

## M&A Hotline

July 21, 2016

### TIME TO RECONSIDER MERGERS AND ACQUISITIONS PRICING NORMS?

The article was first published in the July 20, 2016 edition of the economic times.

It is almost universally accepted that valuation is an art and not a science and the value determined by one expert can vary significantly from that of the other expert especially for large and complex M&A (mergers and acquisitions) transactions even if both the experts are independent and reputed. Rather ironically, the Indian M&A rules rely heavily on valuation reports and fairness opinions prepared by experts based on historical market prices.

For example, the Indian takeover code prescribes the minimum offer price to be the higher of — the price paid to the controlling shareholders or the historical market price calculated as per a prescribed formula. Curiously, courts have applied the traditional business judgment rule to examine the fiduciary duties of directors in the context of M&As and consequently adopted a hands off approach to valuation (or other business decisions) unless mala fides are established.

This approach may not be the most optimum and certainly requires a closer re-look. To elaborate, consider the example of the recent Delaware Chancery Court ruling in the Dell buyout case. To provide some context first — In 2012, Michael Dell, the founder of Dell Inc. (Dell) communicated to its board his intention to partner with Silver Lake, a financial sponsor and take Dell private after the stock had underperformed for almost half a decade.

The board hired at least three financial advisors to set in motion a sale process to ascertain the fair value of the shares of Dell. The board and its team of advisors approached several financial sponsors prior to the signing of the deal. Curiously, the board had not approached any strategic buyer prior to signing the deal with Michael Dell and Silver Lake but had engaged with one such strategic buyer, Hewlett Packard only after the deal with Michael Dell and Silver Lake was inked.

After almost 15 months of hectic negotiations and after evaluation of several offers including one from the legendary activist shareholder Carl Icahn, the shareholders by a very narrow margin approved Michael Dell and Silver Lake's merger offer. The merger offer, which was recommended by the board, touted as fair by the financial advisors, and approved by the shareholders was at a significant premium to the current and historical market prices. Significant number of shareholders dissented to the merger price and invoked the appraisal jurisdiction of the Delaware courts to determine the fair value of the shares.

The Delaware court found the merger price to be unfair. At the heart of the Delaware court's findings were three factors — first, the market price cannot be considered as a benchmark as the value of each share does not represent the intrinsic value of the entire company, especially, when the company is undergoing a transformation and the market has undervalued such a stock. Second, the financial sponsors valued the company in a way that would enable them to achieve a certain IRR (internal rate of return) after 4-5 years and therefore, such a self-serving process of valuation could not be used as a benchmark to determine the fair value of a company. Third, the sale process was not competitive enough to achieve a fair price as the board of Dell had not actively engaged with strategic buyers and other noteworthy financial sponsors prior to signing the deal with the Michael Dell and Silver Lake. The court finally based on its own analysis of the discounted cash flow valuation presented by two expert witnesses arrived at the revised merger price which was significantly higher than the original merger price.

A similar fact pattern in the Indian context would have resulted in divergent outcomes and the intent of this piece is not to undertake a prognosis of that. However, the ruling has a larger philosophical undertone which policymakers and all M&A stakeholders in India must take note of. The ruling re-enforces a couple of points — one, market or deal price is not necessarily reflective of the fair price in a M&A scenario and two, fair value cannot be achieved by only commissioning an independent valuation but a competitive and robust sale process is imperative in achieving a fair outcome. The Indian takeover code does not endeavour to achieve a "fair" value for the minority shareholders but instead endeavours to assure a price which is not "inferior" to the one paid to the controlling shareholders. This pricing policy while persuasive may be suboptimal in the Indian context.

First, due to the concentrated shareholding pattern of Indian companies, an acquirer can achieve a controlling stake merely by negotiating a deal with the controlling shareholder and therefore, there is no incentive to pay a premium to the minority shareholders to acquire their shares. Second, the controlling shareholders, especially, in the case of India where still a significant number of listed entities are family owned, may have various reasons of exiting a company including to deleverage group debt, explore a new line of business etc. and in such cases the controlling shareholder may not necessarily strike a deal at a "fair" price. Third, while any additional disguised payment such as non-compete fees, etc. is required to be added to the offer price per the existing Indian takeover rules, there are still instances of camouflaged payments being made to controlling shareholder in the form of guarantees, board seats and fees in lieu thereof, future business arrangements, etc. These disguised payments render a body blow to the

## Research Papers

### Mergers & Acquisitions

July 11, 2025

### New Age of Franchising

June 20, 2025

### Life Sciences 2025

June 11, 2025

## Research Articles

### 2025 Watchlist: Life Sciences Sector India

April 04, 2025

### Re-Evaluating Press Note 3 Of 2020: Should India's Land Borders Still Define Foreign Investment Boundaries?

February 04, 2025

### INDIA 2025: The Emerging Powerhouse for Private Equity and M&A Deals

January 15, 2025

## Audio

### CCI's Deal Value Test

February 22, 2025

### Securities Market Regulator's Continued Quest Against "Unfiltered" Financial Advice

December 18, 2024

### Digital Lending - Part 1 - What's New with NBFC P2Ps

November 19, 2024

## NDA Connect

Connect with us at events, conferences and seminars.

## NDA Hotline

Click here to view Hotline archives.

## Video

### Reimagining CSR: From Grant Giving to Blended Finance & Outcome Based Funding

June 16, 2025

### Courts vs Bankruptcy code: The

entire philosophy of assuring a “non-inferior” price for the minority shareholders.

The question is where does all this leave the minority shareholders today? To be fair, all is not gloomy for the minority shareholders. There is enough in the Indian M&A rules which can be relied upon to force boards to get a fair outcome. For example, the Indian takeover rules require independent directors to provide a “reasoned” recommendation on an open offer.

Similarly, in the case of mergers, the listing rules require the audit committee to approve the valuation. Can these be construed to mean that the boards are required to achieve a fair price or undertake a sale process to obtain the best price? Are boards required to ensure that there are no disguised payments and therefore actively engage in the deal negotiations? Will the courts question the fairness of the business decisions and abandon the blanket reliance on the business decisions made by the board (traditional business judgement rule) in suitable cases? An ambitious and activist shareholder will certainly test these propositions, especially, in an environment where the stakes are high. Board of Indian companies on their part would do well to take a more nuanced position of their role in M&As as given the global trend their actions would be under microscopic scrutiny.

— **Ankit Mishra & Nishchal Joshipura**

You can direct your queries or comments to the authors

---

## DISCLAIMER

The contents of this hotline should not be construed as legal opinion. View detailed disclaimer.

This Hotline provides general information existing at the time of preparation. The Hotline is intended as a news update and Nishith Desai Associates neither assumes nor accepts any responsibility for any loss arising to any person acting or refraining from acting as a result of any material contained in this Hotline. It is recommended that professional advice be taken based on the specific facts and circumstances. This Hotline does not substitute the need to refer to the original pronouncements.

This is not a Spam mail. You have received this mail because you have either requested for it or someone must have suggested your name. Since India has no anti-spamming law, we refer to the US directive, which states that a mail cannot be considered Spam if it contains the sender's contact information, which this mail does. In case this mail doesn't concern you, please unsubscribe from mailing list.

**JSW-Bhushan Saga**

June 04, 2025

**Vyapak Desai speaking on the danger of deepfakes | Legally Speaking with Tarun Nangia | NewsX**

April 01, 2025