or on its behalf. The selling shareholders receive either cash compensation or shares in the acquiring company as consideration for their shareholding.

Typically a foreign company buys out the shares of Indian company from the shareholders of the Indian company. Where the foreign company acquires 100% of the shares in the Indian Company, it results in Indian company becoming a wholly owned subsidiary of the foreign company. The relevant tax implications are as under:

Gains on transfer of shares - Taxability in the hands of the shareholders

The consideration for exchange of shares in the target company flows directly to the shareholders in the form of cash, equity shares, and the like. Any non-cash consideration in lieu of the shares transferred is taken at the fair market value.

The exchange of shares would trigger a taxable gain, short-term or long-term, in the hands of the shareholders who would be liable to pay tax accordingly based on the period of holding of the shares transferred.
Tax implications on the company after change in shareholding:

Treatment of unabsorbed losses

A change in shareholding in certain circumstances disentitles a closely held company carrying forward and setting off its losses.

The Act provides that in case of a company not being a company in which public are substantially interested where a change in shareholding has taken place in a previous year, no loss incurred in any year prior to such previous year shall be carried forward and set off against the income of the previous year unless on the last day of that previous year and on the last day of the previous year in which the loss was incurred the shares of the company carrying not less than 51% of the voting power were beneficially held by the same person.

The exceptions to the above rule are:

(1) Where a change in shareholding takes place on account of the death of a shareholder, or transfer shares by way of gift to any relative of the shareholder: or

(2) Any change in the shareholding of an Indian company, being a subsidiary of a foreign company, arising as a result of amalgamation or de-merger of the foreign company provided that 51% of the shareholders of the amalgamating or de-merger foreign company continue to remain the shareholders of the amalgamated or the resulting foreign company.

The provision applies to all losses, including losses under the head capital gains. However, it does not affect the set off of unabsorbed depreciation.
Assets Values

There would not be any change in cost of assets pursuant to the share buyout.

Depreciation Claims

Unabsorbed depreciation would be carried forward and be eligible for set-off, notwithstanding any change in the shareholding pursuant to the buyout. Further, there would not be any change in the depreciation claim to be made in the year of the share buyout.

Expenses incurred on transfer of shares

The expenses incurred on buy-out of the shares may have to be treated as capital expenditure.

Takeover Code

Where the Indian company is a listed company, the foreign company would have to make a public offer for the acquisition of the shares under the guidelines prescribed under the SEBI Takeover Code.

De-merger

Where a company has a business housed with other businesses under the same entity, the target business may be de-merged into resulting company not foreign acquisitions.

In case of an acquisition by a foreign entity, the stock of such resulting company may be acquired by the foreign company. Alternatively, the de-merger can be structured to vest the target business in a foreign acquirer’s pre-owned resulting company. Typically the acquirer would need an Indian SPY to acquire the target business through de-merger.
Tax impact in the hands of De-merged Company and its Shareholders

Gains on transfer of capital assets- Not liable to tax

Any transfer of a capital asset by the de-merged company to the resulting company under the Scheme of de-merger is exempt from capital gains tax, if the resulting company is an Indian company.

Issue/Allotment of Shares - Not liable to Tax

Under the Scheme of de-merger, the shareholders of de-merged company are issued shares in the resulting company on a proportionate basis.

Akin to amalgamation the Act provides that any transfer or issue of shares by the resulting company to the shareholders of de-merged company in consideration of the demerger would not be liable to tax in the hands of the share~olders under the head capital gains.

The cost of acquisitions of shares in the resulting company shall be the amount, which bears to the de-merged company, same proportion as the net book value of the undertaking bears to the net worth of the de-merged company immediately before such de-merger.

Tax impact on the resulting company:

Issue/Allotment of shares - whether liable to DDT

Pursuant’ to a de-merger, distribution of shares by the resulting company to the shareholders of the de-merged company (regardless of a reduction of capital in the demerged company) shall not be treated as deemed dividend. Accordingly, the resulting company will not be liable to any DDT on such issue of shares.
Asset Values

Actual cost of assets under the scheme of de-merger, all the assets and liabilities of the de-merged company (relating to the undertaking or division) are transferred to the resulting company at book value. In consideration of acquisition of such assets, the resulting company issues shares to the shareholders of the de-merged company.

“Actual cost” is defined as actual cost of the assets to the owner reduced by cost met directly by any other person or authority. Accordingly the cost of the assets acquired by the resulting company would be the fair value of shares issued to the shareholders of the de-merged company.

In order to prevent step up without recognition of gain, the cost of the capital assets in the hands of resulting company is restricted to mean the cost actually incurred by the demerged company as if the de-merged company had continued to hold the capital asset for the purposes of its own business.

Cost of Depreciable Assets

Under the Scheme of de-merger, all the assets (including depreciable assets) of the demerged company (relating to the unit/undertaking) are transferred to the resulting company.

The WDV of the block of assets acquired by the resulting company would be the WDV of such assets of the de-merged company immediately prior to the de-merger.

Depreciation Claims

Depreciation under Act is allowed at prescribed rates with reference to WDV of the specified block of assets.
Depreciation in the years of de-merger

In the year of de-merger, depreciation is allowable on pro-rata basis to the de-merged and resulting company in ratio of number of days for which they use the assets.

Expenses in connection with de-merger

Similar to the allowance for claim of the expenses on amalgamation, the resulting company may claim a deduction of $\frac{1}{5}$th of the expenditure incurred wholly and exclusively for the purpose of de-merger, over a period of 5 successive years beginning from the previous years in which the de-merger takes place.

Treatment of the accumulated loss and unabsorbed depreciation

The accumulated loss and unabsorbed depreciation of the undertaking/unit of the demerged company as belonging to the resulting company would be determined as under:

1. Accumulated loss and unabsorbed depreciation directly relatable to the undertaking or the division transferred of the de-merged company would be deemed to be those of the resulting company.

2. Where the accumulated loss and unabsorbed depreciation is not directly relatable to the undertaking or the division transferred than the same would be allocated to the resulting company on a proportionate basis, viz, in the proportion of the assets of the undertaking retained by the de-merged company and transferred to the resulting company. The portion of accumulated losses/unabsorbed depreciation so allocated to the
resulting company would be deemed to be those of the resulting company.

The term accumulated loss and unabsorbed depreciation have been defined to mean so much loss or depreciation which remains to be allowed, if de-merger had not taken place.

It may be noted that unlike amalgamation, there is no provision relating to de-merger which requires that the undertaking transferred should continue to be owned by resulting company.

Continuing benefits in the hands of the resulting company

The provisions relating to continuity of tax holidays in case of de-merger of specified undertaking/industrial undertakings are similar as is prescribed in the case of merger/amalgamation. Relevant discussion section 2 may accordingly be referred.


This is an “Act provide that operation of economic system does not result in the concentration of economic power to the common detriment, for the control of monopolies, for the prohibition of monopolistic and restrictive trade practices and for matters connected therewith or incidental there to.” Powers of the act have been curtailed by the amendments made by MRTP (Amendment) Act, 1991. Chapter 3 of MRTP Act which allowed scrutiny and clearance of merger proposals has been deleted to a great extent. Later, in the ruling of HLL-TOMCO merger case in 1992, Supreme Court of India stated that prior approval of government is not required for amalgamations following amendment to MRTP Act. The commission has now powers post facto to investigate if merger have had any adverse effect.
Sick Industrial Companies (Special Provisions) Act 1985, (SICA, 1985)

This is an “Act to make in public interest special provision with view to securing the timely detection of sick and potentially sick companies owing industrial undertaking, the speedy determination by board of experts of preventive, ameliorative, remedial and other measures which need to be taken with respect to such companies and expeditious enforcement of the measures so determined and for matters connected therewith or incidental thereto. An industrial company will be deemed to be sick industrial company if it has been registered for at least five years and has accumulated losses more than or equal to its net worth at the end of any financial year. Once a company becomes sick company, it will be referred to BIFR, which may as per section 18 sanction its merger with a healthy company for its revival. The sanctioned scheme must be approved through a special resolution by the shareholders of the healthy company. This Act also provides for hearing the views of employees, particularly of transferor sick company who may anticipate uncertainty on merger, and the scheme once sanctioned will be binding on them.

The Companies Act, 2002

The Competition Act was enacted “to provide, keeping in view the economic development of the country, for the establishment of a Commission to prevent practices having adverse effect on competition, in markets, to protect and sustain competition in markets, to protect the interest of consumers and to ensure freedom of trade carried on by any other participants in markets, in India, and for matters connected therewith incidental thereto.” This Act, primarily deals with regulation of combinations (more generally, mergers), in order to prevent
anti-competitive practice abuse of dominant positions of an enterprise which affects free competition. It contains a prohibition against a combination, which causes or is likely to cause an appreciable adverse affects on competition also has provisions requiring pre-notification of combinations form through acquisitions, mergers or amalgamations.

Laws Applicable to Takeovers

In Indian context, there are separate legislations applicable for takeover of public limited companies quoted Stock Exchange. These are:

Clauses 40A and 40B of the Listing Agreement the company entered in to the Stock Exchange SEBI’s Substantial Acquisition of Shares and Takeovers Regulations, 1997 Takeover and Listing Agreement Exemptions: Clauses 40A and 40B of Listing Agreement Clause 40A deals with substantial acquisition of shares and requires the offeror and the offeree to inform the stock exchange when such acquisition results in an increase in the shareholding of the acquirer to more than 10% clause 40B deals with the takeover offers. A takeover offer refers to change in management, clause 40B also provide an exemption to the schemes by BIFR. There is no provision under clause 40B for exemption of non BIFR companies.

Securities and exchange board of India (SEBI) (substantial acquisition of shares and takeovers) regulations, 1997

Securities and Exchange Board of India (SEBI) is “an Act to provide for the establishment of a board to protect the interest of investors in securities and to promote the development of and to regulate the securities market and for maters connected therewith or incidental thereto.” The SEBI’s Substantial Acquisition of Shares and Takeovers
Regulations, 1994 are a first and significant step in laying down rules to be followed when corporate takeover is planned. Regulation 3 of Substantial Acquisition of Shares and Takeovers Regulations, 1994 provides that Chapter 3 of the Regulations (relating to takeovers) would not apply to acquisitions of shares pursuant to a scheme of amalgamation u/s 391 and 394 of Companies Act, 1956 and to the acquisition of shares pursuant to a scheme framed under the Sick Industrial Company (Special Provision) Act by BIFR.

These regulations remained in force till 20 February, 1997 when revised Substantial Acquisition of Shares and Takeovers Regulations, 1997 were reinforced to regulate the takeover bids. The main objectives of these regulations are to provide greater transparency in acquisitions of shares and takeovers of companies through a system of disclosure of information. It provides that any acquirer holding 10% or less of voting rights in capital of company shall acquire further shares only from shareholders of the company by making public announcement in the following way:

1. Appoint a merchant banker in category one holding a certificate of registration granted by SEBI who is not an associate of group of acquirer or target company.

2. The public announcement shall be made not later than four working days of entering into an agreement for acquisition of shares.

3. Copy of public announcement must be submitted to SEBI through merchant banker at least two working days prior to such issuance. Also, copies should be sent to all stock exchanges on which shares are listed and to Registrar’s office of the company for being placed before Board of Directors of the company.
Public announcement shall be made by the acquirer in all the editions of one English and Hindi daily each with wide circulation and one vernacular newspaper of the place where shares of that company are listed and traded. It must be ensured that, announcement, any other advertisement, circular, brochure, material or letter of offer issued after acquisition of shares do not contain any misleading information.

The other disclosures in this announcement include the offer price, number of shares to be acquired from the public, identity of acquirer, purpose of acquisition, future plans of acquirer, if any, regarding the target company, change in control of target company if any, procedure to be followed by the acquirer in accepting shares tendered by the shareholders and period within which all formalities pertaining to the offer will be complete.

The offer price in the public announcement is not approved by SEBI but has to be justified in the offer document after taking into consideration the relevant parameters. In order to cover the events and market functions just prior to the public announcement, the concept of average of daily high and low of the closing prices of shares during the two weeks preceding the date of public announcement has been included in determining the offer price. In case were target company’s shares are frequently traded on Stock Exchange, the offer price is the higher of average of weekly high and low of closing prices of shares as quoted on Stock Exchange during the twenty six weeks prior to date of public announcement and average of daily high and low of closing prices of shares during the two weeks preceding the date of public announcement. The offer price of infrequently traded shares is determined by taking into consideration the negotiated price under agreement, or parameters like return on net worth, book value of shares of Target Company, earnings per share and price earning multiple vis-a-vis the industry average.
Within fourteen days from the date of announcement, a draft of letter of offer at minimum price has to be filed with SEBI through merchant bankers and twenty one days thereafter, the letter of offer shall be dispatched to shareholders. Within twenty one days of submission of offer, SEBI may specify some changes which have to be incorporated before dispatching to shareholders.

The offer at minimum price should be to acquire an aggregate minimum of 20% voting capital. If the offer results in decreasing public shareholding to less than or equal to 10% of voting capital of the company, then acquirer can make another offer. This offer can be made within three months from close of public offer to acquire remaining shares at same price, or disinvest, or offer for sale, or issue fresh share capital to public within six months, such number of shares so as to satisfy Listing Agreements.

The acquirer, under regulation 28 is required by way of security for his performance, to deposit in an Escrow Account such sum as specified in the form of cash deposit, bank guarantee or deposit of acceptable security. No public offer, once made can be withdrawn except under special circumstances.

LAWS OUTSIDE INDIA

Laws in US

Mergers and acquisitions continue to be an important phenomenon in the US economy. Their continued presence has created tremendous interest in this topic. Despite US being a free economy, laws have been framed from time to time to regulate these activities coinciding with the merger waves. Congress has, on three occasions tried to deter the growth of corporate size and power, in 1890 with the passage of Sherman Act,
in 1914 with the passage of Clayton Act and in 1950 with Celler Kefauver Amendment of Sec 7 of Clayton Act.

In US, Securities and Exchange Commission regulates the conduct of takeovers. The justice Department and the Federal Trade Commission regulate economic and anti-trust issues. Many industries have their own regulatory bodies, such as the Federal Reserve Board (banking), the Federal Communications Commission (Broadcasting), the inter State Commerce Commission (railroads and trucking) and the Transportation Department (airlines). The major antitrust regulations of US which have a bearing on merger are contained in the following statutes:

The Sherman Act, 1890

This Act, which prohibits any restraint on trade or attempt to monopolistic trade, was passed in the midst of greatest merger wave of US’s history. Although not directed solely at mergers, one of the goals of Sec 2 of the Act was to stop creation of monopolies through mergers as was occurring in numerous industries at that time. But the Act could not prevent mergers that brought together companies of less than monopolistic dimensions. Recognition of this fact contributed to the impetus behind the second major effort to curtail corporate power in 1914.

The Clayton Act, 1914

Section 7 of the Act prohibits mergers that would substantially lessen competition or tend to create a monopoly. More specifically, the section prohibits full or partial acquisition by a commercial corporation of the stock or assets of another, engaged in commerce in the country, if the effect of such an acquisition may be substantially to lessen competition or tend to create monopoly. The prohibition applies to horizontal, related and conglomerate acquisitions. The various statutory
rules are enforced by the Federal Department of Justice (FDU) and Federal Trade Commission (FTC). Prospective mergers have to be notified to these agencies. Both agencies then investigate and if necessary, initiate proceedings in federal courts. The FTC also has various appeal procedures involving the administrative law courts and independent FTC commissioners.

Merger Guidelines, 1968

In 1968, Department of Justice issued merger guideline which made it difficult for horizontal and vertical mergers in adjacent stages of production and distribution to take place. This had the effect of encouraging conglomerate acquisitions. According to FTC commission statistics, conglomerate acquisitions which accounted for 3% acquisitions in 1940’s and 1950’s rose to 49% by mid 70s.

The 1968 guidelines specified the following thresholds:

1. Horizontal Merger: If the four firm concentration ratios are less than 75%, a merger upto 30% of acquirer and 10% of acquiree might not be challenged. If four firm concentration ratios are more than 75%, the percentages fall to 15% and 1% respectively.

2. Vertical Merger: Where supplying firm has at least 10% of sales in its market and purchasing firm has at least at 6% of total purchases in that market, the merger will be challenged.

3. Conglomerate Merger: Where reciprocal buying and market dominance occurs, the merger will be challenged.

The Williams Act, 1968

This Act regulates tender offers with the help of Security and Exchange Commission. It imposes obligations on both offeror and targets and prevents secret accumulation of large securities by requiring
acquisition of 50% or more of voting shares to be disclosed within ten days. Williams Act defines that when a tender offer commences, the information to be disclosed includes sources of funds and the purpose of the offer. Tender offer must be open for twenty business days and revised offer kept open for another ten business days. Williams Act imposes obligations on targets in response to tender offer. It requires the targets to inform its shareholders of its position on tender offer within ten business days. Targets management must disclose any conflict of interest and also refrain from any materially misleading statements.

Harr-Scott Rodino Anti Trust Improvement Act, 1976

This Act of 1976 brought an improvement on Clayton Act, 1914 to lighten antitrust laws. Merger transactions in which parties have significant assets or sales are regulated by this Act. It requires such parties to notify the Department of Trade (DOT) and Federal Trade Commission (FTC) of such a transaction, observe a prescribed waiting period before completing them. The Act stipulates a threshold test of applicability based on size of parties and a test based on transaction size. It is a two phase process with an initial filing and a second request for more elaborate information.

In April 1997, the US government unveiled new merger guidelines issued by FTC. Although these guidelines do not have any law backing, they are for government staff and lawyers representing merger parties. It is a common phenomenon even in US that Companies proposing to merge always argues that their merger will bring about efficiency. Under the revised guidelines, the government regulators shall not clear the merger proposal unless it passes the test of claimed efficiencies from merger proposing to enhance merged firm’s capacity to behave
competitively, leading to higher quality, better service, lower prices or new products.

Laws in UK

Merger and takeovers have been very frequently in UK also. Laws have been enacted to control and regulate these business combinations. Although restrictive trade practices have been subject of government scrutiny since 1948, mergers have been subject of antitrust regulations only since 1965 with the enactment of Monopolies and Merger Act during which period the UK government policy has gone through distinct phases. While the main trust of antitrust regulation has been maintenance of effective competition, many other issues of public interest have been considered relevant in determining whether merger should be allowed or not. For the first time, merger can be investigated prior to consumation rather than in effective post-merger evaluation situation in which government was never willing to insist on divestiture of private enterprise.

The UK anti-trust regulations are currently dominated by two stage process. The first stage is the preliminary screening by Office of Fair Trading (OFT) created under the Fair Trading Act. 1973. This stage may be lead to recommendation to the President of the Board of Trade for a more detailed investigation by Monopolies and Merger Commission (MMC), the second stage. The MMC undertakes such an investigation and presents its report to the President, who then accepts or rejects its recommendations. The takeover rules are determined by City Panel on takeovers, a self regulatory agency of London Stock Exchange. The secretary for Trade and Industry, regulates all UK industries, so with single regulatory body, government policies are more likely to be consistent across industries.
Fair Trading Act, 1973

The OFT, created under the Fair Trading Act, 1973, is an independent company watch dog and monitors all mergers proposals or actual mergers in U.K. From its initial screening of a merger proposal, the OFT has to determine whether it is merger situation qualifying for investigation by MMC after taking into consideration the various factors and the presents government policy. Over the years, there has been shift of emphasis between competitive and non competitive factors. In period 1965-1973, government encouraged consolidation of UK firms’ in order to enhance their international competitiveness to build national champions. This led to policy of benign “indifference” towards mergers which decreased competition in UK. In the period 1974-83, the policy was changed. Most of the mergers, including conglomerates were rigorously scrutinized and some even disallowed. More recently, the approach seems to be dilution of competitive approach.

Monopolies and Merger Commission

In the second stage, MMC, which is an independent advisory body, may present one of the following three conclusions to the President for recommendation.

(1) Merger does not operate against public interest and can therefore be allowed to proceed.

(2) The merger operates against public interest and may therefore be prevented.

(3) The merger can be allowed subject to adverse effects on competition being remedied.
To conclude, through this concern of anti-trust authorities in UK and US seems to be paradoxical for these laisses-faire economies, yet they suggest the amount of authority they possess in ensuring competition and fair corporate practices.

VALUATION IN A MERGER: METHOD OF SHARE EXCHANGE RATIO

One of the most important aspects of merger is valuation of business of business in order to determine share exchange ratio in mergers. Valuation of the business is tool to assess the worth of a company which is subject to merger or takeover so that consideration amount can be quantified and the price of the one company for the other can be fixed. Valuation of both companies subject to business combination is required for fixing the consideration amount to be paid in the form of exchange of shares. Such valuation helps in determining the value of share of acquired company as well as acquiring company to safeguard the interest of shareholders of both the companies. There are three methods used for valuation of business.

Net Asset Value (NAV) Method

Net asset value is the sum total of value of assets (fixed assets, current assets, investments on the date of balance sheet less all liabilities including both current and likely contingent liability, debts, borrowings and preference share capital) Deductions will have to be made for arrears of depreciation, arrears of preference dividend etc. However, there may be some modifications in this method and fixed assets may be valued at current realizable, (especially real estate and investments), replacement cost (Plant and Machinery) or scrap value(obsolete machinery). The net
asset value so arrived is divided by fully diluted equity to get NAV per share.

Following are steps for valuing shares are:

1. Valuation of assets
2. Ascertainment of liabilities
3. Fixation of the value of different types of equity shares

Yield Value Method

This method, also called profit earning capacity method is based on the assessment of future maintainable earning of the business.’ While the past financial performance serves as guide; it is the future maintainable profits that have to be considered. Earning of the company for next few years are projected (by valuation experts) and simple or weighted average of these profits is computed. These net profits are divided by appropriate capitalization rate to get true value of the business. This figure divided by equity value gives value per share. While determining operating profits of the business, it just is valued on independent basis without considering benefit on account of merger. Also, past of future profits need to be adjusted for extra ordinary income or loss not likely to recur in future. While determining capitalization rate, due regard has to be given to inherent risk to each business. Thus, a business with established brands and excellent track record of growth and diverse product portfolio will get a lower capitalization rate and consequently higher valuation where as a cyclical business or a business dependent on seasonal factors will get a higher capitalization rate. Profits of both companies should be determined after ensuring that similar policies are used in various areas like depreciation stock valuation etc.
Market Value Method

This method is applicable only in case where shares of companies are listed on a recognized stock exchange. The average of high or low value and closing over a specified previous period is taken to be representative value per share.

Now, the determination of share exchange ratio i.e. how many shares of amalgamating company are to be exchanged for how many shares of amalgamated company is basically an exercise in valuation of share of two or more of amalgamating companies. This is done by using the above mentioned techniques not in isolation but keeping in view board objective and other factors. This problem of valuation has been dealt with by Weinberg and Blank (1971) by giving the relevant factors to be taken into account while determining the final share exchange ratio. These relevant factors have been enumerated by Gujarat High Court in Bihari Mills Ltd. And also summarized by the Apex Court in the case of Hindustan Levers Employees Union v. Hindustan levers Ltd. (1995) as under.

1. The stock exchange prices of the shares of the companies before the commencement of negotiation or the announcement of the bid.

2. The dividends presently paid on the shares of two companies. It is often difficult to induce a shareholder to agree to a merger if it involves a reduction in his dividend.

3. The relative growth prospects of the two companies.

4. The cover, (ratio of after tax earnings to dividends paid during the year) for the present dividends of the two companies. The fact that the dividend of one company is better covered than
the other is a factor which has to be compensated to some extent.

5. The relative gearing of the shares of the two companies. The gearing of an ordinary share is the ratio borrowing to equity capital.

6. The value of net assets of the two companies.

7. The voting strength in the merged company of the shareholders of the two companies.

8. The past history of the prices of the two companies.

There are, however, no rules framed specifically for the working out of share exchange ratio in case of amalgamations. According to Delhi High Court statement: “The valuation of shares is a technical matter which requires considerable skill and expertise. There are bound to be difference of opinion as to what the correct value of shares of the company is. If it is possible to value the shares in a manner different from the one adopted in the given case, it cannot be said that the valuation agreed upon has been unfair.” Also, in the Hindustan Lever Ltd. Case, Supreme Court held that approved the scheme, and with the valuation having been pursued by the Financial Institutions. The crux of valuation has been rightly summarized by Nan Stone as “what gets measured gets managed”. On the basis of decided cases in courts in India, the following points emerge:

1. In case of amalgamations of companies listed on recognized stock exchanges with substantial public holding, the courts have unanimously held that a detailed report of an independent expert have also been laid down by the courts.
2. However, even in the cases of amalgamation of closely held listed companies where unanimous approval of share exchange ratio is obtained from shareholders, some courts (especially in Calcutta) have not insisted on experts certificate.

3. In other cases of private listed companies or closely held unlisted companies, in case of complete unanimity to the determined share exchange ratio, lack of expert’s report is overlooked by the courts.

The Law as it stands in India today, does not make it obligatory for the proponents of the scheme of merger to disclose to anyone, the basis on which valuation is done or its actual working unless the court specifically insists on it. It is also not necessary to inform the shareholders or the creditors of the detailed workings of share exchange ratio. Thus, the disclosure of these workings by the company under the present existing scenario is very limited. Hence, very few companies bother to inform the shareholders the basis of arriving at the share exchange ratio or the swap ratio.

SIGNIFICANCE OF APPOINTED DATE AND EFFECTIVE DATE

Amalgamation of two companies involves transfer of all properties and liabilities of amalgamating company to amalgamated company. The date when this transfer takes place is a very crucial decision. Compliance of statutory requirements of income Tax Act and other Acts are dependent on this date. Since the sanction of scheme completely by court may take time (even running up to a few years), the tax liability of the intervening period of both companies could be a matter of dispute.
The date is also significant from the point of view of creditors and shareholders of both the companies.

Appointed date denotes the cut off date from which all the moveable or immovable properties, including rights, powers and privileges of all kinds of Transferor Company shall be transferred to the transferee company. Unless the court alters the appointed date contained in the scheme, the date so contained will be the appointed date and all assets and liabilities of Transferor Company shall vest in Transferee Company effective from this date. It is the date from which both the companies accounts are closed and audited. Also, valuation of assets and liabilities is done for this purpose. It is the date when both companies are merged into one i.e. scheme of merger becomes operational. Transfer date or appointed date remains on paper if scheme is not approved by three fourth majorities of shareholders of both the companies or not sanctioned by the court. However, even if scheme is sanctioned by the court, merger does not become effective until certified copy of High Court order is filed with Registrar. This is called effective date. Effective date is the date on which transfer and vesting of undertaking of Transferor Company takes effect. In other words, all the requisite approvals are obtained after company takes effect. In other words, all the requisite approvals are obtained after completing all the required formalities. Once court gives sanction, merger becomes effective not from date of sanction but from the date when it was arrived at. So once the formalities are over, merger is effective from transfer date. In majority of merger cases appointed date is fixed even in future. The Boards of Reliance Group of Companies announced the merger of Reliance Polypropylene and Reliance polyethylene with Reliance Industries Ltd. On 7\textsuperscript{th} November, 1994 and proposed the amalgamation to be effective from 1\textsuperscript{st} January, 1995.
However, appointed date fixed in past can not be earlier than date of incorporation of either of the two companies involves in merger. In case of premises Ltd. The appointed date as per the scheme was fixed at 1st April, 1991 where as transeree company was incorporated on 28th October, 1991. The appointed date was accordingly modified by the court as 28th October, 1991 being date of incorporation of the company. The objection of Central Government that appointed date could not be earlier than 9th April, 1992 when certificate of commencement of business was issued to Transferee Company was overlooked.

Many cases have been cited when disputes have occurred because of confusion over these dates. There have been avoidable legal battles on interpretation of these dates. Review of merger schemes over last few years show lessons being learnt by drafters of these schemes. Now management ensures that appointed date or transfer date is used and all references are linked to these dates. Indofil Chemicals Ltd. Was merged with modipon Ltd. Vide approval date 1st February, 1986 whereas appointed date was 1st July, 1982. Assessing Officer assessed the assesses in respected in income after the appointed date and did not allow credit for Advance Payment of Tax (APT) and Tax Deduction at Source (TDS) by amalgamated company in its own name.

Income Tax Tribunal held that date of amalgamation was from appointed date and there after all assessments would be made by amalgamated company. They considered that amalgamation was like transfer of immoveable property, where transfer is not complete till registered, but once registered, transfer takes effect from date of sale deed. Similarly merger is effective when all formalities are complete (called the effective date) but effective from the appointed date which is the date of merger.
Similarly, in Marshall Sons and Company (I) Ltd, the court considered the question of determining the appointed date since no specific date was laid by the court sanctioning the scheme. It was held that every scheme of amalgamation has to provide a date necessarily, with effect from which amalgamation or transfer shall take place. In the instant case, a date was incorporated in the scheme. It is open for the court considering the scheme to prescribe any other date for transfer. Since in this case, the court did not prescribe any date for giving effect to the scheme, the date contained in the statement itself shall be date of transfer or amalgamation.

INTERIM PERIOD BETWEEN APPOINTED DATE AND EFFECTIVE DATE

As stated earlier, an amalgamation, though effective from the appointed date becomes operative from the last of the following dates or such other date (effective date) as the court may direct, namely,

(i) The date on which last of all consents, approvals permissions, resolutions, sanctions and orders as mentioned in the scheme are obtained or

(ii) The date on which certified copies of order of the court under Section 391, 392 and 394 of Companies Act, 1956 are filed with the Registrar of Companies.

Thus, there is a time period between appointed date and date on which scheme finally takes effect (i.e. effective date). During this period,

(1) The transferor company shall carry on or deemed to have carried on all its business and activities and shall hold and
stand possessed of and shall be deemed to have held and stood possessed of all the said assets on account of and in trust for the transforee company.

(2) The transferor company shall carry on its business and activities with reasonable diligence and business prudence and shall not undertake any financial commitments, borrow any amounts nor incur any other liabilities, issue any additional guarantees to its subsidiaries or group companies or any third party or save, as expressly permitted by this scheme, and shall not, without the prior written consent of the transforee company, deal with the said assets or any part thereof provide that the transferor company may create charge over the said assets in favors of the transferor group.

(3a) The transferor company shall not make any change in its capital structure either by increase, (by issue of equity shares whether by way of public issue, private placement, on a rights basis, or issuance of bonus shares, convertible debenture or otherwise) decrease, reduction, reclassification, subdivision or consolidation, re-organization, or in any manner, which may, in any way affect the equity share exchange ratio, except by mutual consent of the board of directors of transferor company.

(b) The transforee company shall not make any change in its capital structure by issue of any fresh equity shares except by mutual co~sent of respective Board of Directors of both the companies.

(4) With effect from the appointed date all the profits or incomes accruing or arising to the transforee company or expenditure or
loses arising or incurred by the transferor company shall, for all purpose, be treated and be deemed to be and accrue as the profits or incomes or expenditures or losses of the transferee company, as the case may be.

DUE DILIGENCE

Types of Due Diligence

Broadly, due diligence practices can be categorized into two types. One is the Anglo-Saxon practice. This involves comprehensive legal and financial due diligence and significant disclosure before the signing of an agreement. Contrast this with the practice in much of the rest of the world, which involves more modest preliminary legal and financial due diligence with correspondingly limited disclosure.

Who is involved in due diligence?

This includes company employees, the company’s traditional professional advisors and those hired for their expertise in certain legal, tax, finance accounting and operational issues present in Target Company’s home country. They include financial legal and operational professionals.

Financial Due Diligence

Financial due diligence involves critically examining the target legal company’s historical, current and prospective operative operating result as disclosed /discharged/obtained from the following sources:

1. Audited financial statements.
2. Unaudited financial information
3. Financial information with stock exchanges and regulators regulation
4. Tax returns
5. Cash flow statements etc.

Generally, the process starts at a comprehensive analysis of the balance sheet. A review of the target firm’s financing and capital structure is very much required. Further, this analysis should include details of short-term and long-term borrowings, the percentage of debt and equity ratios in the company’s balance sheet, interest and fixed charges coverage ratios etc.

Financial due diligence also involves analysis of the cash flow statement. One must not forget to examine the quality of company’s relationship with its lenders and an ultimate opinion concerning the reliability and credibility of its financial statements.

Legal Due Diligence

Legal due diligence involves the practices of addressing certain fundamental legal issues which includes good compliance practices as per the Companies Act, SEBI Act, Income Tax Act and other corporate legislations. Analysis of legal due diligence process could be undertaken from the following sources:

(i) Memorandum of Association
(ii) Articles of Association
(iii) Target company’s prospectus
(iv) Documents filed with Registrar of Companies including Registration of Charge
(v) Title deeds of properties
(vi) Tax return and compliance certificate
(vii) Environmental law compliance
(viii) Lending agreement, covenants borrowing powers.
(ix) Compliance with any special industry legislations.
(x) Labor agreement, compensation etc.
(xi) Pending litigations.

Today’s legal environment has become highly specialized. Today, even midsized deals involve battery of corporate tax, real estate, environmental employee benefits, insurance and other kinds of legal professionals. Further, legal due diligence requires careful attention to actual and threatened litigation. Litigations can emerge from various statutory bodies, shareholders, debt holder, suppliers, assistance product liability etc.

Further in the era of increasing regulatory and judicial scrutiny, matters like allegations of improper behavior by corporate officers directors and employees, workplace safety matters, employee benefits, potential equal opportunity violations ever increasing environmental scrutiny may take center stage.

Operational Due Diligence

Operational due diligence includes investigating the target’s intellectual property, its production, its sales and marketing efforts, its human resources and the other operational issues. Meaningful generalizations of operational due diligence practice are difficult to make as it varies from target. Operational due diligence practices can be undertaken by analyzing the information from the following sources:

(i) Newspaper and magazines reporting about the target company.
(ii) Available information with trade association’s chambers and regulatory bodies.
(iii) Market reports.

(iv) Company journals, brochures and websites.

(v) Gathering inputs from the market, market experts, suppliers and customers

(vi) Interviewing the employees, ex-employer etc.

One has to appreciate that preparation of any due diligence report is as good as the persons who conduct it and the correctness of the information gathered. In the case of operational due diligence it is more often very subjective, depending upon the person who is interviewed to gather the information and one may be able to only estimate the future profitability. The successes of due diligence process will depend on the quality and quantity of data collected or supplied.

A Practical Guide to Due Diligence Process

There are two ways of conducting due diligence:

(a) Presentation of predetermined data by the seller/target company in a ‘data room’;

(b) Data provided in response to the acquirer’s questionnaire.

In Data Room method, large amount of data is presented to interested parties to study and value it and get due diligence conducted. Here mammoth data is provided. Data room method has been successfully used for disinvestments by the tender route. By this process, the seller is able to ensure that all the bidders are treated fairly and that they are given access uniformly to the same data or information. Hence, uniformity of the information and documents supplied to all bidders is maintained.
Any discrimination in the supply of information or documents could vitiate the bidding process. This applies more to disinvestments by the central or state government or government companies, which can be subjected to judicial review under the provisions of the Constitution of India.

In other method, a questionnaire is put to target company and on that basis further one-to-one negotiations are done.

Thereafter a due diligence report is prepared by professionals which can be effectively used to negotiate the vexed question of the representations and warranties to be included in the sale and purchase or financing agreement, the disclosures that inevitably qualify (some if not many of them) and the amount, if any, to be set aside in escrow and on what conditions.

Managing the Due Diligence Process

How do we actually go about due diligence? What kinds of people are involved in this procedure? What are the parameters? Let us examine each in some detail.

(1) Initial parameters: Management requires a preliminary evaluation of the areas of key importance for the success of the transaction. This can be continuity of targets, key personnel, suppliers and customers after the mergers and acquisitions.

(2) Selecting due diligence teams: The core team for the conduct of the due diligence should consist of:

- Management representatives of the acquirer;
- Legal counsel;
- Valuation adviser;
• Chartered Accountants, company secretaries/Project consultants;
• Technical consultants;
• Merchant bankers.

This stage will also involve the coordination plan among the team members, and allocating responsibilities and functions. Usually, all external counsels are required to execute confidentiality agreements before commencement of the assignment.

(3) Preparing and executing preliminary investigation: The objective of the preliminary survey is to identify deal-breaking issues upfront before money and other valuable resources are committed to detailed investigations. Some of the critical issues that may emerge during this exercise are:

- concealment of facts and figures;
- insufficient internal controls;
- non-compliance of or adventurous interpretations of contracts, legal provisions, accounting principles policies or standards;
- employee retention and core management succession;
- contingent liabilities;
- statutory non-compliance;
- industrial sickness (erosion of net worth); and
- Legal proceedings.

(4) Detailed due diligence: The success of the investigation to make a well-informed decision would lie in a wellplanned, integrated and coordinated detailed enquiry procedures.

(5) Certification of completeness of disclosures: The due diligence team should obtain a declaration or certificate from the target company
confirming the completeness of the disclosed information and documents, and that no material data has been withheld by the target company.

Contents of the Due Diligence Report

The due diligence report ordinarily contains information pertaining to:

1. company information; share capital and shareholdings;
2. corporate capacity;
3. directors, their interests and conflicts, if any;
4. account and financial statement;
5. statutory compliance with the applicable regulations;
6. personnel;
7. compliance with the industrial disputes Act 1947, the payment of Bonus Act 1965, the payment of Wages Act 1936, the payment of Gratuity Act 1972, the Employees Provident Funds and Miscellaneous Provisions Act 1952, the Employees State insurance Act 1948, and the Local Shops and Establishments Act; as well as with any industrial settlement award, judgment or order in any labour dispute or litigation; recognized trade unions, retrenchments, lay-off and voluntary retirement schemes; and share options, share incentive, profit sharing or other incentive schemes for employees; pension, retirement provident fund, superannuation and gratuity schemes;
8. licenses, permits, approvals and specific statutory compliance;
9. intellectual property rights - identifications of all patents, trade marks, copyrights, industrial designs, all other forms of
registered and unregistered intellectual property rights or other form of monopoly or property rights used or owned by the target company and rights granted to third parties;

10. industrial property know-how, trade secrets;

11. infringement of third party rights;

12. assets- immovable and movable property;

13. exports and imports, compliance with laws;

14. litigation-judicial, quasi-judicial, arbitral and other administrative proceedings;

15. taxation issues - income tax, customs, excise and sales tax;

16. insurance - quality of insurance cover;

17. contractual liabilities and commitments; and

18. environment-related issues - compliance with law, social issues, and the rehabilitation of people likely to be outsider by large. natural resources projects.

Due Diligence Check List

A. Financial Due Diligence

Financial Information

1. Year-to-date financial statements, with comparison to same period of prior year.

2. For the past three years, all annual and quarterly financial statements, including accompanying schedules, of the company and its subsidiaries (balance sheets, income statements, statement of cash flows, and reconciliation of retained earnings). If available, include financial reporting (revenues
and costs) by line of business and revenues from top ten major accounts.

3. Current trial balance and other significant financial statements and internal financial reports of the company and its affiliates.

4. List of bank accounts including bank type or account number, and authorized signatories. Obtain copies of bank reconciliations for review for all accounts for the last two months and each quarter for the last two calendar years.

5. Bank statements for the last month of the fiscal year-end and of the prior year and all months of the current year.

6. Summary of major accounting policies, nothing any that may be controversial or different from the investor country’s generally accepted accounting principles (GAAP) or that may not be in accordance it generally industry practices. Listing of accounting selective methods, particularly significant estimates (e.g., accruals, valuation methods, and depreciation).

7. All auditors’ and independent certified public accounts’ letters and opinions for the company and its affiliates. Obtain auditors’ reports to management concerning internal accounting controls and procedures and other matters and any management responses thereto and internal memoranda (particularly internal audit or regulatory compliance memoranda) concerning the company or its affiliates.

8. Financial projections, if any, for the remainder of the current year and next, year, including assumptions. Include full-year detailed income statement by month, end-of-year estimated
Performa balance sheet and cash flow forecast, budget for the current year, and comparison of actual versus budget year to date for the current year.

9. Identification and description of all contingent liabilities not reflected on the company’s financial statements, established monetary provisions, allowances and reserves, and disagreements with company’s outside auditors concerning the company’s financial reporting during the preceding two years.

10. Copies of letters to management relating to the potential improvement of the company’s internal control systems together with any reports, letters, or correspondence prepared by accountants of the company or any subsidiaries or, partnership.

11. Copies of all tax filings and returns (including shareholder, corporate, or partnership) for the last three years, including income taxes, sales, use property, employment, and franchise taxes (and any other local taxes). Include copies of any correspondence with tax authorities (other than routing transmittals) and copies of tax sharing agreements between the company and its subsidiaries or affiliates.

12. All income tax audit results and any communication (documented or oral) from the government agencies in all jurisdictions that require tax filings.

13. Schedule describing ongoing tax disputes, together with copies of tax authority reports, correspondence, and similar matters, with respect to pending tax proceedings regarding open years or items for the company or any affiliate.
14. Prior year’s tax returns for all companies acquired within the past three years.

15. A schedule of shareholder “due to” and “due from” accounts for the last two years.

16. A listing of any significant nonrecurring expenses occurring in the past year or current year.

17. Schedule of accounting firms that have represented the company or any of its affiliates in any material matters in the last five years.

18. A schedule with supporting agreements showing cooperative arrangements with suppliers detailing year-to-date payments to be received for the balance of the year.

19. A schedule with supporting agreements showing commission arrangements with top ten suppliers detailing commissions received year to date and estimated commissions to be received for the balance of the year.

20. A schedule showing current accounts receivable and payable, accrued expenses, and customer deposits.

21. A schedule of property, plant, and equipment; depreciation schedules, and amortization schedules.

22. Detailed listing of capital investments that will be made during the current fiscal year, especially if not completed as of the date of the company’s most recent financial statements.

23. Reports on the company from any outside consultants, analysts, or others.
24. Description of contingent liabilities arising from any agreements, severance payments for terminated employees, unresolved legal matters, price redetermination or renegotiation, sales subject to warranty or service agreements, product liability, unfunded pension plan liability, and environmental or other matters.

Financing Documents

1. Any significant debt agreements to which the company or any affiliate is a party, such as or revolving loan agreements, bank lines of credit, mortgages, promissory notes significant property or equipment leases, and other similar agreements and arrangements, and all guarantees by the company or any subsidiary together with any interest rate cap, hurdle, swap or other hedging mechanism relating to the foregoing.

2. Summaries of all evidences of compliance with the agreements described in preceding item 1, and any communications regarding defaults, potential defaults, or waivers of defaults.

3. Documents relating to proposed new indebtedness, including but not limited to term sheets, commitment letters, draft agreements, and similar documents.

4. Disclosure documents used in public offerings, state of control, private placements of securities, industrial development bond financing or institutional or bank loan applications.

5. Copies of letters of credit, performance guarantees, and bonds.
6. All pledges, security agreements or other agreements or documents creating or purporting to create liens or other security interest in any assets of the company.

Properties and Equipment

1. List of addresses of properties currently owned or leased by the company and related documentation. Obtain a summary of the office floor plan, facility hours (times and hours per weekday), and revenue generated by each facility.

2. Copies of all deeds or other titles evidencing ownership of the properties owned by the company or a subsidiary/affiliate.

3. For each property owned by the company or affiliate, a copy of the latest owner or leasehold title insurance policy issued, as applicable, and the most recent survey covering such properties.

4. Copies of all leases for use of the real property owned or leased by the company or any affiliate.

5. Copies of all mortgages encumbering the properties owned or leased by the company or affiliate.

6. All equipment and auto leases for a period in excess of two years or that require payments in excess of an immaterial amount annually.

7. List of all automobiles, including title documentation.

8. Plans with respect to any facility closings.

9. Summary of any construction plans for significant new facilities and date on projected construction costs for such facilities and any facilities currently under construction.
10. Copies of all principal trademarks. Licenses, patents, copyrights, websites, toll-free telephone numbers, or trade names of the company or its affiliates, the expiration dates thereof, and pending applications therefore.

11. Details of recent acquisitions, divestitures, spin-offs, or dispositions of assets.

Due Diligence Check List
B. : Operational Due Diligence - A Framework

1. Deal rationale: Identify rationale for the transaction (e.g., market, territories, products and product development, other strategies for revenue growth, strategies for cost savings).

2. Concrete goal: What concrete goals expected to be met, and over what time frame? How will achievement of those goals be measured?

3. Preliminary plan for achieving goals: Specifically, what is the preliminary plan for achieving the goals out-lined above?

4. Drivers of value creation: Based on the above, what is preliminary view regarding the drivers of value creation for the transaction?

5. Most significant hurdles: Preliminary view: What is the preliminary view of the biggest hurdles to achieving the goals set for the transaction?

6. Key due diligence: Are these aspects of due diligence, including operational due diligence, that are especially critical to the plan for the combined enterprise?

7. Integration plan: How will the due diligence process be developed into an integration plan? Are the people and processes in
place to make sure there is a seamless transition from due diligence to integration?

8. Negotiation and pricing strategy: How will information and analyses generated through the due diligence processes be taken into account in the negotiation and pricing strategies? As the deal negotiations precede, will due diligence be appropriately re-targeted along the way? Are the people and processes in place to make sure that these things happen?

9. Macro framework for due diligence: What are the deal team’s key assumptions about macro economic and demographic factors that should frame operational due diligence? These include world economic growth, trade growth; and population growth, age profile, income levels, and other demographic assumptions in the relevant jurisdictions.

10. Economic factors affecting the relevant jurisdictions: What are the assumptions about economic factors affecting the relevant jurisdictions: foreign exchange rates, currency exchange regulations, and fiscal and monetary policies, including taxation and import-export?

11. Political factors: What are the assumptions regarding macro-level political/environment/ecological factors, such as political stability, potential human rights issues, environmental or health issues, and community or social development obligations?

Analysis of the Value-Creation Process

Undertake the following analysis for the target company as well as for the combined enterprise.
(i) The Operations Overview Map

1. On one or more maps, chart the supply chain, facilities, personnel, and products and services produced against sales, distribution, and marketing.

2. On these maps, analyze the following:
   - Markets, including new markets, for products/services
   - Competitive positioning
   - Distribution channels
   - Marketing strategies
   - Operations and technology strategies
   - Sales/services outlets
   - Planned production
   - Supply and transportation synergies and vulnerabilities
   - Political and macroeconomic -trends and vulnerabilities
   - Personnel overlap and shortfall
   - Flow of funds and financing needs, both operating and capital expenditures; analyze currency requirements and foreign exchange and exchange control risk, as well as taxation and transfer pricing issues.

(ii) Marketing, Sales, Distribution and Customer Relationship Management

1. Product analysis: Describe the company’s products/services. Break down into relevant categories and describe territorial markets. Describe uses of the products and assess the qualities of the products against those of competitors, including products substitution. Consider the following factors:
- Price
- Quality
- Service
- Availability/sales formats
- Design/engineering features and standards
- Sales terms (right to return, credit terms, charge-backs, warranties)
- After-sales service, upgrade, follow-on, etc.

Which of the above are most important to customers in the various markets? In which of the above does the company enjoys an advantage sustainable or natural, or is it marginal and temporary (can be copied or eroded)? At any stage of the product life cycle are the various products in their various markets? Do any of the products of the combined enterprise compete with one another? What is the proposed approach to this problem were it exists?

Are there any known negative qualities associated with the product, such as health risks, product liability risk? Or negative environmental or social qualities?

2. Market analyses: demand: How is demand generated, and on what does the level of demand depend? Is it seasonal or cyclical? Is product substitution or technological obsolescence a major risk in terms of basic demand? To what extent can the company control demand? What are the biggest drivers of changes in demand?

3. Market analysis: competitors: Describe the competitive situation by product/market and its effect on product design, product mix, marketing and positioning and pricing.
4. Market analysis: customers (end users): What is the market, and who are the company’s customers? If customers are not end users, this analysis should be done for direct customers and at each stage of the distribution chain all the way to end users. Break down along all relevant categories (for business: industry, size, profitability, outlook; for retail: national, cultural, income level, lifestyle choirs, other demographic features), including geographic. For each major category of customer (end user), assess prospects and indicate the most significant macro trends that could affect demand. Indicate whether customers (end user) relationships tends to be long term, one-off, or something in between. Is there dependence on one or just a few customers?

5. Customer data: What level of information is available and useful, on a realistic basis, about customers (and end users, if different) and the market? How much of that information is being gathered now? How much of the gathered information is, or should be, analyzed for marketing or product design and positioning purposes? What are the implications for IT needs, in terms of capture data in a database, data mining, and customer relationship management?

6. Using product/market data to identify synergies (cost reduction, rationalization, product extensions): Map existing products and services to existing customers/markets. Are there obvious overlaps? Are these obvious product or market extensions? What are the implications for production rationalization, cost reduction through efficiencies over a greater base, design and production for product extensions?

7. End-user remote sales: How much selling occurs remotely - by phone, mail, or computer? Describe how this works and present volume figures and product/customer information. Indicate where sales are
direct; by franchise; through wholesale-retail or other multi-stage distribution chain; or by some other arrangement.

8. Point of sale analysis: What exactly happens at the point of sale? In terms of human (or other, such as online) interaction. If people are providing a service or assisting at the point of sale, describe how they interact. With customers (on-off versus ongoing and personalized), staff turnover, the level of training, and quality control.

9. Inventory analysis: Analyze inventory levels and mix. What are the levels of stockouts, substitutions, and back orders? What is inventory turn at each level and by product category? What is the analysis at each level of fast-moving, slow-moving, and obsolescent inventory?

10. Wholesale comparable analysis: If the company makes a significant amount of sales on a whole-sale or other mediated basis, prepare an analysis comparable to that regarding the point of sale, sales volume by product, and so on.

11. Sales and distribution analysis: Based on the above, and as relevant, chart the company’s sales through distribution channels, indicating mark-up or other cost at each level and the associated method/timing of transport. Does this analysis suggest possible cost-reduction and efficiency moves, such as following:

- Elimination or consolidation of duplicated or overlapping sales/service outlets
- Elimination or consolidation of duplicated or inefficient distribution paths use of centralized warehousing
- Creation of additional distribution centers
• Negotiation of better transport contracts or integration of the transport function.

12. Possible weaknesses or anomalies: Is the distribution system subject to channel stuffing or “field warehousing”? What portions of sales are made on consignment or on approval? What is the experience with returns and change backs? What are the possible effects of FIFO/LIFO/average basis accounting as used by the company and others in the chain of distribution, such as retailers- for example, what are the dynamic or pressures relating to inventory management in different price scenarios?

13. Sales force analysis: What are the sales channels? Who employs them, or are they independent agents/distributors? From the company’s point of view, how are they organized (by product, by region, and so on), and how are they compensated (salary, commission, and so on)?

14. Channel management: what are the sales channels? Is there real or potential channel conflict, and is it being managed? Does company organization maximize sales overall, or are business units competing with each other for the same business? Describe any existing areas of channel conflict, and describe the effect of the proposed transaction in terms of channel conflict.

15. Systems analysis of sales and distribution: What is the state of systems support of product or service delivery? Consider physical and logistical aspects such as the following:

• The order-processing and order-fulfillment process from a systems perspective. Are there any possibilities for automation or for enhanced support of sales personnel? Are sales data fully
exploited for marketing implications for IT support of this function?

- The state of inventory delivery to or availability at point of sales: Is that inventory sufficient, and is the product mix correct? If the company sells through a retailer or other agent, is inventory management executed in a coordinated fashion resulting in optimal product delivery and sellthrough?

- Are the logistical aspects of product transport and delivery? Optimized by actively managing scheduling?

- Are the logistical aspects of inventory storage and handling optimized by use of coding, warehouse management, standardization of materials and packing, and so on?

- How does information about sales make its way back into inventory ordering and management system? How does it make its way back into product design and marketing? How frequently and on what basis?

- Are there opportunities for rationalization of the sales and distribution system, such as streamlined order processing; smarter coding and packaging; improved tracking; use of computerized stock picking and automated packaging; improved IT-based scheduling systems, including loading dock scheduling and like; integration of scheduling systems with those of transporters; tighter design of inventory management by use of current sales date and automatic or rapid replenishment/ redirection strategies?

16. System flexibility and responsiveness: How much flexibility and responsiveness is built into the sales and distribution system, and can it be increased (at what cost?) How sophisticated is the company’s rapid replenishment capability, how far back into the production process does it go, and what is the customer’s ability to change or cancel orders?
How does the company deal with unhappy customers or those who change their minds after order fulfillment has been completed? What is the IT support for the above?

17. Outsourcing: If aspects of sales/distributions have been outsourced, describe. What are the benefits and possible negative aspects of this outsourcing?

18. After-sale
   - What are the company’s responsibilities after sale?
   - What are the company’s policies on returns or exchanges?
   - What are the company’s policies on warranties? What is the associated pricing if any? What is the company’s experience? Assess the cost of warranties to the company, and analyze the warranty reserve, if any.
   - If the company provides after-sale service, what are the terms and pricing? How well is it performed? If there are call centers, are they staffed and organized to optimize response against cost, using queuing theory, IT support at the phone level, and knowledge management tools to assist personnel? Analyze these systems and their cost.
   - If service is at the customer’s location, how is availability and training of personnel managed?
   - How is customer satisfaction measured? Be specific.

19. Brand management: By product or product category, describe the company’s branding strategy or other corporate identify as it is intended to be perceived by the public, including customers. How is the company’s brand managed across product categories and across borders? Is there a corporate brand that serves as an umbrella across subsidiary brands? Comment on how the branding online and intra company.
Comment on how consistent the branding strategy is with the corporate culture, and if there is a mismatch, how that is managed. Do any of the aspects of the proposed transaction pose a challenge in term of managing brand? and

20. Brand product design and positioning: How is the company’s branding strategy translated into product or service design and engineering and product positioning, including pricing? Does branding strategy and market information get communicated effective to R&D, engmeerIng, and others who interact with the public, including customer service call centers and the like?

21. Outside consultants and advertising agencies: Describe the company’s relationship with corporate image consultants, PR firms, and advertising agencies around the world. Are any firms or individual especially important in this regard? Does the company itself do most of the global coordination in house, or do out- siders handle it?

22. Value of the brand: What is the estimated value of the brand? Does proposed transaction pose any threat of diluting brand s for the value?

23. Implication integration plan: Do any of the above points suggest potential cost saving through streamlining of the sales and distribution channels or potential product or market extensions, product repositioning, or different or additional branding and marketing strategies?

24. Implications for projections, negotiation, and pricing: How strongly does the information regarding customers, Products, and market support deal assumptions about projected revenues? In particular, if revenue growth for certain product lines is assumed, does the
information gathered point to clear paths—through product or market extensions, acquisition of new customers, or higher sustainable price points—through which the increase in revenues can be achieved? Discuss the implication for deal negotiation and pricing.

25. Extraction, manufacturing, or other production of goods and services: Assuming the target’s market and planned products/services have been defined above, assess in general how well the existing manufacturing or other production system is set up to profitably meet market demands (giving effect to possible divestitures for antitrust or other reasons).

26. Geographic map of production capacity: Review the map of productive capacity against customers needs on a geographic basis. Indicate overall industry capacity for the relevant markets. Tie product sales estimates arrived at above to production capacity.

27 Process and process unit: Describe the process of production or provision of services at a schematic/technical/engineering level. Categorize the work in terms of work flow as special order, batch process, line process, or continuous flow analyzes the critical inputs into the production process:

- Capital investment, know-how, plant design or specialized machinery,
- Skilled labor, pool of available labor. Is the company’s use of these inputs consistent with industry norms? Better? Worse?

28 Process flow analysis: Within a physical plant or between physical plants and including approval processes, transport stages, and all other stages of critical path or other comparable basis, with special attention to the following:
• How production tends to relate to production schedules, and how production schedules related to sales forecasts, specific orders, and so on.

• Defective production, excess production, returned goods, and warranty claims.

• Idle time and downtime, for all reasons (differentiate among reasons). Waste and scrap.

• At all points in the process, damaged or obsolete stock/inventory.

• Absenteeism, accidents grievances, overtime, employee turnover.

• Whether design and ongoing production reflect sophisticated operations management tools, such as economic production order quantities, time and motion studies, queuing theory, and so on.

• Capacity /throughput mismatches creating bottlenecks.

• Bottlenecks due to approval requirements or other management processes (especially where approval from 3 different location or time zone is required).

• Excess inventory buildups (with associated working capital cost).

• Critical inventory and spare parts requirements management against lead time (where disruptions in supply will immediate stoppage).

• Flexibility for product change (for example, setup time required, batch size, potential to re-order custom steps toward the end of the production process).

• Associated IT or Other information-based or automated support of the process, such as tracking.
29. Outsourcing: Is some of the production outsourced? If so, describe the extent to which the company can control execution against specifications, and how quality control is managed, particularly in light of timing considerations. Assess the pluses and minuses of the outsourcing arrangements. Are there potential environment liabilities, social obligations, or other costs, liabilities and risks associated with the production outsourcing?

30. Risk analysis based on process flow: Identify the most significant risks associated with the process flow and their impact on the business. Is backups work-around or replacements available? Is insurance coverage for the risk available on it cost-effective basis? What risks cannot be either mitigated or insured against?

31. Review of physical plant: Describe in detail the physical plant and facilities of the company:

- Type
- Location
- Size/capacity/throughput measures
- Measures of utilization, including as a percentage of Capacity
- Level of downtime, exclusive of scheduled maintenance
- Scheduled maintenance and associated downtime
- Quality of output
- Age, original cost and method of depreciation
- Depreciated (book) value
- Market (appraised) value
- If leased, terms of lease
- Remaining useful life
- Adequacy of warehousing/storage
• Associated environmental facilities
• Social obligations (housing, medical, family care, schools roads, parks, other)
• Facilities related to social obligations (medical of day-care facilities, other)
• Materials handling methods (pallets, conveyors, forklifts, trucks, vacuum or magnetic lifting or moving devices)
• Proximity to transport
• Utilities infrastructure support
• Climate and nature hazards (Flood, Volcano, earthquake, tornado, hurricane, rain, snow)
• Building code and zoning
• Real estate taxes and other fixed costs
• State of title (including leasehold title); lines and condemnation proceedings
• Insurance coverage
• Safety and security features
• Maintenance costs; capital improvements

32. Review of machinery and equipment: List and describe principal machinery, noting the following:
• Age, original cost, and method of depreciation
• Depreciation (book) value
• Market (appraised) value
• If leased, terms of lease
• Remaining useful life
• Maintenance
• Health and safety issues
• Auxiliary equipment - tools patterns, materials handling equipment.

33. Quality of technology: Describe the technology used in overall terms: Is the company an industry leader in advanced, high-quality technology? Is its applied technology the most modern? What is risk of rapid obsolescence? How the technology does used rank in terms of production efficiency (inventory, utilities, workers needed, maintenance requirement, and periodic capital improvements)? Is there a rival technology being utilized or upcoming that will create competitive difficulties for the company or render its technology obsolete?

34. Quality control: What is the company’s quality structure? Are the company’s facilities, ISO-compliant? What specific quality control measures are used (Total quality Management, Statistical Control Processes, Six Sigma, and so on), and what is the management structure for dealing with quality control problems?

35. Review of engineering platforms and standards: Describe in detail the engineering platforms and standards used in production. If it is assumed that the production process will be spread among different facilities in order to optimize capacity utilization, have the underlying assumptions been identified and checked out engineering platforms, measurements and standards, languages used by engineers, and so on? How long will it take for manuals, processes and standards to be written down and harmonized to enable dispersed production? How will conflicts that arise in this process be resolved?

36. Analysis of capacity on a combined basis: What does the analysis of process flow suggest about excess, duplicate, or inadequate capacity at one or more points of production? Analyze desirable
production capacity, after smoothing within the system, against expected sales volume.

37. Excess capacity: If there is excess capacity, how should the determination to reduce capacity be made, and what is the plan for disposition or shutdown? What would be the financial consequences (on an accounting and cash basis) of disposition or shutdown?

38. Additional capacity: If the analysis suggests that additional capacity is required, where would it be located and what would it consist of? How long would it take to get online? What are the costs? Are there regulatory or other barriers to the planned expansion?

39. Production cost structure analysis: If the analysis suggests the need for investments to improve the production cost structure, quantify the cost of those improvements, taking into account the time required to effect the changes. Weigh these against the expected operating cost reductions.

40. Tie production to cost accounting: What are the company’s policies for cost accounting? Are these consistent with industry norms? Tie these to the process flow analysis above, and reconcile for each company in the transaction. What is the relationship between fixed and variable costs, the break-even point, and the relation of volume variances? Is the company’s production process satisfactorily profitable on a cost accounting basis? What is the range for gross margin (by product or product category as relevant) based on the price assumptions made in the projections and supported by the marketing analysis above?

(iii) procurement and Supply-Chain Management- External Infrastructure Requirements
1. Raw materials, intermediate inventory, and supplies needed: Analyze the company’s need for raw materials, intermediate inventory, and supplies, based on the market and capacity analyses above. Based on the process analysis above, describe critical items and associated lead times.

2. Cost raw materials, intermediate inventory, and supplies: Do raw material, intermediate inventory, or supplies needs represent a vulnerability to price volatility or constricted supply? Track the percentage relation of these components of production to price levels for finished goods, and for each category describe future price trends and market conditions. Assess how much risk the company is taking with respect to these inputs to the production process.

3. Supplier analysis: Describe suppliers by category of product and volume. Where they located? Are they stable financially? Are there multiple suppliers for specific needs, or backup suppliers? Which suppliers are dependent on the company’s business, and to what extent? On which suppliers is the company dependent?

4. The procurement system: What is the procurement system?
   - How centrally managed is it?
   - Does it balance cost saving and efficiency with design and quality control?
   - To what extent does the company use a formal purchasing manual based on order quantities, up-to-date vendor evaluation files (covering delivery on order information), and a formal program for reviewing the value and quality of purchased materials? What procedures are used in procurement? How are costs compared, and how is purchase approval given?
• What are the circumstances in which goods may return? How flexible is procurement system in dealing with changes in customer orders or fluctuation in sales?
• Does consolidation or streamlining of procurement represent future potential cost savings? If so, quantify.

5. Long-term contracts: If there are long-term contracts, describe the process for reaching agreement on them, their status, and in what circumstances they would be favorable and unfavorable to the company.

6. Utilities and other infrastructure support: Analyze the company’s need for utilities (including water supply) and other infrastructure support, such as transportation and communication. Are these facilities all available on an assured basis, or can back-up be arranged if there is a problem? Are there potential cost savings here or does infrastructure a vulnerability to price volatility or constricted supply?

7. Support for facility expansion: If there is a decision to expand the facility are sufficient supplies of the following available at the selected location?
  • Manpower with the right skill levels
  • Utilities, transportation, communication, and other infrastructure support
  • Raw materials and supplies on a secure and cost-effective basis
  • Real estate at appropriate pricing with appropriate zoning

8. Supply-chain analysis: Analyze the logistical of supply chain in light of rationalized production capacity. Are there potential cost saving in the supply-chain structure, such as streamlined order processing; smarter coding and packaging; improved tracking; computerize stock
picking; auto-mated packing, improved IT-based scheduling systems with those of transporters; tighter design of inventory management by use of current sales/production data; and automatic or rapid reordering/redirection strategies?

9. Supply-chain risk analysis: Are there vulnerabilities in the supply chain- to shipping disruption, transportation price volatility, currency risks- and if so, is there available work-around, or are these risks inherent to the production process?

10. Collapsing the supply chain: Are there potential efficiencies in combining the company’s supply chain to the point of production/shipping with the distribution/sales to customers?

(iv) Analysis of information, Technology, Communications, and General Systems Support of the Vale-Creation process; intellectual Capital and intellectual Property

1. Traditional MIS: Describe the management information systems of the company as they relate to traditional NIS functions: payroll, benefits, payables, receivable, cost accounting and financial accounting generally. What is the target company’s hardware configuration for data processing and for networking? What is the target’s software platform-venders, operating systems, database management system, programming environments, and software applications- and how integrated is it across company units, both functionally and geographically?

2. Integration for MIS: What does an integration plan for traditional MIS look like? Can apply, and are there any items that do not really need to be integrated? What is a realistic time frame for MIS
integration, and how can functions be maintained with minimal disruption for that period?

3. ERP: Does the company have an ERP system or other partially or fully integrated IT system? Which one? Describe implementation, vendor and contracts.

4. Other valuable IT systems and assets: Does the company have other valuable systems or processes that are IT-based, such as

- Online order or transaction processing
- Online search, tracking, or other information-retrieval systems
- Knowledge-sharing systems, such as a firm intranet or other groupware
- Engineering platforms such as computer-assisted design systems
- Computer-based scheduling or routing systems
- Document production systems that go beyond general office needs
- Special mathematical or engineering data-modeling or data-processing support, such as that required for minerals extraction
- Decision support systems
- Robotics
- Sensing, feedback, and control mechanisms in extraction or production
- Large database support of, for example, customer relationship management or R&D.

5. System assessment; IT personnel and budget: For any of the items above that are fundamental to the business, a full-scale assessment of hardware (data storage, processing, and network) and software adequacy, scalability, and robustness of the systems is required. Security
and backup are both very important to most of these types of systems, as is error-free ordinary operation. For all such systems: What level of personnel support is required? What are ongoing maintenance costs? How long to obsolescence? Are there multiple systems, and should some standardization be imposed? How is procurement managed?

6. Ownership; vendor relationships: Does the company own the rights to its IT systems, or are some aspects of the systems operated under license? What is the company’s position in term of vendor lock-in? How vulnerable is it to force and roundrobin u-grades and price increase? Are some aspects of the company’s IT systems proprietary to it, and if so, are these proprietary aspects treated as confidential of otherwise as protected as they can be from duplication by competitors, including departing employees?

7. Outsourcing: Are any of the company’s IT functions outsourced? Describe the arrangements, the vendor (including the vendor’s stability), and the backup and recovery systems. Describe the pros and cons of the arrangements.

8. Systems risk analysis of the IT systems: Describe the systems risk inherent in the company’s IT infrastructure and such issues as redundancy, backup, crashes, and how often do these occur? What is the tolerance for IT failure in terms of the company’s operations?

9. Intellectual property and know-how; licensing: What intellectual property underlies the company’s value-generating processes? Describe these including processes or branding concepts that might not be written down or that might not fall within a legal definition of intellectual property. Describe all licensing agreements and their terms.
10. Ownership of intellectual property: Does the company have the right to use of its important know-how? What is the risk of infringement claims? How much of the company’s valuable know-how is property to the company, and of that how much is entitled to legal protection and under what rubric- e.g. trademark and trade name, patent, copyright, trade secrets? Has the company taken all appropriate steps to protect its rights in its cross-border implications (in what countries are the company’s intellectual properties protected, and so on).

11. Product development and innovation: Assess the company’s general product development and product innovation experience and strengths in design, engineering, and general creativity and responsiveness.

12. Cross-border implications: For each aspects of the constituent companies’ important know-how that it is assumed will be applied cross-border after closing: Must such know-how be tailored to local needs and conditions? Will the know-how retain its protected character it transplanted to the new site? How easy will be for competitors to copy the know-how?

13. R&D generally: How important is R&D to the company and to competitors? How does the company’s R&D budget compare to those comparable companies, as a percentage of sales and against other measures? How successful is the company at turning R&D into valuable products/services over a reasonable period time? How integrated is the company’s R&D efforts with its marketing strategy (or how relevant is its marketing strategy to its R&D effort)?

14. R&D facilities and capabilities: Describe in detail the R&D facilities, capabilities, and directions of the company and define areas of
overlap or obvious areas of extension for the combined enterprise. Are
there opportunities for cost reduction or important new initiatives in
combined R&D functions?

15. IT and intellectual property/know-how overview: Of all of the
company’s IT-based systems and other know-how noted above, are some
elements so valuable that they constitute a critical aspect of the value
proposition? If so, are they fully understood, and is their legal status and
confidentiality protected as fully as possible? Can the associated systems
and know-how be successfully scaled and deployed across borders in the
combined enterprise?

16. IT systems overview: What knowledge and information
requirements of the combined enterprise cannot be met through
combination and integration of the existing information system? What
are the budget and timetable for these, and can they be grafted into the
more basic IT infrastructure?

(v) People Analysis: Management Structure, Labour Relations, Corporate
Culture, Recruitment and Training as Related to Operations

A. Management Structure from an Operational Perspective

1. Management structure and lines of reporting: Document the
official lines of reporting, and comment on management
communications formats that do not coincide with the formal structure.

2. Management structure and business units: How does
management structure translate into operational/production functions,
entities, or units such as:

- Factories/mines/other facilities for extraction/production
  (manufacturing)
- Professional and production offices and studios (professional services firms, media)
- Networks and systems (transportation, communication)
- Sales outlets and customers service centers
- Corporate office: corporate-wide systems such as accounting and finance, legal, information systems, procurement, brand management and marketing, engineering, R&D, and quality control.

3. Management operations across borders: Are there any country/regional managers? How autonomous is the country manager, and how do country manager roles integrate corporate-wide decision making? Are there matrix management structures or other processes in place to coordinate country practices and policies within a global strategy?

4. Identifying key personnel (non-management) from an operational perspective: Which non-management categories of personnel are key from an operational perspective? Consider the following:
- Creative
- Writers and editors (media) - Designers (retail/manufacturing)
  Marketing
- Scientists and engineers
  : Systems and operations engineers (airlines, other transportation, telecommunications)
  : Doctors and other health professionals and researchers (Pharmaceuticals, health care)
  : Design engineers (automotive, other manufacturing)
  : Software engineers, electrical engineers (information Technology)
Mining, construction, mechanical, or other engineers (Extraction, construction, manufacturing)

- Finance/legal/other professionals
  - Lawyers, accountants, consultants
  - Bankers
  - Pilots (for an airline)

- Sales and customer-relationship-management
  - Sales and marketing personnel

- Skilled and unskilled production labour
  - Office staff (for a professional services firm, for Example)-
  - Factory skilled and unskilled workers (Manufacturing firm)

For the target and the combined company, rank the relevant categories, and set forth the analysis and implications for integration strategy:

- Are there individuals or teams in this category so essential that losing them after closing would negate the value of deal? Those people can take the value of the business with them or become competitors (for example, key bankers leaving after a bank is acquired star sales managers leaving an advertising agency, the most productive software engineers leaving a software development firm).

- Is one category of personnel so essential that managing that group as a whole is key element of the deal (for example, airline pilots for an airline, and doctors for a health care organization)?

- Are replacement personnel available?

- Will there be personnel redundancies post deal? How will these be deal with?
For existing personnel, consider in general terms their numbers, location, work performed, compensation, and terms of employment (including union or other contracts).

B. Operational Questions across Categories of Personnel

5. Workers and planned strategic Initiatives: Review all categories of workers in light of strategic initiatives for the combined company. Will strategic redirection reengineering of processes render some workers unneeded, or will new categories of workers be required?

6. Recruitment and training: How are workers recruited and trained? Is recruitment and training appropriately geared to operational needs?

7. Workers and process review: What are the general terms of employment as they relate to process design and other operations matters, such as shift length vacation expectations, and flexibility in learning new skills and being rooted into different jobs? Will these need to be reconciled between the companies after closing, or reconfigured in order to implement new process designs, and if so, how?

8. Workforce integration: Will there be integration of workforces? If so, what impediments are there to smooth integration (such as language barriers)?

9. Workforce reduction: If a workforce reduction is contemplated, how will that be executed, keeping in mind the need to retain motivated staff? How much will it cost—soft costs as well as hard costs?

10. New hires: If the combined enterprise plans relocation or expansion, or if new facilities or lines of business are planned, will new employees be required, and are they available?
11. Social obligations: Does the company have social obligations to its workers, such as requirements to provide or fund housing, schooling, or medical services? What is the basic infrastructure available to employees to meet these needs? How do these obligations potentially affect operations?

C. Corporate Culture and Operations

Compare the corporate cultures of the parties to the transaction in terms that seem most useful to the deal structure and to developing an integration plan from an operational perspective.

12. General aspects of corporate culture: Some markers or attributes that might be considered in terms of how employees work together might be these:
   - Relative rankings of jobs as perceived in the companies, importance of formal hierarchy
   - Formality, style of dress, office configuration, open doors or closed doors.

13. Communications formats: What are the formats for various types of communications, such as:
   - Meeting scheduled in advance with/without prepared agendas
   - Impromptu meeting
   - Memos, e-mails, voice mails
   - Formal reporting lines versus back channels
   - Formal committees versus 'kitchen cabinets"
   - Collaborative work

14. IT support for communications: Is there adequate IT support for IT-based intracompany communications (for example, e-mail, an internet, or other groupware is important for intra company
communication, quality control and promulgation of standards, and collaborative design and engineering)?

15. Knowledge sharing and knowledge management: What is the attitude about information in the enterprise: Is it shared, or do individuals tend to keep their knowledge to themselves? If knowledge is shared, is that solely through informal means or by way of formal training formats? What are the implications for IT support of knowledge sharing and transference (for example, for worker training and rotation)?

16. Company approaches to systems design: Are employees rewarded for exercising initiative or for acquiescence in management instruction? How free do employees feel to question their superiors? How comfortable are managers with, questions or challenges from those they supervise?

17. Documentation of systems design: Are work processes and practices fluid and open, or do they tend to be rigidly defined role bound? Do work processes and practices tend to be documented, or is there more of an oral tradition?

18. Conflict resolution and change management in integration planning and systems design: How do employees react to things that they don’t agree with? Do they have a forum for discussing and resolving issues with management, or will dissatisfaction show up in other up in other ways? Are people more or less comfortable with group or consensus decision making in comparison to individual Leadership? How important is it that groups validate leaders’ decisions? What is the mechanism for creating “buy-in,” and has this process been considered in integration planning at a practical?
19. Life-balance issues in operations planning: How permissible is it to acknowledge the importance of family or personal life, and how flexible is the company in accommodating the family and personal lives of their employees?

D. Background Culture Questions Affecting Operations

20. Language: What is the dominant language used for spoken and written communications, within the company and with suppliers, customers, and investors? Are there enough persons with multilingual capacity to bridge the language gaps?

21. How things really get done?: Does the background culture accord a significant amount of weight to long-term contracts, or are the most importance relationships or aspects of relationships likely to be undocumented? A related question: How is business agreements reached? Are key decision makers interested in and patient with lengthy and detailed negotiations? Or do they rely more on establishing personal bonds with their correspondents? Do people enjoy haggling, or do they avoid it?

22. Importance of documentation and record keeping: Are things generally written down or otherwise recorded and kept? How important is record keeping and the memorialization of events and decisions/ How important are formal and written inquiries and justifications? To what extent is arbitrariness accepted?

23. Transparency to outsiders: Do companies routinely share information with outsiders, such lenders, investors, or the press, or are information closely held? What types of information are shared with vendors, suppliers, and customers, and on what terms?
24. Involvement of equity owners: Does the ownership structure of the company have an impact on operational decisions— for example, has common ownership resulted unfavorable or unfavorable business relationships with vendors and suppliers or customers? Is the background culture one in which professional management is given a great deal of leeway day to day or one in which equity owners are likely to be involved in operational issues?

25. Attitude toward rules and protocol: Do people tend to follow written rules and procedures to the letter or take a more relaxed attitude?

26. Attitudes toward accounting standards, taxation, and regulatory compliance: What is the company’s attitude toward these requirements?

27. The basis of customer relationships: How would you characterize typical business-to-business transactions and business-to-consumer transactions? For example, is there more emphasis on a branded or otherwise consistent corporate identity or on local/personal relationships? In what circumstances are purchasers entitle to refunds and exchanges? What are the most effective channels for marketing and production/company communication?

28. Social contract with workers: What is the background understanding about the social contract with workers? Among government, the family, and business, who bears the costs of various risks to workers: unemployment, health, family care, retirement, and need for retraining? What are the long-term obligations assumed by a company when it hires an employee?

29. Attitude toward change: Is change “and rapid response valued, or do people tend to value tradition, the status quo, and stability?
Due Diligence Check list

C: Legal Due Diligence

(A) Corporate Documents of the Company and Subsidiaries

(1) The latest Memorandum and Articles of Association of the Companies and its subsidiaries.

(2) Minutes of all Board of Directors, committee and shareholders meetings and all circular resolutions passed.

(3) List of branches and offices in different States from where the business is run.

(4) Material information or documents furnished to shareholders and to directors during the last two years.

(5) Copy of Annual returns and form 32 filed for the last two years.

(6) Copy of charge registered.

(B) Issue of Shares

(1) Shareholders, debenture holders, if any, information, indicating number of shares/debentures held, dates of issuance, and subscribed amount;

(2) All stock options, stock purchase and other employee benefit plans and forms of agreements.

(3) List of any outstanding stock option.

(C) Material Contracts an Agreements

(1) List of banks or other lenders with whom Company has a financial relationship (briefly describe nature of relationship-lines of credit, etc.);
(2) Mortgages, financial or performance guaranties, indemnification, liens, equipment leases or other agreements evidencing outstanding loans to which the company is a party or was a party within the past two years.

(3) All material correspondence with lenders during the last three years including all compliance reports submitted by the company or its accountants.

(4) List of major clients and their locations.

(5) Any other material contracts.

(D) Litigation

(1) Copies of any lawsuits involving the company or the subsidiaries;

(2) Summary of dispute with suppliers, competitors or customers.

(3) Correspondence with auditor or accountant regarding threatened or pending litigation, assessment or claims.

(4) Decrees, orders or judgment of courts or governmental agencies.

(5) Any settle made in any of the litigations and if so documents relating thereto.

(E) Employees and related information

(1) A management organization chart and information on managerial personnel.

(2) Summary of any labour agreement and disputes, if any.

(3) Notes concerning pending or threatened labor disputes, if any.
(4) All employment and consulting with officers, directors, key employees and related parties.

(5) Schedule of all remuneration paid to officers, directors and key employees for most recent fiscal year showing separately salary, bonuses and perquisites (i.e. use of cars, property, etc).

(6) Summary of employee benefits and copies of any provident fund trusts, gratuity trusts, pension schemes, and other employee benefit schemes and related documents.

(7) Confidentiality agreements with employees.

(F) Immovable property

(1) List of all immovable properties owned by the company.

(2) Documents of title, mortgages, and other security agreements pertaining to the properties listed in (1) above.

(3) All outstanding leases with an original term greater than one year for immovable property to which the Company is either a lesser or lessee.

(4) Documents pertaining to any copyright or patent fillings.

(G) Taxation

(8) Income tax, Sales tax returns for the three years.

(9) Details of all pending assessments before Income-tax, Sales tax, customs and Excise authorities

(10) All pending litigation relating to the above taxes and/or

(11) Evidence of company being up to date on income-tax deduction at source, sales tax, service tax, professional tax, payment of provident fund, and other tax payments.
(H) Insurance and Liability

(12) Schedule or copies of all material insurance policies of the company covering property, liabilities and operations, including product liabilities,

(13) Schedule of any other insurance policies in force such as “key man” policies or director indemnification policies.

(14) All other relevant documents pertaining to the company’s insurance and liability exposure, including special reserve funds and accounts.

(I) Joint venture or collaboration Agreements

Copies of any Partnership agreements or joint Venture Agreements or collaboration agreements.

(J) Governmental Regulations

(15) Copies of all permits and licenses necessary to conduct the Company’s business.

(16) Copies of all approvals received from the Government authorities relating to issues of shares to non-residents, export credit obtained etc.

(17) Copy of all filing with Securities Exchange Board of India and Stock Exchanges and Approvals, if any, taken.

CONCLUSION

Merger and Acquisitions are most impotent strategic tools for the corporate restructuring of business. The assets and liabilities of acquired company transferred to the acquiring company. The basic difference between these two terms is that, in case of merger, the merging company
loses its identity, while acquiring company maintains its identity. In case of acquisition or takeover, however, acquired company maintains its identity, only a change in ownership takes place. Both these methods have been traditionally used for business consolidations, increasing market share and diversification of risk through diversification of operations.

In last two decades M&A activity has been seen across the world for restructuring and consolidation in various sectors. In India also after linearization opportunities for external growth is increased due to simplified legislation and reduction in control by the government. Corporate restructuring activities In Indian industries made business combinations effective empower companies to gain core competencies, adopt new technology, expansion of business in new market, and to achieve significant growth. However, it matter of great concern that number of mergers have been resulted in failures in spite their best efforts in due diligence pre-deal and post deal require to ascertain what determines their success or failure.

In subsequent chapter, review of literature and analyze M&A deal that have taken place in India and abroad have been included. Efforts have also been made to examine success or failure of these deals.

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