COMPARATIVE ANALYSIS OF THE EFFECT OF MERGERS AND ACQUISITION ON STAKEHOLDERS: INDIA & USA

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Abstract

Mergers and Acquisition is the consolidation of companies or their major assets which is done to facilitate the growth of the company through market and product extension. This helps the company in reducing the competition and take benefits of economies of scale. Though these transactions can prove to be a great opportunity but at the same time they can have negative impacts on the stakeholders of the company. Many micro and macro factors are responsible for the effect of Mergers and Acquisitions on the stakeholders of the company which includes the take of the market when such news is first released, terms and conditions of such deal, the post and pre-integration formalities. This paper focuses on such impacts of Mergers and Acquisition transactions which can lead to losses for shareholders, employees, and government. This impact on shareholders varies depending upon the rules and regulations of a particular area guiding such transactions. It also varies as per the demand patterns of consumers, corporate governance policies as prescribed by the law, and the resource availability of companies in such areas. Hence, this article further compares the laws present in USA and India regarding Mergers and Acquisitions and the lacunas in their respective laws. It also covers suggestions for the introduction of certain USA provisions in the Indian statutes governing the rights of shareholders, employees, and government. USA being a developed country have mature laws on the subject of mergers and acquisition along with its anti-competitive laws present under the Sherman Act. This provides India a great opportunity to learn from such mature provisions and inculcate the required laws as per requirements which includes a more inclusive ownership structure by providing rights to minority shareholders. The article also mentions certain rules and regulations which provide a better stand to these shareholders in India than in the USA. Thus, praising the legislatures for forming such laws.

Keywords: Mergers, Acquisitions, Stakeholders Competition, SEBI, USA.

Introduction

With the coming up of new companies and the cutthroat competition, a company must strive hard for its survival, profits, and growth. A company should grow both externally and internally if it wants to gain profits. Where the internal growth of a company depends upon introducing new products and sales, the external growth is a result of various processes like merger, amalgamation, acquisition, takeovers, etc. It refers to the consolidation of companies or their assets through various financial transactions.[1]

A merger refers to a contract that combines two or more companies into one with profit as their motive. Whereas acquisition refers to the process through which one company acquires another. Desire to increase the market share, access new markets and technologies, achieve economies of scale, and reduce competition serves as major motivating factors leading to Mergers and Amalgamations.[2]

The impact of M&A on shareholders, employees, and government varies on several factors, including the terms and conditions of the deal, the take of the market on such merger or acquisition, the post-merger integration process, etc. The process of mergers and acquisitions can lead to both profits and losses it depends upon the due diligence exercised through a comprehensive review of the target company's finances, operations, and legal issues to calculate the potential risks and opportunities. The success of M&A activities depends on several factors, including the strategic fit of the companies, the ability to achieve synergies and cost savings, and the effective integration of operations and cultures.[3]

Mergers and acquisitions have different effects on the stakeholders of different countries because of the difference in their regulatory framework, and market conditions which include the market sizes and demands for the product or service of the company. This paper deals with a comparative analysis of mergers and acquisitions on the stakeholders in India and the USA. It mainly focuses on shareholders, employees, and the government. Its further deals with the lacunas in the Indian laws protecting the rights of shareholders, government, and employees.

Shareholders

Mergers and Acquisitions in a company can have both positive and negative impacts on the shareholders of the company.

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[1] Richard A. Shick, *Mergers Benefit to Shareholders of Acquiring Firms,* 3 FIN MGMT., 45-50 (1974).
[2] Dennis C Mueller, *Mergers and Market Share,* 67 THE REV. OF ECON. & STAT., 256-267 (1985).
[3] Richard Rosecrance, *Mergers and Acquisitions,* 80 THE NAT'L INT'S, 65-73 (2005).

- **Stock price:** Since the profits of the shareholder depend mostly on the price of companies share. Such prices can either decrease or increase with the announcement of a Merger or acquisition taking place in a company. This price change depends upon how the market is perceiving the deal. If the market believes that such a merger will create value for the company then the stock price of the company goes up otherwise it might fall drastically leading to losses for the shareholders. [4]
- **Cash or stock consideration:** At the time of the merger or acquisition of a company the shareholders may receive cash, stock, or both as consideration for their shares in the company. The type of consideration they receive at the time of M&A describes their future with the company, if they receive the cash, they can opt for investing out of the company but if they receive stock their relationship with the company strengthens.[5]
- **Control of the company:** Depending on the type of Merger and Acquisition the control of the existing shareholders of the company may dilute. In case the acquiring company has a major stake then the stakeholders will lose their control which can be positive and negative both depending upon the goals and expectations of the stakeholders.[6]
- **Synergies:** Mergers and Acquisitions lead to synergies and cost savings which increases the companies. Combining two companies leads to economies of scale, which refers to the decrease in the cost per unit of output with the increase in the size of the operation. It also gives rise to cross-selling opportunities and a reduction in procurement costs. This ultimately increases the profits of the company.[7]
- **Integration Risk:** Mergers and acquisitions might lead to integration since they are complex in nature, this might lead to negative impacts on shareholders, and this might be due to increased costs and decreased performances.

Since Mergers and acquisitions impact shareholders who are the major stakeholders of the company since their hard-earned money is invested in the same, so stringent regulatory framework is needed for the same. In India, there are several rules and regulations in place to protect the interests of shareholders at the time of mergers and acquisitions (M&A). This includes the ***Companies Act, 2013***[8] which makes it mandatory for the company to take prior

[4] Samuel C, *Merger and Acquisition Valuation,* 20 FIN. MGMT., 85-96 (1991).
[5] Richard J Rosen, *Merger Momentum and Investor sentiment: The Stock Market Reaction to merger Announcements,* 79 J. OF BUS. 987, 1017 (2006).
[6] Josoph P. H, *On the Patterns and Wealth Effect of Vertical Mergers,* 79 J. OF BUS. 877, 902 (2006).
[7] Myles J., *A Paradox of Synergy: Contagion and Capacity Effects in Mergers and Acquisitions,* 31 THE ACAD. OF MGMT. REV. 962, 976 (2006).
[8] Companies Act, 2013, No. 18, Acts of Parliament, 2014 (India).

approval of the shareholders through a special resolution that requires a minimum of 75% of the votes cast by the shareholders. The company also needs to provide shareholders with information including the valuation report, the share exchange ratio, and the scheme of arrangements. Similarly, laws like the ***Securities Act of 1933***[9] in the US require the company to provide full and fair disclosure of all material information related to M&A transactions to their shareholders.

The Sarbanes-Oxley Act of 2002[10] was passed in response to corporate accounting scandals and includes provisions related to M&A transactions. The above act obligates the companies to maintain controls over their financial reporting and to provide shareholders with accurate and timely information about their financial condition.

Under the ***Securities and Exchange Board of India (SEBI) Regulations, 2011***[11] certain rules safeguarding the interests of minority shareholders have been provided which include a mandatory provision for acquirers to make an open offer to minority shareholders in case they acquire more than 20% of the shares of a listed company. ***The Securities Exchange Act of 1934***[12] in the US requires the company to disclose information about any material changes in their business or financial condition that may affect the value of the company's securities.

The Competition Act, of 2002[13] regulates M&A transactions to ensure that it does not lead to anticompetitive behavior or abuse of market dominance. Any Merger or Acquisition that will have a severe impact on the competition needs to go through the Competition Commission of India. ***The Hart-Scott-Rodino Antitrust Improvements Act of 1976***[14] requires companies to notify the Federal Trade Commission (FTC) and the Department of Justice (DOJ) before completing certain types of M&A transactions. This enables them to keep a check on antitrust transactions.

Under the ***Income Tax Act, of 1961***[15] the interest of the shareholder is protected by providing their company with tax exemptions and reductions for companies involved in M&A transactions, subject to certain conditions.

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[9] Securities Act of 1933, (U.S.A).
[10] Sarbanes-Oxley Act of 2002, (U.S.A).
[11] Securities and Exchange Board of India (SEBI) Regulations, 2011, Act of Parliament (India).
[12] Securities Exchange Act, 1934, (U.S.A).
[13] The Competition Act, 2002, No. 12, Acts of Parliament, 2003 (India).
[14] The Hart-Scott-Rodino Antitrust Improvements Act, 1976 (U.S.A).
[15] Income Tax Act, 1961, No. 43, Acts of Parliament, 1961 (India).

The Delaware General Corporation Law,[16] which is followed by many US states, provides a framework for the governance of corporations and includes provisions related to M&A transactions. The law requires that shareholders receive fair value for their shares in a transaction and provides them with appraisal rights if they disagree with the value offered by the company. Such a law does not exist in India.

In both India and the USA, shareholders can benefit from M&A if the deal creates value for the company. However, Indian companies tend to have a higher proportion of promoter ownership, which can lead to conflicts of interest and potential benefits to promoters at the expense of minority shareholders. US companies, on the other hand, have a more dispersed ownership structure, which can make them more vulnerable to shareholder activism.

Employees

To improve the effectiveness and efficiency of a company reorganizes its operations, management, and finances and that process is known as company restructuring. Examples of company restructuring are takeovers, buybacks of shares, mergers and acquisitions, spin-offs, etc. Mergers and acquisitions are known to be the most common type of company restructuring. One of the major stakeholders of a company is the employees. They are considered to be the backbone of the company. They are associated with an organization for commission. When a takeover or merger takes place, the employment contract gets invalidated. Job security is more dependent on presumptions, which Mergers and Acquisitions (M&A) tend to shatter[17]. Because of the role played by the employees, it becomes necessary to analyze the effect that employees have after M&A takes place. The effects are explained as follows –

- **High Workload**: When M&A takes place, the entire structure of the company changes. Owing to the changes, the employee has to work hard to adapt to the changes. He has to adhere as well as adapt to the new business strategies. Before M&A, the employee's attention will be focused only on one market but after M&A, they have to look after two to three markets. Due to the increase in the markets, the higher authorities of the company expect to derive more profit and hence they pressurize the employees. To achieve the goals of the company, the employees have to work more hard post the M&A.

[16] Delaware General Corporation Law, 1899 (U.S.A)
[17] Purbaja Sarmah, *Merger and Amalgamation of Companies in India: An Analysis of Its Impact on Various Stakeholders,* 1, AIJACLA, 320-330, (2021).

- **Job insecurity and uncertainty**: In the Companies Act, 2013[18] there is no legal provision that specifically deals with the protection of the employees when the merger and acquisition take place. During M&A, one company is acquired by the other. The company which acquires the other is in a safer position concerning the position of the employees. The acquired company's employees face job insecurity when compared with the acquirer company. Due to the uncertainty few employees might be relocated or can be assigned new jobs resulting in a change in their job profile and working conditions. According to research, the M&A activity in the business costs at least two hours of productive work for each employee due to confusion and multiple individuals.
- **Disagreement among the employees**: When the merger takes place, there is a merger of not only the shares, assets, etc. but a bunch of employees also. There are employees with different mentalities and backgrounds. The differences lead to conflict as a result of the difference of opinion. It becomes extremely important to maintain an amicable relationship among the employees if not it will not only have an effect on employees but even on the quality of the work in the long run.
- **Cultural differences**: According to the functions of a company, different cultures are adopted by a company. When the merger and acquisition take place, two companies come together which means, two different cultures come together. There will be a shift in the cultures and differences are bound to arise when employees from two different companies with different cultures come together. Employees may inherit the values and identities of their respective companies. Additionally, a quick move may cause cultural shock and the need to adjust to cultural differences. Employees' stress and anxiety can undoubtedly escalate if they are unable to adapt to a new culture.
- **Technological Changes**: Once M&A takes place, the company or firm tries to maximize their profit, and due to the advancement and the changes in technology, there is often fear for the employees about their replacement. If technology is adopted then the investment for human capital will eventually decrease leading to fear for the employees. There is already job insecurity prevalent among the employees and the technological changes that take place during the M&A can impact the employees.

A federal form of government is present in the United States (U.S.). When a potential acquirer chooses a company as an attractive acquisition or merger option, it is known as the target company. The target company which is incorporated falls under a dual jurisdiction in the state

[18] *Supra* note 8.

in which it is incorporated and under the federal government. When M&A takes place, there are both positive and negative effects on the shareholders resulting in organizational changes. The impact of the M&A differs based on the entity.[19] An economic impact is created upon the employees of a company when an M&A is attempted which might or might not be successful. The operation styles tend to get affected when a merger takes place as each company has its style of operation. The effects of M&A on employees are –

- **Retention Bonuses:** If the employees of the target company choose to remain with the company, then success is said to remain with the company when an acquisition takes place. For increasing the likelihood of the employees remaining with the company they are usually given retention bonuses or transactions that shall become payable to the employees. The bonuses shall become payable only upon the completion of the acquisition and not otherwise. Compensation agreements may also be entered by the acquiring company if the acquisition is closed.
- **Consideration of employees' interest by the target company**: When a potential merger or offer takes place, there is no necessity on the part of the target company to consult the employees. There is however an exception to this. In certain states excluding Delaware, there are certain statutes in the ***Securities Act of 1933***[20] and ***Securities Exchange Act of 1934***[21] that permit or require the target company to take into consideration the interests of employees while recommending an offer or approving a merger.
- **401(k) plan – Tax-free development of investment returns:** In the U.S., there is a qualifying profit-sharing plan's 401(k) element that entitles employees to set aside a percentage of their earnings for personal accounts. Except for Roth deferrals that are specifically specified, elective salary deferrals are not included in an employee's taxable income. Employers may make deposits into their employee's accounts. According to this, there would be tax-free development of their investment returns.

When any M&A takes place, there are ups and downs. The laws governing the M&A for India and U.S. are different and hence there are differences in the effect it has on employees too.

[19] Akansha Arora, *Post M&A - Effect on Employment*, 2 LAW Essentials J 411 (2021).
[20] *Supra* note 9.
[21] *Supra* note 12.

- In India, in the case of ***Sunil Kr. Ghosh & Ors. v. K. Ram Chandran & Ors***.[22], it was held by the Supreme Court that the consent of the employees has to be taken mandatorily before they are transferred to a new company even if there aren't any crucial changes in their working conditions. It should be done to establish healthy working conditions among the employees post-M&A. Whereas in the U.S., according to ***Delaware's General Corporation Statute (DGCL)***,[23] the acquiring companies are not mandated to consult the employees or take into consideration their interests.
- In India, retrenchment compensation is given to the employees when any disagreement takes place between the employees and the company. This was ordered by the Apex court to protect the employees from getting thrown from their jobs as per the company's fancies and whims. This is governed by ***Section 25FF of the Industrial Disputes Act, of 1947.***[24] In the U.S. employees are paid retention bonuses which are governed by the ***United States Constitution.***[25] But it is paid only after the acquisition is closed and no compensation is given to the employees if there is any disagreement unlike in India

Government

The government of every country is one of the major stakeholders in the company that operates within its boundaries. Any issue or activity of the company can have an impact on the government of the country. Such activities can have a negative as well as a positive impact, depending upon the activity. In the case of Mergers and Acquisitions, the effect can mostly be seen in the employment, tax, and competitive sector.

- **Employment and Economy:** When it comes to employment, merger and acquisitions can have a negative as well as a positive impact depending upon the job being created and diminishing from the mergers of two companies. This lack of employment can create a loop that can further lead to a situation of inflation in the country[26]. It can also have a positive impact by employing new people, which will further improve the economy of the country and contribute to the increase in the GDP of the country.

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[22] Sunil Kr. Ghosh v. K. Ram Chandran (2011) 14 SCC 320.
[23] *Supra* note 16.
[24] Industrial Disputes Act, 1947, § 25FF, 1947 (U.S.A)
[25] U.S. CONST. § 5754.
[26] INVESTOPEDIA, https://www.investopedia.com/articles/markets/081515/how-inflation-and-unemployment-arerelated.asp#:~:text=In%20a%20scenario%20wherein%20monetary,to%20raise%20prices%20even%20faster. (last visited April. 18, 2023).

- **Tax Rates and Tax Collection:** Another problem faced by the government is that mergers and acquisitions have a significant impact on tax collection, and this problem further increases when the companies involved are multi-national companies. This, in many cases, can lead to a miscalculation of the correct tax rate for the company, which can have a negative impact on the government of the company.
- **Prevention of monopoly in the Market**: M&A is a powerful tool that can be used by companies to expand the business and to acquire assets that will help the company to gain more assets. However, it can be seen in many cases that it can also create a threat to the existing competition in the market as the more prominent companies acquire the smaller growing companies that will remove any kind of competition, they are facing in the current market[27]. It is the role of the government to make sure that the more prominent companies are not creating barriers for the smaller companies to grow and make the competition open for all. To perform the task successfully, laws have to be in place regarding the same. When it comes to India and the USA, both countries have separate laws that deal with anti-competitive behavior in the market and make sure that the market is not solely run by multinational corporations.

In India, the law that governs competition is called the **Competition Act of 2002**[28], which was passed by the Indian parliament to prevent the more significant firms from creating market barriers and prohibits any form of cartelization and agreement among companies that may lead to the exploitation of the market. The government must make sure that the companies are not undertaking any form of agreement that will create a market monopoly. In the case of a merger between the two telecom giants Vodafone and the Idea that took place in the year 2018, the main concern for the government was that after the merger, the two groups would be the largest telecom network in India with a Market capitalization of 35%[29]. This prompted the government to frame new guidelines regarding the merger of telecom companies and to make sure that no company has a monopoly in the market.

In the case of the USA, the law that governs competition is called the **Sherman Act of 1890,[30]** which was implemented to protect the free market and stop anti-competitive behavior in the

[27]THE WHITE HOUSE, https://www.whitehouse.gov/cea/written-materials/2021/07/09/the-importance-of-competition-for-the-american-economy/ (last visited April. 18, 2023).
[28] *supra* note 13.
[29]VODAFONE, https://www.vodafone.com/news/corporate-and-financial/merger-vodafone-india-idea(last visited April. 18, 2023).
[30] Sherman Act, 1890 (U.S.A).

market. However, it is different in a way that it tries to get the same result while taking a different approach compared to the ***Indian competition act.***[31] Unlike the competition act[32] bans anti-competitive agreements, and abuse of dominance and combinations, ***the Sherman Act of 1890***[33] prohibits monopoly in the market and is broader in its approach compared to its Indian counterpart.

The government of the country faces many challenges when a company undergoes a Merger and Acquisition process. It has to deal with the various economic and social complications that are created in the market due to M&A and make sure that the rights of the stakeholders are not violated during such a merger.

Conclusion and Suggestions

After a company completes the process of M&A, the company must see that its ideas are combined as planned and expected. Stakeholders are considered to be the backbone of the company. The shareholders, employees, and the government are the topmost important stakeholders who majorly influence the company's success. It is the stakeholders who define the goals of a company and they expand the plans which shall help them in achieving the goals. If during the M&A, the interest of the stakeholders is not given importance then the company can be at stake due to the impact that the stakeholders will have, they might not be able to function at their full capacity. After analyzing the effect that the three main stakeholders will have when the company merges in both India and U.S., it can be concluded that their conditions can be bettered by covering the lacunas that are currently existing in their respective laws. Then the M&A can be said to have a positive and successful impact.

- Though there are laws in India where an open offer can be made to minority shareholders by the acquirers there is no law requiring prior approval of minority shareholders before the completion of a merger and acquisition. There are no clear laws on what and how much information a company has to disclose to the shareholders at the time of merger and acquisition which leaves the shareholders in the dark about the potential risks and benefits.
- There is a lack of clear guidelines regarding the formation of the valuation report which leaves room for manipulation and biases thus leading to disadvantages for minority shareholders. There should be a clear mechanism through which the shareholders can

[31] *Supra* note 13.
[32] *ibid.*
[33] *Supra* note 29.

enforce their rights or hold companies accountable for violating them. Thus, in India regulatory laws are required to make the process of M&A transactions a transparent and fair process.

- Appraisal rights should be provided to the shareholders in M&A transactions in India just like the USA, provided it should be guaranteed by a central act, unlike the US.
- In India, M&A can be led to job losses due to the redundancy of roles or the need to streamline operations. However, in the USA, there are often legal protections for employees, such as the ***Worker Adjustment and Retraining Notification (WARN) Act***[34] which obligates the company to provide notices of layoff in advance. Additionally, in the USA, M&A can be led to increased job opportunities due to the creation of new jobs in merged companies.

[34] Worker Adjustment and Retraining Notification (WARN) Act, 2019 (U.S.A).