EMERGING TRENDS IN CROSS-BORDER MERGERS AND THEIR TAX IMPLICATIONS IN INDIA: A CRITICAL APPRAISAL

AVIN TIWARI,

Indian Institute of Technology Kharagpur (Kharagpur, India)

GAURAV SHUKLA,

University of the South Pacific (Suva, Fiji)

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The Indian economy has seen steady and sustainable growth over the past decade, even though other countries have been cash-strapped and suffering from stagnation. Most of this development is due to the inflow of foreign direct investment (FDI) into India through cross-border mergers and acquisitions (M&A) and the unparalleled rise in the size and number of cross-border M&A in India with a favourable market climate for such trade. As a business strategy, cross-border M&As in India are rife with many legal complexities and issues. This paper documents the steady growth of cross-border M&A activity in India over the years and presents a comprehensive depiction of cross-border M&As, what the applicable laws are, what the legal issues and complexities involved are, and finally how they can be offset. The paper highlights the tax implications and issues involved in a cross-border M&A and how far the Income Tax Act, 1961 is attuned with the corporate laws in force to promote cross-border M&As in India. The paper concludes with a broader observation that cross-border M&As bring massive economic benefits and global stature to a growing economic superpower like India. For this reason, the business and legal environment should be made more conducive to cross-border M&A activity.

Keywords: cross-border mergers and acquisitions; M&A waves; FDI; Income Tax Act, 1961; anti-trust; corporate restructuring strategy; merger control.

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Introduction

A merger between two giants in a declining industry is like the financial version of a couple having a baby to save a marriage.[1]

Adam Davidson[2]

On the global level, India is one of the fastest-growing economies, right behind the United States and China. India's economic transformation and immense market potential have attracted significant interest in the Indian economy.[3] India is among the top global investment destinations and ranked 12th in foreign direct investment (FDI) inflows in 2018, with a 20% growth in FDI inflows, which amounted to USD42 billion in 2018, and USD51 billion in 2019.[4]

The Indian economy has shown promising evidence of increasing depth and maturity, with an estimated real annual gross domestic product (GDP) growth rate of 8.8% in 2021,[5] owing to a strong capital market and market-friendly and competitive, regulatory reforms. In 2018, India recorded her highest ever half-yearly Mergers and Amalgamations (M&As) deal figures of USD75 billion comprising 638 transactions, including ten deals in the billion-dollar category, and around 52 deals having an

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[1] Adam Davidson, *How Dead Is the Book Business?*, New York Times, 13 November 2012 (Jan. 02, 2021), available at https://www.nytimes.com/2012/11/18/magazine/penguin-random-house-merger.html.

[2] Adam Davidson is a renowned American journalist and social commentator.

[3] Afra Afsharipour, *Rising Multinationals: Law and the Evolution of Outbound Acquisitions by Indian Companies*, 44(3) UC Davis L. Rev. 1029, 1030 (2011).

[4] UNCTAD, World Investment Report 2020: International Production Beyond the Pandemic (2020), at 5, 10 (Jan. 02, 2021), available at https://unctad.org/webflyer/world-investment-report-2020.

[5] Real GDP Growth, IMF DataMapper, India, International Monetary Fund (October 2020) (Jan. 02, 2021), available at https://www.imf.org/en/Countries/IND; Sridhar Ramasubramanian, *Expert Speak on the Overall Economic Outlook*, 16(4) GTILLP 1, 25 (2018).

estimated value above USD100 million each, which together contributed 93% of the total deal value.[6] The year 2018 witnessed 235 M&A transactions amounting to USD65.5 billion, along with the highest cross-border M&A deal value since 2011 at USD25 million, a monumental increase of 5.8 times the total value in 2017.[7] The following year 2019 witnessed an aggregate deal value of USD67 billion, and despite a fall of 34.4% from 2018, the year ended as second best in terms of deal volume and value.[8]

The extraordinary events of 2020 brought on by the outbreak of COVID-19 were experienced in countries the world over, and India was no different in this respect. Yet, while wrestling with the pandemic, state-wide lockdowns, an economic slump, geopolitical tensions, and massive uncertainty, India still managed to better its 2019 performance by 7%, and the total deal value was recorded at an unprecedented USD80 billion across 1,268 transactions during the year.[9]

Mergers and acquisitions are the essential precursors to globalization.[10] They promote geographical expansion, exploration,[11] and utilization of their core competencies in an expeditious, efficient, and economical manner.[12] Over the years, the juggernaut of cross-border mergers has rolled on and gathered unprecedented momentum, gaining prominence relative to worldwide mergers.[13] Many countries[14] have specific tax rules which grant tax benefits involving mergers, and acquisitions transactions, by allowing tax deferral otherwise imposed on the owners of some of the participating parties upon completion of a deal.[15] Once mergers and acquisitions transactions go beyond the national borders, countries are reluctant to provide tax incentives to attract investment and achieve economic growth, as, in such cases,

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6 Ramasubramanian 2018, at 8.

7 Anuj Chande, *Setting New Records for Indian M&A*, Grant Thornton UK LLP, 2 August 2018 (Jan. 02, 2021), available at https://www.grantthornton.co.uk/insights/2018-setting-new-records-for-indian-ma.

8 Harsh Pais et al., *M&A Report 2020: India*, International Financial Law Review, 25 March 2020 (Jan. 02, 2021), available at https://www.iflr.com/article/b1lmx6b3qynryg/mampa-report-2020-india; UNCTAD (2020), *supra* note 4, at 5, 10.

9 Swaraj S. Dhanjal, *India clocks $80 bn of M&A activity, PE deals in '20: report*, LiveMint, 24 December 2020 (Jan. 02, 2021), available at https://www.livemint.com/companies/news/india-clocks-80-bn-of-m-a-activity-pe-deals-in-20-report-11608775915889.html.

10 Pehr-Johan Norbäck & Lars Persson, *Globalization and Profitability of Cross-Border Mergers and Acquisitions*, 35(2) Econ. Theory 241, 263 (2008).

11 James G. March, *Exploration and Exploitation in Organizational Learning*, 2(1) Organ. Sci. 71, 82 (1991).

12 Joseph A. Clougherty et al., *Cross-Border Mergers and Domestic-Firm Wages: Integrating "Spillover Effects" and "Bargaining Effects*,*"* 45(4) J. Int. Bus. Stud. 450, 459 (2014).

13 Robert L. Conn, *International Mergers: Review of Literature and Clinical Projects*, 29 JFEd 1, 19 (2003).

14 To encourage trade and investment, countries such as the UK, USA, Singapore, Cyprus, Mauritius, Russia, etc., give way to tax grant benefits through DTAA (Double Taxation Avoidance Agreements).

15 Merle Erickson, *The Effect of Taxes on the Structure of Corporate Acquisitions*, 36(2) J. Account. Res. 279, 281–82 (1998).

relief from taxation practically implies tax exemption, super deductions, tax holidays, and immunity.[16]

Cross-border mergers are more complex and imbued with surprises and other pitfalls since there are multiple jurisdictions involved in the transaction.[17] The total range of concerns has expanded as the speed and volume of international deals have increased.[18] Domestic mergers and acquisitions are, generally, socially desirable transactions, as less risk is involved in comparison to cross-border M&As.[19] Companies in many countries[20] enjoy tax deferrals to the extent to which they use stock to compensate target corporations or their shareholders.[21] Tax laws should promote cross-border mergers and acquisitions to attract foreign investors and establish a pro-investment climate.[22]

Mergers and acquisitions are intricate, have multifarious dimensions, and are attracted and governed by various laws and regulations simultaneously depending on the stakeholders and tax regimes involved.[23] Further, given the cut-throat competition in the world market and pressure on top-line and bottom-line growth,[24] Indian companies look at mergers and acquisitions as vehicles for change, significant growth, and a critical business strategy tool.[25]

Income generated overseas is repatriated to an Indian company in interest, royalties, service or management or technical fees, dividends, and capital gains.[26] When such income is repatriated to the Indian company by Indian Holding Companies[27] or to

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16 Ralph Sonenshine & Kara Reynolds, *Determinants of Cross-Border Merger Premia*, 150(1) Rev. World Econ. 173, 187–88 (2014).

17 Sydney Finkelstein, *Cross-Border Mergers and Acquisitions*, FTMGB (1999) (Jan. 02, 2021), available at http://mba.tuck.dartmouth.edu/pages/faculty/syd.finkelstein/articles/cross_border.pdf.

18 Frank Stähler, *Partial Ownership and Cross-Border Mergers*, 11(3) J. Econ. 209, 212 (2014).

19 Petri Böckerman & Eero Lehto, *Geography of Domestic Mergers and Acquisitions (M&As): Evidence from Matched Firm-Level Data*, 40(8) Reg. Stud. 847, 852 (2006).

20 Barendra K. Bhoi, *Mergers and Acquisitions: An Indian Experience*, 21(1) RBI Occasional Papers 133, 160–61 (2000).

21 Alan J. Auerbach & David Reishus, *The Impact of Taxation on Mergers and Acquisitions* in *Mergers and Acquisitions* 69, 73–74 (Alan J. Auerbach ed., 1988).

22 Carla Hayn, *Tax Attributes as Determinants of Shareholder Gains in Corporate Acquisitions*, 23(1) J. Financ. Econ. 121, 130 (1989).

23 Emanuel Gomes et al., *Critical Success Factors Through the Mergers and Acquisitions Process: Revealing Pre- and Post-M&A Connections for Improved Performance*, 55(1) Thunderbird Int. Bus. Rev. 13, 17 (2013).

24 John A. Pearce & Fred David, *Corporate Mission Statements: The Bottom Line*, 1(2) Academy of Management Executive 109, 113 (1987).

25 Manish Agarwal & Aditya Bhattacharjea, *Mergers in India: A Response to Regulatory Shocks*, 42(3) Emerg. Mark. Finance Trade 46, 62–63 (2006).

26 Edward D. Kleinbard, *Stateless Income*, 11 Fla. Tax Rev. 699, 774 (2011).

27 "Holding Company to one or more other companies means a company of which such companies are subsidiary companies ..." Sec. 2(46) of the Companies Act, 2013, No. 18, Acts of Parliament, 2013 (India).

Indian Holding Companies by the target company it would attract double taxation.[28] The liability is then off-settled by tax treaties,[29] which decide the taxing rights between the two countries. An ideal situation for an Indian Holding Company would be one with a low/nil withholding tax on receipts, on income streams, and subsequent re-distribution as passive income.[30] Some jurisdictions[31] have relatively favourable tax treaties with India, e.g. the Indo-Mauritius, Indo-Singapore, Indo-Cyprus Double Taxation Avoidance Agreements (DTAAs), where repatriation of income back to India may be observed.[32]

Given the essential role that mergers and acquisitions play in the globalization process, the Indian corporate environment has radically altered and aligned itself with the economic policy changes and the introduction of new institutional mechanisms.[33] The modern industrial policy changes of 1991 ushered in the era of free trade in the economy.[34] The past two decades reflect India's substantial rise in mergers and acquisitions activity in almost all sectors of the economy.[35] Indian industries underwent structural changes in the post-liberalization period when mergers and acquisitions were considered vital cogs of the corporate restructuring process, and of redirecting capital flows towards efficient management. In a way, corporate restructuring became imperative to the new economic paradigm.[36]

1. Mergers and Cross-Border Mergers Differentiated

Whereas a "merger" is the "amalgam of two or more corporate entities into one, leading to accumulation of assets & liabilities of the distinct entities, and the organization

28 "Double taxation is a situation where two or more taxes are paid for the same transaction/income which arises due to the overlap between tax laws and jurisdictions of two countries." George O. May, *Double Taxation*, 5(1) Foreign Aff. 69, 79 (1926).

29 These are country-specific Double Taxation Avoidance Agreements (DTAA). Benjamin F. Siggelkow, *Tax Competition and Double Tax Treaties with Mergers and Acquisitions*, MPRA Paper No. 49371 (2013), at 3–4 (Jan. 02, 2021), available at https://mpra.ub.uni-muenchen.de/49371/1/MPRA_paper_49371.pdf.

30 Monica Singhania & Venugopal Dastaru, *Taxation of Cross Borders Mergers & Acquisitions: Vodafone Hutch Deal*, IITCOE (2015) (Jan. 02, 2021), available at https://iitcoe.in/ITS/topics/Regulation/TaxationofCrossBordersMergersAcquisitionsVodafoneHutchDeal.pdf.

31 E.g. Mauritius, Cyprus, Singapore, and the Netherlands.

32 DIPP, Quarterly Fact Sheet on FDI (March 2020) (Jan. 02, 2021), available at https://dipp.gov.in/sites/default/files/FDI_Factsheet_March20_28May_2020.pdf.

33 Viral U. Pandya, *Mergers and Acquisitions Trends – The Indian Experience*, 9(1) Int. J. Bus. Adm. 44, 46 (2018).

34 For Industrial Policy Changes of 1991 in India and its effects, *see* Montek S. Ahluwalia, *Economic Reforms in India Since 1991: Has Gradualism Worked?*, 16(3) J. Econ. Perspect. 67, 82–83 (2002).

35 Avin Tiwari et al., *Cross Border M&A's in ASEAN and India: A Comparative Critique*, 11(2) J. Adv. Res. Law Econ. 619, 626 (2020); P.L. Beena, *Trends and Perspectives on Corporate Mergers in Contemporary India*, 43(39) Econ. Polit. Wkly 48, 54–55 (2008).

36 Pandya 2018, at 48.

of such entity into one business";[37] a "cross-border merger"[38] means "any merger, arrangement or amalgamation between an Indian company and foreign company by Companies (Compromises, Arrangements, and Amalgamation) Rules, 2016[39] notified under the Companies Act, 2013."[40] Reversing the earlier prohibition, which was imposed by the 1956 Companies Act on mergers of Indian companies with foreign companies, the 2013 Act permits the merger of an Indian company with a foreign company (incorporated in foreign jurisdictions notified by the Central Government), provided prior approval of the Reserve Bank of India is obtained.[41] Under the new cross-border mergers regime, inbound[42] and outbound mergers[43] are permitted. While an inbound merger refers to a cross-border merger where the resultant company is an Indian company, an outbound merger refers to cross-border mergers where the resultant company is a foreign company.[44]

Thus, a "cross-border merger" is an activity wherein a large foreign corporation purchases a controlling interest in a small local corporation. The company so acquired ceases to exist and is integrated into the acquiring corporation as a subsidiary.[45] It is "an activity where an enterprise from one country purchases the entire asset or controlling interest of an enterprise in another country."[46]

Related to the wider reach of this concept, in 2001 Faulkner argued that there has been a growing interest in cross-border mergers and acquisitions since the 1990s, thus raising additional challenges to ethnic, linguistic, and institutional diversity.[47] He further argued that post-merger integration could be problematic in cross-border mergers from the perspective of value addition mainly because they have to integrate their operations in different countries.[48] Thus, internationalization

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37 To be understood as a means of corporate restructuring under Secs. 230–240 of the Companies Act, 2013.

38 Sec. 2(iii) of the Foreign Exchange Management (Cross-Border Merger) Regulations, 2018.

39 MCA, The Companies (Compromises, Arrangements, and Amalgamation) Rules (2016) (Jan. 02, 2021), available at http://www.mca.gov.in/Ministry/pdf/compromisesrules2016_15122016.pdf.

40 Official Gazette of India, Notification No. G.S.R. 1134(E), effective from 15/12/2016.

41 RBI, Foreign Exchange Management (Cross-Border Merger) Regulations, 2018, Notification No. FEMA. 389/2018-RB (2018) (Jan. 02, 2021), available at https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=11235&Mode=0.

42 *Id.* Sec. 2(v).

43 *Id.* Sec. 2(viii).

44 *Id.* Sec. 2(iv).

45 Carla L. Koen, *Comparative International Management* 111–17 (2005).

46 Zhanwen Zhu & Haifeng Huang, *The Cultural Integration in the Process of Cross-Border Mergers and Acquisitions*, 3(2) Int. Manag. Rev. 40, 41 (2007).

47 Noelia-Sarah Reynolds & Satu Teerikangas, *The International Experience in Domestic Mergers – Are Purely Domestic M&A a Myth?*, 25(1) Int. Bus. Rev. 1, 2 (2016).

48 John Child et al., *The Management of International Acquisitions* 251–52 (2003).

theory predicts a positive return from cross-border acquisitions because of gains from geographic diversification and synergies.[49]

1.1. Strategic Motivations and Determinants of Cross-Border Mergers and Acquisitions

Cross-border M&As provide an additional set of factors that affect the likelihood that two firms decide to merge.[50] The main reasons and motives for domestic mergers as well as cross-border mergers can be found in (i) Neoclassical profit-maximization theory,[51] which includes efficiency, strategy, and shareholder value as its core value; (ii) Principal-agent theory,[52] which is based upon managerial efficiency and considerations; (iii) Internationalization theory in the OLI eclectic paradigm,[53] which is based upon ownership, location advantages, and internalization of a firm; and (iv) Comparative ownership advantage theory,[54] which is based upon five characteristics[55] of accelerated internalization. These theories explain the basis and reasons for corporate mergers.[56] In simple terms, mergers are corporate strategies aimed at market access,[57] diversification,[58] expansion,[59] risk-reduction,[60] and creation of a sustainable competitive advantage[61] for

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49 Leonard Waverman, *Corporate Globalization Through Mergers & Acquisitions* 197–98 (1991).

50 Isil Erel et al., *Determinants of Cross-Border Mergers and Acquisitions*, 67(3) J. Finance 1045 (2012).

51 J. Peter Neary, *Cross-Border Mergers as Instruments of Comparative Advantage*, 74(4) Rev. Econ. Stud. 1229, 1250 (2007).

52 Bernd Wübben, *German Mergers & Acquisitions in the USA* 290–99 (2007).

53 John H. Dunning, *The Eclectic Paradigm of International Production: A Restatement and Some Possible Extensions*, 19(1) J. Int. Bus. Stud. 1, 30 (1988).

54 Sunny Li Sun et al., *A Comparative Ownership Advantage Framework for Cross-Border M&As: The Rise of Indian and Chinese MNEs*, 47(1) J. World Bus. 4, 15 (2012).

55 Industrial factor endowments; dynamic learning; value creation; reconfiguration of the value chain; and institutional facilitation and constraints.

56 Michael Firth, *Takeovers, Shareholder Returns, and the Theory of the Firm*, 94(2) Q.J. Econ. 235, 237–38 (1980).

57 Peter J. Buckley et al., *Host–Home Country Linkages and Host–Home Country Specific Advantages as Determinants of Foreign Acquisitions by Indian Firms*, 21(5) Int. Bus. Rev. 878, 888–89 (2012).

58 Randall Morck & Bernard Yeung, *Why Firms Diversify: Internalization Versus Agency Behavior*, ResearchGate (March 1998) (Jan. 02, 2021), available at https://www.researchgate.net/publication/228253193_Why_Firms_Diversify_Internalization_Versus_Agency_Behaviour; *Intangible Assets: Values, Measures, and Risks* 390, 397 (John R.M. Hand & Baruch Lev eds., 2003).

59 Katsuhiko Shimizu et al., *Theoretical Foundations of Cross-Border Mergers and Acquisitions: A Review of Current Research and Recommendations for the Future*, 10(3) J. Int. Manag. 307, 347–48 (2004).

60 Yakov Amihud & Baruch Lev, *Risk Reduction as a Managerial Motive for Conglomerate Mergers*, 12(2) Bell J. Econ. 605, 607 (1981).

61 Kotapati S. Reddy, *Extant Reviews on Entry-Mode/Internationalization, Mergers & Acquisitions, and Diversification: Understanding Theories and Establishing Interdisciplinary Research*, 16(4) Pac. Sci. Rev. 250, 270 (2014).

the company.[62] There are four key independent yet inter-dependent motives for M&As, namely strategic, market, economic, and personal.[63] Thus, both domestic M&As and cross-border M&As are important strategic decisions[64] for maximizing a company's growth.[65]

Additionally, synergistic operational advantages are among the most significant purposes that mergers and acquisitions intend to achieve.[66] The combined effect of two corporate entities compared to separate effects is always more beneficial since it reduces expenses relating to production, administration, and sales.[67] It utilizes the optimum capacities and factors of production.[68] Other benefits of integration are reduced competition, cost savings by reducing overhead, capturing a larger market share, and pooling technical or financial resources.[69] A company mired with financial constraints can also opt for a merger.[70] Per-unit cost will fall when output increases is noted as a reason for mergers and acquisitions. As a result of the scale effect,[71] products can be offered at a more competitive price in the market.[72]

Strengthening their financial position and revival of sick companies,[73] the advantage of brand-equity,[74] diversification, competitive advantage, and sustaining growth are some of the other reasons for which companies go for mergers.[75]

In addition to these factors, the geography, quality of accounting disclosure, and bilateral trade increase the likelihood of cross-border mergers between two

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62 J. Myles Shaver, *A Paradox of Synergy: Contagion and Capacity Effects in Mergers and Acquisitions*, 31(4) Acad. Manag. Rev. 962, 963–65 (2006).

63 H.D. Hopkins et al., *Cross-Border Mergers and Acquisitions: Global and Regional Perspectives*, 5(3) J. Int. Manag. 207, 232–33 (1999).

64 Elazar Berkovitch & M.P. Narayanan, *Motives for Takeovers: An Empirical Investigation*, 28(3) J. Financ. Quant. Anal. 347, 350 (1993).

65 Neary 2007, at 1231.

66 Jyrki Ali-Yrkkö, *Mergers and Acquisitions: Reason and Results*, ETLA Discussion Papers, No. 792, Research Institute of the Finnish Economy (ETLA) (2002) (Jan. 02, 2021), available at https://www.econstor.eu/bitstream/10419/63797/1/344861414.pdf.

67 Wübben 2007, at 299.

68 Amihud & Lev 1981, at 607.

69 Erel et al. 2012, at 1050.

70 Friedrich Trautwein, *Merger Motives and Merger Prescriptions*, 11(4) Strateg. Manag. J. 283, 294 (1990).

71 Barney Warf, *Mergers and Acquisitions in the Telecommunications Industry*, 34(3) Growth Change 321, 340 (2003).

72 George J. Benston, *Economies of Scale of Financial Institutions*, 4(2) J. Money Credit Bank. 312, 339 (1972).

73 Sec. 3(1) O of the Sick Industrial Companies (Special Provisions) Act, 1985, (SICA) Act No. 1, Acts of Parliament, 1986 (India).

74 R.K. Srivastava, *The Role of Brand Equity on Mergers and Acquisition in the Pharmaceutical Industry: When Do Firms Learn from Their Merger and Acquisition Experience?*, 5(3) J. Strateg. Manag. 266, 282 (2012).

75 Alexander Roberts et al., *Mergers & Acquisitions* 4–5 (2003).

countries.[76] Cross-border mergers can create market power since it is legal for post-merger combined firms to charge profit-maximizing prices themselves, but not for pre-merger separate firms to collude to do so collectively.[77] Similarly, mergers can also have tax advantages if they allow one firm to utilize tax shields that another firm possesses.[78] Such benefits accrue in the form of tax credits, carry forward and set-off of losses,[79] foreign exchange arbitrage gains,[80] etc. Tax efficiency in M&As is another tangible form of financial synergy.[81] However, these synergies are unrelated to the "cost of capital" improvements and other tax benefits.[82] One of the main benefits is that profits or tax losses may be transferred within the combined company to benefit from the differential tax regimes.[83] Moreover, the merged company's net operating losses may be used to shelter the income of the more profitable company before the merger.[84] Thus, often profit-making firms acquire firms making losses for this purpose.[85] After the economic liberalization, it has been noticed that the largest share of foreign direct investment (FDI) takes the shape of cross-border mergers and acquisitions because low-cost firms find it profitable to merge with high-cost firms, since the monetary union would enhance goods competition across countries through a reduction in the trade cost, elimination of exchange rate risk, and improved price transparency.[86]

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76 Erel et al. 2012, at 1045.

77 *Id.*

78 Merle M. Erickson & Shiing-wu Wang, *Tax Benefits as a Source of Merger Premiums in Acquisitions of Private Corporations*, 82(2) Account. Rev. 359, 382 (2007).

79 Sec. 72A of the Income Tax Act, Act No. 43, Acts of Parliament, 1961 (India).

80 Robert G. Hansen, *A Theory for the Choice of Exchange Medium in Mergers and Acquisitions*, 60(1) J. Bus. 75, 90 (1987).

81 Hayn 1989, at 152.

82 Sergey Lebedev et al., *Mergers and Acquisitions in and out of Emerging Economies*, 50 J. World Bus. 651, 659–60 (2015).

83 Duncan Angwin, *In Search of Growth*: *Choosing Between Organic, M&A, and Strategic Alliance Strategies* in *The M&A Collection Themes in Best Practice: Themes in Best Practice* 19, 21–22 (Scott Moeller ed., 2014). However, such trade practices may not be possible in the post-BEPS world, where there is tight scrutiny and regulation of such transactions; still, the existence of transfer pricing in some form or other cannot be denied.

84 PWC, Mergers and Acquisitions: The Evolving Indian Landscape (2017) (Jan. 02, 2021), available at https://www.pwc.in/assets/pdfs/trs/mergers-and-acquisitions-tax/mergers-and-acquisitions-the-evolving-indian-landscape.pdf.

85 *Id.* at 11–12.

86 Nicolas Coeurdacier et al., *Cross-Border Mergers and Acquisitions and European Integration*, 24(57) Econ. Policy 55, 56–58 (2009).

2. Mergers and Acquisitions in India: The Legal Landscape

The word "merger" is not defined under either the Companies Act, 2013 or the Income Tax Act, 1961. However, in academic parlance, the words merger/acquisitions and amalgamations are used very loosely and synonymously. Under the Income Tax Act, 1961, the words "amalgamation" and "demerger" find explicit mention. Under the Income Tax Act, 1961, "amalgamation" means the merger of one or more companies with another company to form one company in such a manner that the conditions mentioned in the Act are satisfied.[87] Similarly, a "demerger" is defined as the transfer of one or more undertakings to any resulting company under a scheme of corporate arrangement described in Sections 230 to 240 of the Companies Act, 2013 in such a manner that it conforms to the conditions mentioned therein.[88] Despite being a voluminous piece of legislation, the Companies Act, 2013[89] fails to accommodate terms such as "merger" or "amalgamation." However, Sections 230 to 240 of the Companies Act, 2013 provide for the different means of corporate restructuring which involves both mergers and acquisitions.[90] Thus, the Companies Act, 2013 did not strictly define the term "merger" or "amalgamation," but brought the concept under the broader ambit of corporate restructuring.[91]

Similarly, under the mandatory accounting standard 14 (AS-14),[92] "amalgamation" means an amalgamation under the Companies Act, 1956, or any other statute applicable to corporations. The standard provides for "two methods of amalgamation," one of them being a merger and the other being an acquisition.[93]

2.1. Cross-Border Mergers and Acquisitions in India: The Legal Framework

In India, a plethora of laws affect and regulate cross-border mergers and acquisitions. Chief among them are (i) the Companies Act, 2013;[94] (ii) SEBI (Security and Exchange Board of India) Substantial Acquisition of Shares & Takeovers

87 Sec. 2(1B) of the Income Tax Act, 1961.

88 *Id.* Sec. 2(19AA).

89 Sec. 2 of the of the Companies Act, 2013.

90 Ch. XV, Compromises, Arrangements & Amalgamations, Secs. 230–240 of the Companies Act, 2013.

91 "A merger, therefore, is a combination or fusion of two or more entities into one, the desired effect of which is the accumulation of assets and liabilities of the distinct entities, and organization of such entity into one business": to be understood as a means of corporate restructuring under Secs. 230–240 of the Companies Act, 2013.

92 Accounting Standard (AS 14) of the Institute of Chartered Accountants of India, New Delhi (2016) (Jan. 02, 2021), available at https://resource.cdn.icai.org/46922asb36718-as14.pdf.

93 *Id*.

94 Companies Act, 2013.

Regulations 2011[95] and the Amendment Act, 2017;[96] (iii) Competition Act, 2002;[97] (iv) Insolvency and Bankruptcy Code, 2016;[98] (v) Income Tax Act, 1961;[99] (vi) Transfer of Property Act, 1882;[100] (vii) Indian Stamp Act, 1899;[101] (viii) Foreign Exchange Management Act, 1999 (FEMA);[102] and other allied laws as may be applicable based on the merger structure.[103]

The provisions relating to "mergers" and "acquisitions" are covered under Sections 234 to 240 of the Companies Act, 2013.[104] Section 234[105] contains provisions for the cross-border mergers of Indian and foreign companies. Further, Companies (Compromises, Arrangements, and Amalgamation) Rules, 2016,[106] as amended by the Companies (Compromises, Arrangements, and Amalgamation) Amendment Rules, 2017 (Co. Rules),[107] were issued. It is worth taking note that after the incorporation of the 2017 Rules a foreign company is allowed to merge with a company registered under the Companies Act, 2013, or vice-versa, only with the prior approval of the Reserve Bank of India (RBI). The RBI issued draft regulations relating to cross-border mergers for comments from the public[108] and then issued the Foreign Exchange Management (Cross-Border Merger) Regulations, 2018,[109] which was to be effective from the date of notification in the official gazette.[110]

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95 SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, as amended up to 14 August 2017 (Jan. 02, 2021), available at https://www.sebi.gov.in/legal/regulations/sep-2011/sebi-substantial-acquisition-of-shares-and-takeovers-regulations-2011-as-amended-upto-august-14-2017-_35784.html.

96 *Id.*

97 Competition Act, 2002, No. 12, Acts of Parliament, 2003 (India).

98 Insolvency and Bankruptcy Code, No. 31, Acts of Parliament, 2016 (India).

99 Income Tax Act, No. 43, Acts of Parliament, 1961 (India).

100 Transfer of Property Act, No. 4, Acts of Parliament, 1882 (India).

101 Indian Stamp Act, No. 2, Acts of Parliament, 1899 (India).

102 Foreign Exchange Management Act, No. 42, Acts of Parliament, 1999 (India).

103 Tiwari et al. 2020, at 627.

104 Secs. 234–240 of the Companies Act, 2013.

105 *Id.* Sec. 234.

106 MCA, The Gazette of India, Notification No. G.S.R. 1134 (E) (2016) (Jan. 02, 2021), available at http://www.mca.gov.in/Ministry/pdf/compromisesrules2016_15122016.pdf.

107 MCA, The Gazette of India, Notification No. G.S.R. 368 (E) (2017) (Jan. 02, 2021), available at http://www.mca.gov.in/Ministry/pdf/CompaniesCompromises_14042017.pdf.

108 Ajit Prasad, *Press Release No. 2016-2017/2909* (2017) (Jan. 02, 2021), available at https://taxguru.in/rbi/draft-foreign-exchange-management-cross-border-merger-regulations-2017.html.

109 Foreign Exchange Management (Cross-Border Merger) Regulations, 2018, s*upra* note 41.

110 Foreign Exchange Management (Cross-Border Merger) Regulations, 2018 were notified *vide* Notification No. FEMA 389/2018-RB, and published in the official gazette on 20 March 2018.

SEBI regulates M&A transactions concerning the entities listed on the recognized stock exchanges[111] of India, and, in addition to the Companies Act, 2013, the listed public companies must comply with the applicable SEBI rules and listing regulations. The SEBI Regulations 2011 regulate both the direct and the indirect acquisition of shares, voting rights, and control in the listed companies that are traded on the stock market.[112] Under the SEBI Takeover Code,[113] if the acquisition of shares of a listed company[114] exceeds 25 per cent by an acquirer,[115] that would trigger the open offer threshold for the public shareholders.[116] Prior approval of the appropriate stock exchanges and SEBI[117] is required for all cases of mergers or demergers involving a listed company before approaching the National Company Law Tribunal.[118]

Concerning the competition regulations, the prior approval of the Competition Commission of India (CCI)[119] is required for all acquisitions[120] exceeding the permissible financial thresholds and which are not within a common group.[121] CCI evaluates an acquisition as to whether the said acquisition would lead to a dominant market position, or not, mainly to avoid unfair and anti-competitive practices[122] in the concerned sector.

Under stamp duty regulations, there is a provision for stamp duty on any issue or transfer of shares at a nominal rate of 0.25 per cent.[123] However, no stamp duty

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111 List of Stock Exchanges, SEBI (2020) (Jan. 02, 2021), available at https://www.sebi.gov.in/stock-exchanges.html; SEBI gives recognition and regulates the functioning of stock exchanges in India.

112 K.S. Reddy, *Institutional Laws, and Mergers and Acquisitions in India: A Review/Recommendation*, MPRA Paper 63410, University Library of Munich, Germany (2015), at 1, 5–6 (Jan. 02, 2021), available at https://mpra.ub.uni-muenchen.de/63410/1/MPRA_paper_63410.pdf.

113 SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (last amended on 6 March 2017) (Jan. 02, 2021), available at https://www.sebi.gov.in/legal/regulations/apr-2017/sebi-substantial-acquisition-of-shares-and-takeovers-regulations-2011-last-amended-on-march-6-2017-_34693.html.

114 *Id.* Sec. 2(1)(b).

115 *Id.* Sec. 2(1)(a).

116 *Id.* Sec. 3(1).

117 *Id.* Sec. 28.

118 Karan Talwar & Nivedita Saxena, *Anti-Acquirer and Pro-Shareholder? An Analysis of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011*, 5(1) NUJS L. Rev. 129, 140–41 (2012).

119 Competition Commission of India is the statutory and regulatory body responsible for enforcing the Competition Act, 2002, ensuring fair trade practices across the Indian Territory, and preventing activities that negatively affect India's competition.

120 Sec. 2(a) of the Competition Act, 2002.

121 *Id.* Sec. 6.

122 *Id.* Secs. 2–5.

123 Sec. 3(a) read with Art. 62, Schedule I of the Indian Stamp Act, 1899.

will be leviable in case of any transfer or issue in a dematerialized form.[124] Further, the conveyance[125] of business under a valid business transfer agreement in case of a slump sale is subject to stamp duty at the same rate levied on the conveyance of assets.[126] A scheme of merger or demerger attracts stamp duty at a concessional rate in comparison to the conveyance of assets. However, the exact rates leviable depend upon the specific heads or entries under respective state laws for stamp duty.[127] All transfers, issues, sale, or purchase of equity shares involving residents and non-residents are allowed under RBI pricing guidelines and permissible sectoral caps. However, mergers or demergers involving any issuance of shares to non-resident shareholders of the transferor company are not subject to prior RBI/government approval.[128] Issuances of any other instrument than equity shares/compulsorily convertible preference shares/compulsorily convertible debentures to the non-resident in the form of debt are subject to prior RBI approval.[129]

3. Tax Implications in Cross-Border Mergers and Acquisitions in India

Tax is a significant business cost to be considered while taking any business decision, particularly when competing with other global players.[130] The new Direct Tax Code,[131] which will replace[132] the current Income Tax Act, 1961, seeks to stress transparency and taxpayer friendliness.[133] Under the Income Tax Act, 1961, capital gains tax would be

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124 Sec. 8(a) of the Competition Act, 2002.

125 *Id.* Sec. 3(10).

126 Gaurav Shukla & Swapneshwar Goutam, *Concept of Slump Sale & Taxation Issues in India*, 3(1) Madras L.J. 75, 76 (2009).

127 Schedule I of the Indian Stamp Act, 1899.

128 Saurav Agarwala & Navaneet Desai, *Tax, Antitrust and Cross Border Mergers: An Interdisciplinary Perspective*, 12 NUALS L.J. 5, 8 (2018).

129 RBI, Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2017, Notification No. FEMA 20(R)/2017-RB (2017) (Jan. 02, 2021), available at https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11253&Mode=0.

130 NDA, Tax Issues in M&A Transactions (August 2020), at 21 (Jan. 02, 2021), available at https://www.nishithdesai.com/fileadmin/user_upload/pdfs/Research%20Papers/Tax_Issues_in_M_A.pdf.

131 The Direct Tax Code 2013, which was expected to become operational from 1 April 2015, is still pending in parliament (Jan. 02, 2021), available at https://taxguru.in/wp-content/uploads/2014/04/DTC-2013-taxguru.in_.pdf.

132 The Finance Minister of India released DTC, 2013 for public discussion and suggestions on 1 April 2014.

133 The Direct Tax Code (DTC), 2013 is an attempt by the Government of India (GOI) to simplify India's direct tax laws. DTC will revise, consolidate, and simplify the structure of India's direct tax laws into a single legislation. The DTC, when implemented, will replace the Income Tax Act, 1961 (ITA), and other direct tax legislation, such as the Wealth Tax Act, 1957. However, it is still pending in parliament because the Government wants to leave no stone unturned in the simplification of the tax regime and it is considering the reccomendations of the CBDT Task Force Committee Report, 2019 on DTC.

levied on such transactions as when capital assets are transferred.[134] From the definition of "transfer," it is clear that if the merger, amalgamation, demerger, or any form of corporate restructuring results in the transfer of a capital asset, it will lead to a taxable event. As far as mergers and acquisitions are concerned, the provisions of the Income Tax Act, 1961 concerning "amalgamation,"[135] "demerger,"[136] "securities transaction tax" (STT),[137] "capital gains,"[138] "slump sale,"[139] "set off and carry forward of losses,"[140] etc., need to be examined intricately to establish legitimate safeguards. In the Income Tax Act, 1961, the transfer of any capital asset is generally subject to capital gains tax in India.[141] However, where a foreign company is holding shares of Indian companies, then, with amalgamation or demerger of that foreign company with another foreign company, the transfer of shares would be exempted from capital gains tax provided it follows certain conditions[142] under the Income Tax Act, 1961.[143]

Nevertheless, there might be situations wherein the parties enter into a non-compete agreement, and a non-compete right is transferred.[144] Where a foreign company transfers its shares to another company and the value of the shares is derived mainly from the assets based in India, then capital gains so derived on the transfer are subject to income tax in India.[145] Furthermore, under the Indian tax law, specific depreciation[146] rates for tangible assets and intangible assets, such as know-how, patents, copyrights, trademarks, licenses, franchises, or any similar business or commercial rights, are allowed. Therefore, when there is an excess of consideration over the value of the assets, depreciation allowance may be available.[147] However, the situation is ambiguous for expenditure incurred on the acquisition of a non-

134 Secs. 47–54 of the Income Tax Act, 1961.

135 *Id.* Sec. 2(1B).

136 *Id.* Sec. 2(19AA).

137 *Id.* Secs. 96–105.

138 *Id.* Secs. 47–54.

139 *Id.* Sec. 50(B); Shukla & Goutam 2009, at 76.

140 Secs. 71–79 of the Income Tax Act, 1961.

141 *Id.* Sec. 47(vi).

142 *Id.* Sec. 47(iv)–(vii).

143 *Id.* Sec. 47.

144 Shivam Bhardwaj & Samyak Sibasish, *Treatment of a Non-Compete Clause in M&A: Finally Clarifying the Indian Position?*, 7(3-4) NUJS L. Rev. 263, 264 (2014).

145 KPMG, Taxation of Cross-Border Mergers & Acquisitions – India (2014) (Jan. 02, 2021), available at https://home.kpmg.com/content/dam/kpmg/pdf/2014/05/india-2014.pdf.

146 Secs. 32, 72, 72A, 72AA of the Income Tax Act, 1961.

147 KPMG (2014), s*upra* note 145.

compete right. Whether non-compete rights can be treated as capital assets eligible for depreciation or as capital assets not eligible for depreciation remains a grey area.[148]

Though certain mergers enjoy tax-neutrality under Indian tax law, the provisions for mergers and acquisitions are extremely complicated, and the tax system is certainly not neutral.[149] In an inbound merger, a foreign company merges with an Indian company and the amalgamated entity is an Indian company.[150] Amalgamation enjoys tax-neutrality, and both the amalgamating company and the shareholders of the amalgamating company are tax-exempt.[151] The amalgamated company should be an Indian company,[152] and the amalgamation should be under Section 2(1B).[153]

> In an amalgamation, all the properties, assets, and liabilities of the merging companies immediately before the amalgamation should become the properties, assets, and liabilities of the amalgamated company, and further, 75% shareholders of the amalgamating companies shall remain the shareholders of the amalgamated company.[154]

Further, to achieve the aim of tax-neutrality for the amalgamating company shareholders, the entire consideration should be in the form of shares in the amalgamated company.

Similarly, an outbound merger[155] is one

> where an Indian company decides to merge with a foreign company, and where the amalgamated entity is a foreign company.[156] The transfer of capital assets through amalgamation by the amalgamating company to the amalgamated company will lead to the imposition of capital gains tax under the IT Act, and if the amalgamated company is an Indian Company, it will be exempted from tax implications.[157]

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148 NDA, Tax Issues in M&A Transactions (August 2016), at 38 (Jan. 02, 2021), available at https://pdf4pro.com/view/tax-issues-in-m-amp-a-transactions-nishith-desai-2548ec.html.

149 Kusum, *Tax implications on merger and acquisition process*, 3(5) Int. J. Bus. Manag. Soc. Sci. Res. 62, 63 (2014).

150 Sec. 2(v) of the Foreign Exchange Management (Cross-Border Merger) Regulations, 2018.

151 NDA (2016), *supra* note 148.

152 Sec. 2(20) of the Companies Act, 2013.

153 Sec. 2(1B) of the Income Tax Act, 1961.

154 *Id*.

155 Sec. 2(v) of the Foreign Exchange Management (Cross-Border Merger) Regulations, 2018.

156 *Id*. Sec. 2(iv).

157 NDA (2016), *supra* note 148.

However, this exemption is not available in the case where the resultant company is a foreign one, thus leading to a tax burden in the hands of the profit-making acquirer foreign company.[158]

Therefore, the notification of "cross-border mergers under the 2013 Act,"[159] and the introduction of Cross-Border Regulations, 2018,[160] necessitate adequate corresponding changes in the Income Tax Act[161] to establish a favourable legal environment for the promotion of cross-border mergers and acquisitions in India.

Table 1: Key tax provisions in India and their congruity concerning cross-border M&As

Tax Provisions under Income Tax Act, 1961	**Merits/Demerits & Impact on Cross-Border M&As**	**How it can be made more lucrative**
Tax Neutral Merger, s. 2(1B)	Foreign investors and companies will hugely benefit from tax neutrality, and they will derive a better return on investment due to the tax exemptions provided	Similar tax neutrality for Indian investors making foreign investments will go a long way in promoting more cross-border M&As
Tax Neutral Demerger, s. 2(19AA)	Provides for tax neutrality for all the assets and liabilities acquired by way of the demerger	Easing off the shareholding requirements of 75% and conditions under s. 72A(5) will boost more demergers to and from India
Slump Sale, s. 2(42C)	The tax incentives, exemptions, and benefits of an existing business can be transferred to the new owner efficiently	Provisions should be harmoniously read with s.50 B to maximize the tax benefits from a slump sale
Transfer, s. 47	No tax exemptions in the case of outbound mergers may deter the proliferation of cross-border M&A growth in India	Both inbound & outbound mergers should be treated at par with respect to tax levy, and similar exemptions should be provided for both
Carry Forward & Set-off of accumulated losses & depreciation, s. 72A	It provides for the carry forward and set off of accumulated losses and depreciation in case of qualifying merger/demerger, thus giving more flexibility to investors in making an informed decision regarding M&As	Provisions relaxing the 49% shareholding criteria, and allowance of unabsorbed depreciation, will positively maximize the tax benefits, thus promoting more cross-border M&A activity

[158] Kusum 2014, at 73.

[159] Secs. 234–240 of the Companies Act, 2013, notified with effect from 13 April 2017.

[160] Foreign Exchange Management (Cross-Border Merger) Regulations, 2018.

[161] Income Tax Act, 1961.

Capital Gains Tax for unqualified M&As, s. 50C, 50CA, and 56(2)(x)	For all unqualified M&As, capital gains tax will be chargeable, which may deter foreign investors from investing in India, as the norms are still stringent in comparison to other economies	More sectors should be opened up and liberalized so that more transactions can benefit from tax exemptions, which will be an added incentive for investing and hence result in more cross-border M&As in India
Withholding Tax Obligations, s. 195	Payment by a resident to any non-resident, or any passive income in the form of interest, royalties, dividends, etc., is chargeable as withholding tax, which could act as a deterrent to cross-border M&A activity	This tax cost can be substantially minimized if read with DTAAs provisions and applying the treaty benefits to the transaction, thus promoting more cross-border M&As

Conclusion

The increasing trends in cross-border M&As have been motivated by various strategic considerations which normally differ from purely domestic M&As. Compared to domestic M&As, companies engaging in cross-border M&As are facing unique risks, such as "liability of foreignness" and "double-layered acculturation." Due to their international nature, they face unique challenges, as different countries have different institutional, economic, regulatory, and cultural structures.[162]

Section 234 of the Companies Act, 2013[163] permits the integration of Indian markets within world trade wherein Indian companies are now able to participate in "outbound mergers" and acquisitions (M&As), with companies of specified jurisdictions,[164] which was previously prohibited by the Companies Act, 1956. This puts the spotlight on cross-border M&As.

Under the Income Tax Act, 1961 rules, a merger or amalgamation where the resulting entity is an Indian corporation is exempted from capital gains tax. However, where an Indian company merges with a foreign company, a similar exemption is not available, likely because such a deal was not previously allowed. Another potential tax issue for outbound mergers is that operations of the resulting foreign company in India, through a branch or otherwise, could amount to the company having a "permanent establishment" under Indian tax laws and thus attracting 26 per cent corporate tax[165] on account of operations in India.

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162 Robert House et al., *Understanding Cultures and Implicit Leadership Theories Across the Globe: An Introduction to Project GLOBE*, 37(1) J. World Bus. 3, 7–8 (2002).

163 Secs. 234–240 of the Companies Act, 2013, notified on 13 April 2017.

164 The term "specified jurisdictions" means and includes jurisdictions specified in Rule 25A(2)(a), and Annexure B to the Companies (Compromises, Arrangements, and Amalgamation) Rules, 2016.

165 Corporate Tax @22% exclusive of Surcharge (2%–5%) & Health and Education Cess 4% (Introduced from Finance Year, 2019). Therefore, the effective corporate tax rate plus surcharge plus cess would be between 25% and 26%.

Unless the present tax regime affecting cross-border mergers is amended and harmonized with all of the other corporate and allied laws, for the time being in force, the popularity of these provisions, despite the latest regulations, will fail to soar. The proposed Direct Tax Code seems to be a possible solution to such issues.[166] The business environment and the legal regime look to be in favour of cross-border mergers in India, as the Direct Tax Code,[167] which emphasizes lowering the corporate tax rate to boost the competitiveness of India's business environment, is likely to promote cross-border M&As in India by making taxing provisions more certain, competitive, and comprehensive. The recent changes in FDI policy and tax reforms therein, including reduction of the corporate tax rate, concessional tax rates for power and infrastructure companies,[168] tax holiday schemes for investors, and the abolition of dividend distribution tax, will go a long way in making India Inc. a favourite among foreign investors and create favourable opportunities for more cross-border M&As in India.[169]

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166 The New Direct Taxes Code Must Not Die, The Economic Times, 16 September 2018 (Jan. 02, 2021), available at https://economictimes.indiatimes.com/blogs/et-editorials/the-new-direct-taxes-code-must-not-die/.

167 Proposed legislation to replace the Income Tax Act, 1961; presently pending in parliament and most likely to be implemented soon. Shrimi Choudhary, *'Too Radical': Centre Likely to Implement Direct Tax Code in Parts*, Business Standard, 4 February 2020 (Jan. 02, 2021), available at https://www.business-standard.com/budget/article/too-radical-centre-likely-to-implement-direct-tax-code-in-parts-120020400029_1.html.

168 *See also* Gaurav Shukla & Akanksha Garg, *Deductions; Profit and Gains Derived from Industrial Undertaking Held by Companies*, 180(1) TAXMAN 172 (2009).

169 DIPP, Review of Foreign Direct Investment (FDI) Policy on Various Sectors, Press Note No. 4 (2019 Series) (2020) (Jan. 02, 2021), available at https://dipp.gov.in/sites/default/files/pn4_2019.pdf; DIPP, Review of Foreign Direct Investment (FDI) Policy for Curbing Opportunistic Takeovers/Acquisitions of Indian Companies Due to the Current COVID-19 Pandemic, Press Note No. 3 (2020 Series) (2020) (Jan. 02, 2021), available at https://dipp.gov.in/sites/default/files/pn3_2020.pdf.

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Information about the authors

Avin Tiwari (Kharagpur, India) – UGC SRF (Law), Ph.D. Scholar, Rajiv Gandhi School of Intellectual Property Law, Indian Institute of Technology Kharagpur (Kharagpur, West Bengal, 721302, India; e-mail: avintiwari2016@gmail.com).

Gaurav Shukla (Suva, Fiji) – Lecturer in Law, School of Law and Social Sciences (SoLaSS), University of the South Pacific (Suva, 1168, Fiji; e-mail: gaurav.shukla@usp.ac.fj; gaurav.gauravshukla@gmail.com).