

May 11, 2005

All Scheduled Commercial Banks

Dear Sirs

Guidelines for merger /amalgamation of private sector banks

Reserve Bank of India had constituted, on the recommendations of the Joint Parliamentary Committee (2002), a Working Group to evolve guidelines for voluntary mergers involving banking companies. Based on the recommendations of the Group, the guidelines laying down the process of merger proposal, determination of swap ratios, disclosures, the stages at which Boards will get involved in the merger process and norms of buying / selling of shares by the promoters before and during the process of merger have since been finalised. The detailed guidelines are enclosed.

2. While dealing with the merger proposals between two banking companies or between a banking company and a non-banking financial company, banks may act in accordance with the enclosed guidelines. Boards of the banks have to play a crucial role in the process. It may be ensured that the decision of merger should be approved by two third majority of the total Board members and not those present alone. However, in view of the importance of the responsibility implicit in such merger decisions, it will be necessary that the directors who participate in such meetings are signatories to the Deeds of Covenants as recommended by Ganguly Working Group on Corporate Governance, forwarded to banks vide our circular DBOD.No.BC.116/08.139.001/2001-02 dated June 20, 2002.

3. The principles underlying the above guidelines would also be applicable as appropriate to public sector banks.

Yours faithfully
(Prashant Saran)
Chief General Manager

Guidelines for merger/amalgamation of private sector banks

1. General

- 1.1 The Reserve Bank has discretionary powers to approve the voluntary amalgamation of two banking companies under the provisions of Section 44A of the Banking Regulation Act, 1949.
- 1.2 These powers do not extend to the voluntary amalgamation of a banking company with a non-banking company where amalgamations are governed by sections 391 to 394 of the Companies Act, 1956 in terms of which, the scheme of amalgamation has to be approved by the High Court.
- 1.3 However, in both situations, the Reserve Bank is concerned that while amalgamations are normally decided on business considerations such as the need for increasing the market shares, synergies in the operations of businesses, acquisition of a business unit or segment etc., it is essential that considerations like sound rationale for the amalgamation, the systemic benefits and the advantage accruing to the residual entity are evaluated in detail.
- 1.4 These guidelines cover two situations namely :-
 - (a) An amalgamation of two banking companies
 - (b) An amalgamation of a non-banking finance company (NBFC) with a banking company.

2 Amalgamation between two banking companies

- 2.1.1 Section 44A of the Banking Regulation Act, 1949 requires that the draft scheme of amalgamation has to be approved by the shareholders of each banking company by a resolution passed by a majority in number representing two-thirds in value of the shareholders, present in person or by proxy at a meeting called for the purpose.
- 2.1.2 Before convening the meeting for the purposes of obtaining the shareholders' approval, the draft scheme of amalgamation needs to be approved individually by the Boards of Directors of the two banking companies. When according this approval, the Boards need to give particular consideration to the following matters :-

- (a) The values at which the assets, liabilities and the reserves of the amalgamated company are proposed to be incorporated into the books of the amalgamating banking company and whether such incorporation will result in a revaluation of assets upwards or credit being taken for unrealized gains.
- (b) Whether due diligence exercise has been undertaken in respect of the amalgamated company.
- (c) The nature of the consideration, which, the amalgamating banking company will pay to the shareholders of the amalgamated company.
- (d) Whether the swap ratio has been determined by independent valuers having required competence and experience and whether in the opinion of the Board such swap ratio is fair and proper.
- (e) The shareholding pattern in the two banking companies and whether as a result of the amalgamation and the swap ratio the shareholding of any individual, entity or group in the amalgamating banking company will be violative of the Reserve Bank guidelines or require its specific approval.
- (f) The impact of the amalgamation on the profitability and the capital adequacy ratio of the amalgamating banking company.
- (g) The changes which are proposed to be made in the composition of the board of directors of the amalgamating banking company, consequent upon the amalgamation and whether the resultant composition of the Board will be in conformity with the Reserve Bank guidelines in that behalf.

2.2.1 Section 44A of the Banking Regulation Act, 1949 also requires that after the scheme of amalgamation is approved by the requisite majority of shareholders in accordance with the provisions of the Section, it shall be submitted to the Reserve Bank for sanction.

2.2.2 To enable the Reserve Bank to consider the application for sanction, the amalgamating banking company should submit to the Reserve Bank the information and documents specified in Annexure A.

2.3.1 The aforementioned Section provides that a dissenting shareholder is entitled, in the event of the scheme being sanctioned by the Reserve Bank, to claim from the banking company concerned, in respect of the shares held by

him in that company, their value as determined by the Reserve Bank when sanctioning the scheme and such determination by the Reserve Bank as to the value of the shares to be paid to the dissenting shareholders shall be final for all purposes.

2.3.2 To enable the Reserve Bank to determine such value, the amalgamated banking company should submit the following: -

- (a) a report on the valuation of the share of the amalgamated company made for this purpose by the valuers appointed for the determination of the swap ratio
- (b) detailed computation of such valuation
- (c) where the shares of the amalgamated company are quoted on the stock exchange:-
 - (i) details of the monthly high and low of the quotation on the exchange where the shares are most widely traded together with number of shares traded during the six months immediately preceding the date on which the scheme of amalgamation is approved by the Boards.
 - (ii) the quoted price of the share at close on each of the fourteen days immediately preceding the date on which the scheme of amalgamation is approved by the Boards.
- (d) Such other information and explanations as the Reserve Bank may require.

3. **Amalgamation of an NBFC with a banking company**

3.1 Where the NBFC is proposed to be amalgamated into a banking company, the banking company should obtain the approval of the Reserve Bank of India after the scheme of amalgamation is approved by its Board but before it is submitted to the High Court for approval.

3.2 When according its approval to the scheme, the Board should give consideration to the matters listed in paragraph 2.1.2 above. In addition, it should examine whether: -

- (a) The NBFC has violated / is likely to violate any of the RBI/SEBI norms and if so, ensure that these norms are complied with before the scheme of amalgamation is approved.

- (b) The NBFC has complied with the "Know Your Customer" norms for all the accounts, which will become accounts of the banking company after amalgamation.
 - (c) The NBFC has availed of credit facilities from banks/FIs and if so, whether the loan agreements mandate the NBFC to seek consent of the bank/FI concerned for the proposed merger/amalgamation.
- 3.3 To enable the Reserve Bank of India to consider the application for approval, the banking company should furnish to Reserve Bank of India information and documents listed in Annexure A excluding item 4 and also the information and documents listed in paragraph 2.3.2 above.
- 3.4 The provision of paragraphs 3.1 to 3.3 above will also apply mutatis mutandis in the rare cases where a banking company is amalgamated into an NBFC.

4. Norms for promoter buying or selling shares directly/indirectly, before, during and after discussion period

- 4.1 Regulation 2(ha) of the SEBI (Prohibition of Insider Trading) Regulations, 1992, which is applicable to the securities of listed companies, defines price sensitive information, as "any information which relates directly or indirectly to a company and which if published is likely to materially affect the price of the securities of the company".
- 4.2 SEBI regulations on Prohibition of Insider Trading should be strictly complied with, as the various information relating to takeover/merger and transfer of shares of listed banks / NBFCs are price sensitive. Even the unlisted banks / companies should follow the SEBI guidelines in spirit and to the extent applicable.

Information and documents to be furnished along with the application of Scheme of Amalgamation

1. Draft scheme of amalgamation as placed before the shareholders of the respective banking companies for approval.
2. Copies of the notices of every meeting of the shareholders called for such approval together with newspaper cuttings evidencing that notices of the meetings were published in newspapers at least once a week for three consecutive weeks in two newspapers circulating in the locality or localities in which the registered offices of the banking companies are situated and that one of the newspapers was in a language commonly understood in the locality or localities.
3. Certificates signed by each of the officers presiding at the meeting of shareholders certifying the following:
 - (a) a copy of the resolution passed at the meeting;
 - (b) the number of shareholders present at the meeting in person or by proxy;
 - (c) the number of shareholders who voted in favour of the resolution and the aggregate number of shares held by them;
 - (d) the number of shareholders who voted against the resolution and the aggregate number of shares held by them;
 - (e) the number of shareholders whose votes were declared as invalid and the aggregate number of shares held by them;
 - (f) the names and ledger folios of the shareholders who voted against the resolution and the number of shares held by each such shareholder;
 - (g) the names and designations of the scrutineers appointed for counting the votes at the meeting together with certificates from such scrutineers confirming the information given in items (c) to (f) above;
 - (h) the name of shareholders who have given notice in writing to the Presiding Officer that they dissented from the scheme of amalgamation together with the number of shares held by each of them.
4. Certificates from the concerned officers of the banking companies giving names of shareholders who have given notice in writing at or prior to the meeting to the banking company that they dissented from the scheme of amalgamation together with the number of shares held by each of them.
5. The names, addresses and occupations of the Directors of the amalgamating banking company as proposed to be reconstituted after the amalgamation and indicating how the composition will be in compliance with Reserve Bank regulations.
6. The details of the proposed Chief Executive Officer of the amalgamating banking company after the amalgamation.

7. Copies of the reports of the valuers appointed for the determination of the swap ratios.
8. Information which is considered relevant for the consideration of the scheme of amalgamation and the swap ratio including in particular:
 - (a) annual reports of each of the banking companies for each of the three completed financial years immediately preceding the Appointed Date for amalgamation;
 - (b) financial results, if any, published by each of the banking companies for any period subsequent to the financial statements prepared for the financial year immediately preceding the Appointed Date;
 - (c) pro-forma combined balance sheet of the amalgamating banking company as it will appear as of the Appointed Date consequent on the amalgamation;
 - (d) computation based on such pro-forma balance sheet of the following:
 - (i) Tier I Capital
 - (ii) Tier II Capital
 - (iii) Risk - Weighted Assets
 - (iv) Gross and Net NPAs
 - (v) Ratio of Tier I Capital to Risk-Weighted Assets
 - (vi) Ratio of Tier II Capital to Risk Weighted Assets
 - (vii) Ratio of Total Capital to Risk Weighted Assets
 - (viii) Tier I Capital to Total Assets
 - (ix) Ratio of Gross and Net NPAs to Advances
9. Information certified by the valuers as is considered relevant to understand the proposed swap ratio including in particular:
 - (a) the methods of valuation used by the valuers;
 - (b) the information and documents on which the valuers have relied and the extent of the verification, if any, made by the valuers to test the accuracy of such information;
 - (c) if the valuers have relied upon projected information, the names and designations of the persons who have provided such information and the extent of verification, if any, made by the valuers in relation to such information;
 - (d) details of the projected information on which the valuers have relied;
 - (e) detailed computations of the swap ratios containing explanations for adjustments made to the published financial information for the purposes of the valuation;
 - (f) if these adjustments are made based on valuations made by third parties, details regarding the persons who have made such valuations;
 - (g) capitalisation factor and weighted average cost of capital (WACC) used for the purposes of the valuation and justification for the same;
 - (h) if market values of shares have been considered in the

computation of the swap ratio, the market values considered and the source from which such values have been derived;

- (i) if there are more than one valuer, whether each of the valuers have recommended a different swap ratio and if so, the above details should be given separately in respect of each valuer and it may be indicated how the final swap ratio is arrived at.

10. Such other information and explanations as the Reserve Bank may require.