

## **Role of Banks as Independent Adviser in Takeovers and Mergers in Pakistan**

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**Abstract:** The research evaluates Pakistan's corporate laws that govern takeover and merger activity in the country, to suggest amendments in Pakistan's governing laws for introducing the role of the independent adviser in takeovers and mergers to bring them at par with the laws of developed economies and to suggest the benefits of promoting the banks role as one of the most suitable independent advisers on takeovers and mergers. In developed economies, the law imposes an obligation on the companies involved in takeovers and mergers to engage independent advisers to provide an independent advice to enable the shareholders to make an informed decision as to the merits of the takeover or merger transaction. However, there is no mention of the term 'independent adviser' in Pakistan's corporate laws and the companies are not required to obtain independent advice to decide about a takeover or merger offer. Various studies confirm that the expert advice provided by the banks as the independent adviser on takeovers and mergers, not only enables the shareholders to make an informed decision but also safeguards their interest by ensuring compliance with governing laws. This area of research is however, wholly neglected in Pakistan. Neither the role of advisers on takeovers and mergers is ever discussed generally, nor the bank's role as an independent adviser is discussed particularly. This research serves as the foundation work for the subject of the independent advisers and prospective role of banks as an independent adviser in takeovers and mergers in Pakistan. It provides a comparative review of Pakistan's corporate laws with the laws of other jurisdictions, specifically Malaysia and suggest requisite amendments in Pakistan's takeover and merger laws.

**Key words:** Independent adviser, banks, mergers, takeovers, foundation work, governing laws, obligation

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### **INTRODUCTION**

The modern world has seen the formation of companies as a mechanism of integration, enabling individuals with an entrepreneurial approach to establish companies and invest their capital and expertise to further their business objectives. In today's fast-changing business world, companies must strive hard to achieve quality and excellence in their field of operation. The now developed takeover and merger strategies which we hear about have not been invented in recent times. Instead, the first time takeovers and mergers got commerciality at the end of the 19th century. Since then, cyclic waves have been emerging due to radically different strategic motivations.

It can be stated with reasonable certainty that the prime objective of all companies is growth which is possible internally as well as externally. Internal growth can be achieved either through the process of introducing or developing new products or by expanding or enlarging the capacity of existing products or sustained improvement in sales (Mallikarjunappa and Nayak, 2007). On the other hand, external growth can be achieved by companies through multiple avenues such as the acquisition of an existing business through takeovers and

mergers being the primary modes. Takeovers and mergers have received attention from different walks of life, for the changes that these have brought to the market structure.

In many instances, takeovers and mergers have resulted in better use of resources and greater efficiency. Although, a range of benefits may be sought through acquisitions in general, acquisitions are completed primarily to maximise a company's value (Salter and Weinhold, 1979). Various factors decide whether the specific takeover or merger turns out as a success or a failure and the advisory services are one of these factors. The independent adviser, either individual or institutional to the target or acquirer is a vital player to add value to the outcome of takeover and merger transactions.

Due to the rather complex nature of takeovers and mergers, a fundamental requirement of involving external experts to assist with these transactions is both, perceived and needed by the management of the companies involved in takeovers and mergers. The generic term 'adviser' covers all professional advisers including lawyers, accountants, engineers, financial institutions and banks. The term adviser is broad enough to include individual as well as institutional advisers. However in this research, the discussion is focused on banks and their

role as an independent adviser in takeover and merger transactions. To the extent of this research, the term banks refer to the investment banks and investment units of the commercial and Islamic banks.

Independent adviser prepares a report, known as independent adviser's report or the independent advice circular to help directors and shareholders of the companies involved in takeover or merger to deliberate about the desirability of the prospective deal. The adviser's report is critical as it contributes significantly to enable the directors and shareholders to make an informed decision on essential elements of the deal. The adviser's report is discussed in this research, albeit it is not focused on the report per se but on the role of advisers in preparing the report for shareholders of the companies involved in the takeover or merger transaction.

Takeovers and mergers have been responsible for many significant structural changes in different corporate sectors which have substantially changed the environment in which the organizations operate. During the last decade, takeovers and mergers have hit almost every sector of life and this phenomenon is particularly real for well-developed Western countries and to some extent, Malaysia and Singapore. However, the corporate takeover and merger activity are rather minimal in Pakistan as compared to other developed countries of the world, despite the great potential in the market. Takeovers and mergers can be a significant source of economic activity in Pakistan, provided that the several challenges which stand in the way are diligently navigated and ultimately surpassed.

Although, Pakistan is a developing country with a fertile market, the laws and the regulatory framework related to the capital market and corporate governance are not compatible to meet the needs of the time. In particular, the area of corporate laws on takeovers and mergers and protection of investor's interests therein are not given due attention. The lack of corporate governance is very challenging for Foreign investors to handle, especially when they initiate a takeover or merger to acquire the control of existing businesses in Pakistan.

Lack of takeover and merger activity in Pakistan is primarily due to the reason that most of the companies in the country are still run by owner-entrepreneurs, who generally own controlling shares of the company. Although, it is not an unhealthy thing in itself, there is always a likelihood of the oppression of minority shareholders. The complex and tedious process to undertake a takeover or merger and lack of corporate governance in Pakistan discourages the investors to consider external growth by using the strategy of takeover or merger. In Pakistan, the companies can initiate takeover and merger through a standard agreement between the target and the acquirer. However, a simple

agreement would not provide legal cover to the parties to the transaction unless it carries the sanction of the court of proper jurisdiction.

Primary statutes that govern takeover and merger activity in Pakistan are the Companies Act 2017, Securities Act 2015, Competition Act 2010, Stock Exchange (Corporation, Demutualization and Integration) Act 2012, Competition Act 2015 and the Listed Companies (Substantial Acquisition of Voting Shares and Takeovers) Ordinance 2002. The regulations that regulate takeover and merger transactions are the Listed Companies (Substantial Acquisitions of Voting Shares and Takeovers) Regulations 2017 and the Competition (Merger Control) Regulations 2016. There is no pending or draft legislation related to the governance of takeover and merger activity.

None of the corporate laws of Pakistan defines the term independent adviser in general or in the specific context of takeovers and mergers. Moreover, the companies engaged in takeovers and mergers are not obliged by law to appoint an adviser to provide expert advice to decide about a takeover or merger proposal. Malaysia on the other hand, has comprehensive laws related to takeovers and mergers as compared to Pakistan. Malaysia's Companies Act 2016, Capital Market and Services Act 2007, Code on Takeovers and Mergers 2016 and Rules on Takeovers, Mergers and Compulsory Acquisitions 2016 deal with transactions related to change of control in companies.

Malaysia's takeover and merger laws provide very stringent and comprehensive principles to ensure the independent advisers play their role effectively to safeguard the interest of shareholders as well as to close the takeover and merger transactions successfully (Malaysia's Principal Adviser Guidelines, issued on May 8, 2009). Malaysia's takeover and merger laws oblige the board of directors of the companies involved in takeover or merger, to appoint an independent adviser who shall provide independent advice, so that, the shareholders can make an assessment on the merits and demerits of the offer (Code on Takeovers and Mergers 2016 (Malaysia), General Principle: 4).

Malaysia's takeover and merger laws emphasize on the role of independent advisers and specify the duty of the board of directors to appoint an independent adviser. Malaysia's takeover and merger laws have defined independent advisers and laid down criteria of their independence, scope of their role and responsibilities in clear terms. Malaysia's laws offer comprehensive guidelines to determine the independence of advisers (Rules on Takeovers, Mergers and Compulsory Acquisitions 2016 (Malaysia), Rule 3). In Malaysia, the board of director is required to seek independent advice from independent advisers when there is a takeover offer for the company, under Malaysia's Code on Takeovers

and Mergers in principally for corporate transactions involving listed on the Malaysia Stock Exchange (Rule of Takeovers, Mergers and Compulsory Acquisitions 2016 (Malaysia), Rule 3).

Malaysia's corporate laws provide adequate protection to the independent advisers against claims from shareholders or the companies involved in a takeover or merger transactions, in particular setting out the provisions of defences that are available to the advisers against litigation, in cases where the advisers have discharged their duties according to the required standards. The law further guides the soundness of the advice such as 'reasonableness' and 'fairness' of the offer (Rules on Takeovers, Mergers and Compulsory Acquisitions (Malaysia), Rule 11.3). Malaysia's takeover laws require the parties involved in takeovers and mergers to make full and prompt disclosure of all relevant information (Code on Takeovers and Mergers 2016 (Malaysia) General Principle, 5).

In Malaysia's takeover and merger laws, the shareholders and the board of directors of an offeree and the market for the shares that are the subject of a takeover offer shall be provided with relevant and sufficient information including the identity of the acquirer or offeror, to enable them to reach an informed decision on the takeover offer and reasonable time to consider the takeover offer (Code on Takeovers and Mergers 2016 (Malaysia), General Principle, 6). This is instrumental in providing adequate information to market players who shall be meaningful and useful to help shareholders of the companies in making an informed decision as to the merits of takeover or merger offer.

Pakistan on the other hand, lacks such corporate laws. In Pakistan, the companies involved in takeover and merger transactions are not required by law to appoint an adviser to give independent expert advice to its shareholders. Generally and as a matter of practice, in case of large and complex transactions, the companies involved in takeover or merger engage legal and accounting firms in Pakistan to assist in transactions and conduct due diligence. However, it is now imperative to reform Pakistan's corporate laws relating to corporate restructuring to introduce and formalise the role of the adviser in takeover and merger transactions, specifying criteria of their independence and confirming their responsibilities and obligations. The ultimate aim of these reforms shall be to offer expert advice and necessary guidance to the shareholders to make an informed corporate decision.

In this research, Malaysia's corporate laws, specifically, the laws governing takeover and merger activity are selected as a benchmark to compare with the corporate laws of Pakistan because both countries share many similarities including market structure and shareholding pattern which reflects

ownership concentration (Hasan, 2009; Yasser *et al.*, 2011; Javaid and Iqbal, 2008; Ahmed, 2009; Borhanuddin and Ching, 2011). Just like Pakistan, Malaysia's companies are characterised by high levels of ownership concentration and significant participation of owners in management (Claessens and Fan, 2002; Claessens *et al.*, 2000).

Malaysia's takeover and merger laws offer provisions to endorse the role of investment banks as independent advisers in corporate restructuring including takeovers and mergers (Capital Market and Services Act 2007 (Malaysia), Schedule 4-Part I). Whereas in Pakistan, the corporate laws are silent as to the role of advisers as well as the investment banks as an independent adviser in the takeover and merger transactions, neither restricting nor encouraging their participation.

It is globally accepted that the banks are credible and reputable institutions, primarily because the banking industry has since, the last global recession of 2008, been heavily regulated and monitored. Therefore to enhance investor's confidence, especially, Foreign investors, it is about time that Pakistan's corporate law shall support the investment bank's role as an independent adviser in takeovers and mergers, with a reasonable expectation based on global trends that such a move will eventually increase takeover and merger activity in the country.

There is a need to understand that the strategic intent of businesses, actually drives the takeovers and mergers, not the mere legal or accounting logic. Therefore, the exercise to introduce the independent adviser should not be governed by accounting principles or the legal formalities being the sole consideration. Instead, the major crux of the due diligence exercise is to estimate the proposed synergy between the merging companies based on realistic assumptions.

The banks potentially have comparative advantages in advising as an independent adviser to the companies involved in takeovers and mergers. In Pakistan's corporate sector, banks receive the most confidence and trust. Therefore, their role in any such transaction will enhance the credibility and transparency of the deal, leading to the investor's confidence (Kale *et al.*, 2003). The State Bank of Pakistan (SBP) and Securities and Exchange Commission of Pakistan (SECP) regulates and monitors all financial institutions in Pakistan. It is a nationally accepted fact that the SBP is a very stringent and diligent regulator. Therefore, a higher level of supervision and strict accountability of the banks as the adviser is practically possible, keeping the adviser on toes and preventing defective advice.

This research offers an insight into Pakistan's corporate laws related to takeover and merger activity. It further covers the role of regulators that regulate the takeover and merger activity in Pakistan. This research provides a comparative perspective of Pakistan's

corporate laws governing takeovers and mergers with Malaysia's corporate laws. Compared to Pakistan, Malaysia's laws offer greater investor protection to the investors involved in the process of takeovers and mergers and ensure transparency of the transaction. The Securities Commission Malaysia (SC Malaysia) plays an effective supervisory role in Malaysia to regulate adviser's role in takeover and merger transactions.

This research is helpful for Pakistani authorities, so, they may evaluate, scrutinise, compare and accordingly reform corporate laws of Pakistan that govern takeover and merger activity in the country. It provides a foundation for the legislators and regulators to analyse the importance of investment banks as the independent adviser in takeovers and mergers to offer expert advice to the board of directors and shareholders of public sector companies and the listed companies, to make an informed decision about a takeover or merger deal.

**Statement of the problem:** Pakistan's corporate laws, especially, laws related to takeover and merger activity are not comprehensive to enable regulatory bodies to do adequate supervision of such transactions. Despite having great potential in the capital market of Pakistan, there is a minimal activity of takeover and merger in the country (Bashir *et al.*, 2011). Due to the lesser activity of takeover and merger, the capital market of Pakistan has faced many problems such as un-utilised market power, limited opportunities for growth and high risk of the business. One of the main reason for the lack of such corporate exercise, along with others is the undeveloped and incomprehensible corporate laws, that are discouraging for foreign strategic investors, those are coming from regimes having developed corporate laws.

In Pakistan, the process of corporate restructuring through takeover or merger is tedious, time-consuming and complicated, hence, discouraging even for local investors. To encourage takeover and merger activity in Pakistan, protection of investor's right is mandatory and that requires amendments in Pakistan's existing corporate laws. Pakistan is in need of amending its corporate laws and regulations to welcome the strategic takeover and merger in the country.

The independent adviser's role is instrumental in enhancing investor's confidence (Kale *et al.*, 2003). The existing corporate laws of Pakistan neither defines independent advisers nor explain their role, responsibilities, duties and remedies for the shareholders in case of poor advice. In developed countries, where the takeover and merger is the regular phenomenon, the advisers play a vital role to add value in the process of takeover and merger of corporate entities (Kale *et al.*, 2003; Hunter and Jagtiani, 2003). Independent and competent advisers and their concise, informed, unbiased

and thorough advice helps the stakeholders to make an informed decision according to the objectives of the transaction.

Unlike developed countries, Pakistan's corporate laws do not oblige the companies involved in takeovers and mergers to appoint an independent adviser to provide expert advice to its shareholders. In Pakistan, the target and acquirer generally designate legal and accounting companies to give legal and financial consultancy in the process of corporate takeovers and mergers and the terms of engagement letter, generally, govern their role.

**Purpose of the research:** Acquisition of control over a company through takeover or merger involves a variety of information and human capital in analyzing, synthesizing and evaluating both conceptual and technical details. Banks have proved their mettle, nationally and internationally for being specialist in information production and processing. As advisers in takeover and merger transactions, the banks use their information gathering expertise to find out suitable counterparties, the potential for synergistic gains, value of a deal as well as the risks attached to it.

This research seeks to prove that the active and productive role of investment banks operating in Pakistan as independent advisers or deal-makers in transactions related to the acquisition of control over a corporate entity can provide greater protection to the shareholders and allow better supervision from the regulatory body which in turn will encourage takeover and merger activity in Pakistan. The valid corporate law and suitable mechanism in carrying out takeover and merger exercise will increase trust and confidence in the deals and attract more takeovers and mergers.

By virtue of their functions, the investment banks have the potential to play a useful role as independent advisers in takeover and merger transactions to close the deal successfully while safeguarding the interest of the shareholders (Allen *et al.*, 2004; Bowers and Miller, 1990; Hunter and Jagtiani, 2003), if the legal framework governing takeover and merger activity and role of advisers therein is of the international standards and best practices. This research aims to create an awareness that there is a need to reform the legislative and regulatory framework of Pakistan to introduce the independent advisers on takeovers and mergers, criteria of their independence, duties and scope of responsibilities and defences available to an adviser against any claim of shareholders for defective advice.

In Pakistan, the legislative and regulatory developments are now manifesting to bring them at par with the international standards, whereby the law shall include explicit provisions to introduce and promote investment banks as independent advisers. This research seeks to prove that in Pakistan the effective and

independent role of the investment banks as adviser or deal-maker in corporate takeovers and mergers can provide greater protection to the shareholders, allow better supervision from the regulatory standpoint and increase the trust of the investors. This as a result, may encourage takeover and merger activity in Pakistan.

**Research objectives:** The prime objectives of the research are as follows: to analyse Pakistan's corporate laws and regulatory bodies that govern corporate takeover and merger activity in the country. To suggest amendments in Pakistan's takeover and merger laws for introducing the role of the independent adviser in takeovers and mergers to bring these laws at par with the laws of developed economies. To analyze the benefits of promoting the bank's role as one of the most suitable independent advisers for providing independent advice on takeovers and mergers in Pakistan.

**Research questions:** This study investigated the following research questions: Do Pakistan's takeover and merger laws support the role of the independent adviser in corporate takeovers and mergers? What is the extent of recognition given to independent adviser's role in corporate takeovers and mergers in Pakistan? Why the investment bank's role as an independent adviser in takeovers and mergers is critical and what role can investment bank perform in takeovers and mergers activity in Pakistan?

**Research hypothesis:** The hypothesis are as follows: the developed and competitive takeover and merger laws will enhance corporate governance leading to increase takeover and merger activity in Pakistan, thereby allowing more conducive takeovers and mergers in the country. The introduction of the independent adviser's role in Pakistan's takeover and merger laws can ensure that the shareholders are provided with relevant information and independent advice as to the merits of a takeover or merger offer which is critical for safeguarding the interest of the shareholders. Investment banks can play a useful role in takeovers and mergers as an independent adviser to increase the efficiency of the transaction.

**Significance of the research:** This research enlightens the role of advisers in corporate restructuring, precisely takeovers and mergers. The term 'adviser' in the context of advisory for corporate restructuring includes legal and accounting firms, takeover and merger advisory firms and investment banks. However, this research focuses on the role of the investment banks as the independent adviser in takeover and merger transactions. The research provides a comparative review of Pakistan's corporate laws governing takeover and merger activity in comparison to Malaysia's laws. For the reason that

Malaysia's laws offer greater protection and transparency for minority shareholders and empower SC Malaysia to play an effective role. Pakistan's laws related to various strategies for acquisition of control over a company are however not developed.

Unlike Malaysia, Pakistan's corporate laws do not define independent adviser, either in the context of takeover and merger or in general perspective of commercial activities. Malaysia's takeover and merger laws have established the role of independent adviser comprehensively, along with criteria of its independence, obligations and guidelines to perform this critical role. The guidance provided in Malaysia's corporate laws enables the independent adviser to perform its function effectively.

Results of this comparative research primarily contribute to understanding the current mechanism of takeovers and mergers in Pakistan, laws and regulations governing takeover and merger activity, the prospective role of advisers in takeovers and merger and reforms required in legislative and regulatory systems for more conducive takeovers and mergers. This research supplements the minimal literature available in Pakistan on corporate takeovers and mergers. In Pakistan, this is very first research on the role of independent advisers in takeovers and mergers to provide independent advice to the shareholders.

**Scope of the research:** The research attempts to enlighten the importance of investment bank's role as an independent adviser, in takeovers and mergers of corporate entities. The research discusses the regulatory, legal and other constraints to increase takeover and merger activity in Pakistan and recommends legislative and regulatory reforms that are necessary for making the process of takeover and merger investor-friendly and transparent. It endorses that the role of the adviser is significant in takeovers and mergers for investor's protection to provide independent and expert advice to the shareholders to make an informed decision.

This research seeks to highlight the significance of the role of investment banks as the independent adviser in takeover and merger transactions to attract strategic investors to increase the takeover and merger activity in Pakistan. This research is contextual because in Pakistan, very little research is conducted on takeovers and mergers (Afza and Nazir, 2012). The role of the independent adviser in takeover and merger has never been explored in Pakistan. This research forms a foundation to investigate the role of independent advisers in takeover and merger transactions, particularly the role of investment banks as the independent adviser.

This research is useful for both the academia and the practitioners connected to takeover and merger transactions. For academia, it provides a foundation to

explore different aspects of the independent adviser's role in takeovers and mergers. The practitioners may use this research as a guide to provide a better safeguard to the shareholder's interest in takeover and merger deals.

This research may bring awareness to the legislators and regulators in Pakistan, allowing them to recognize the need to reform corporate laws of the country and bring them in-line with the laws of developed countries. It takes into account the views of legislators, regulators, practitioners, banking professionals, qualified consultants and investors. This research highlights a need to introduce and support the independent advisers in takeovers and mergers by provisions of law as a critical player with an emphasis on the role of investment banks as an independent adviser.

**Literature review:** The literature review provides the reader with an insight into the existing literature about takeovers and mergers and the role of independent advisers in takeover and merger activity, particularly the role of investment banks as an independent adviser. In Pakistan, minimal literature is available about corporate takeovers and mergers and not a single research is available for reference on independent advisers and its efficiency impact on takeovers and mergers. This area of corporate governance, however has been studied in Malaysia in various aspects including the role of investment banks as independent advisers on takeovers and mergers (Shim, 2006; Lai *et al.*, 2015; Weinberg *et al.*, 1979; Krishnasamy *et al.*, 2004).

Corporate restructuring through takeovers and mergers is an immense part of the corporate world. Takeovers and mergers have emerged as one of the most effective methods of corporate restructuring and have therefore, become an integral part of the long-term business strategy of the corporate sector all over the world (Mallikarjunappa and Nayak, 2007). Industries are consolidating around the globe through takeovers and mergers. Takeovers and mergers are occurring at a fast pace in European countries. Though in Asia, takeovers and mergers are more of a solution to stay afloat.

The growth of the trend can be judged from the fact that in the USA the last decade of the 20th century witnessed a threefold increase in the number of takeovers and mergers, whereas a fivefold rise has been reported in terms of value. The number and the value of the takeover and merger transactions in the UK were also exhibiting the same pattern. In India, a neighbouring country to Pakistan, almost 85% of the Indian companies are using takeovers and mergers as core growth strategies. In Malaysia, consolidation through the takeover and merger strategy is also at a rise (Shim, 2006).

The investment banks often arrange takeover and merger deals which bring two or more companies together to form a bigger corporate entity. Research

about the acquisitions of control over corporate entities is often done taking into consideration a multitude of disciplines, e.g., finance, law, business, strategy formulation, organizational growth, human resource management and sociology. Developing countries have adopted the takeover and merger laws of the USA with minor changes as per the requirements of their local market, e.g., Japan, France and Germany (Holmstrom and Kaplan, 2001).

Most of the developed jurisdictions have either already vested exclusive authority in one agency for takeovers and mergers or working to do so. Regulating takeovers and mergers at the level of developed countries demands the removal of all barriers for investors to create a level playing field for receptive companies. The right of establishment and free movement of capital have a tremendous potential impact not only on the regulatory framework for companies but for takeover and merger activities in those companies.

Amedu (2004) and Bello (1999) state that takeovers and mergers are immense terminologies which help achieve business progress, growth and survival. While defining a takeover and merger, they state that a takeover entails when a company acquires another company intending to enjoy profitability and endurance while a merger is an activity in which two or more companies combine their businesses to become one big company. According to these researchers, takeovers and mergers occur to merge the available resources and operations for maximizing the shareholder's wealth.

Corporate takeovers and mergers represent the strategic business techniques that companies use for achieving different motives. Business organisations use takeovers and mergers as vital tools to attain their competitive advantages and to survive in the market (Trautwein, 1990). The outcome of a takeover and merger movement is in overall an advantage to shareholders, when their combined post-merger companies are more important than the two separate pre-merger companies (Pilloff, 1996). Takeovers and mergers stimulate performance because the newly established company will have more substantial market power and other qualitative and quantitative factors (Healy *et al.*, 1992).

Various studies have confirmed that in some takeovers and mergers, there indeed are significant synergies (Wang and Xie, 2008; Masulis *et al.*, 2007; Bris and Cabolis, 2008; Fuller *et al.*, 2002; Shelton, 2000; Baker *et al.*, 2012). However, often the acquirer pays more than the real value of a target, especially when the projections of cost and revenue benefits, made at the time of proposing a takeover or merger are misleading (Singh, 1998). The efficiency of any organization can only be improved when the partners of a merger have no efficiency in cost but it also depends upon the management of both the organizations. Often if a chief

operating officer desires an acquisition, both the internal staff and external advisers come up with whatever projections are required to justify its stance which raises serious concerns on the professionalism of the advisers.

Takeovers and mergers are primarily about acquiring control, either total or substantial, over a corporate entity. Business organizations often use takeovers and mergers to meet their strategic goals, e.g., growth, competitiveness. Small organizations take more benefit of takeover and merger in comparison with large size institutions which are not performing (Sufian, 2004). The correct evaluation of the target company through a proper process of due diligence is essential to bring synergy through acquisition. Numerous studies have been conducted to examine various aspects of takeovers and mergers by using different analysis models (Angwin, 2001; Carline *et al.*, 2009; Brudney and Chirelstein, 1974; Caves, 1989).

In Pakistan, the literature on takeovers and mergers is minimal (Afza and Nazir, 2012; Afza and Yusuf, 2012) and it focuses on the takeovers and mergers of banking companies, especially, efficiency impact in the result of the takeover and merger of banking companies (Qayyum and Khan, 2007; Mehmood and Loan, 2006; Ullah *et al.*, 2010). One of the reasons for limited literature about takeovers and mergers in Pakistan is perhaps the minimal takeover and merger activity in Pakistan. Even the available studies of takeovers and mergers of banking companies are limited to the review of one or two banks.

Ullah *et al.*, (2010) investigated the merger of Faysal Investment Bank Limited with Atlas Investment Bank Limited by comparing the 4 years pre and post-merger performance. Three factors: profitability, solvency and capital adequacy were used to determine the financial performance of the merging banks. The test indicates that there was an insignificant increase in profit while capital adequacy and solvency had improved significantly and the post-merger entity was in a better position due to improvement in technology, administration and increase in capacity of the banks to pay-back their term liability.

Kemal (2012) analysed the post-merger financial performance of the Royal Bank of Scotland (RBS) in Pakistan after it merged with ABN AMRO. He analysed their financial statements for 4 years (2006-2009) by using 20 vital ratios. The results show that the financial performance of RBS in the areas of profitability, liquidity, assets management, leverage and cash flows has been entirely satisfactory before the merger deal and concluded that merger deal fails to improve the financial performance of the bank. However, the results were not validated by any test.

Arshad (2012) analysed the post-merger performance of the Standard Chartered Bank, after it acquires the Union Bank, by applying 11 ratios under efficiency ratios,

liquidity ratios and capital ratios on key financial figures. Union Bank was the eighth largest bank in Pakistan before its merger with Union Bank. The research concluded that the performance of the merged entity decreased after the merger. However, no model was used to verify the decrease in post-merger performance.

In developed countries, the role of independent adviser and its significance in transactions related to the acquisition of control over corporate entities has been studied from various aspects. Bowers and Miller (1990) examined the relationship between acquiring companies' stock returns and the choice of investment banks to decide, whether the first-tier investment banks generate better deals in terms of value creation. They confirmed that total wealth gains are more substantial where either the target or the acquirer uses the first-tier investment bank as an adviser. The results suggest the importance of adviser's credibility (reputation) in takeover and merger transactions.

Golubov *et al.* (2012) gave compelling evidence on the role of independent advisers. They examined different types of acquisitions based on the listing status of companies. In a comprehensive study of 4803 American mergers and acquisitions over the period from 1996 to 2009, they find that top-tier advisers deliver higher bidder returns but only in acquisitions where the target is also a listed company.

There is no literature available on the role of the independent adviser in takeovers and mergers in the context of Pakistan. In particular, the role of investment banks as the independent adviser in transactions related to the acquisition of control of corporate entities is never studied in Pakistan. This research serves as the foundation work for the subject of independent advisers and prospective role of investment banks as an independent adviser in takeovers and mergers. It provides a comparative review of Pakistani laws with the laws of other jurisdictions, specifically Malaysia.

Malaysia's takeover and merger laws oblige the board of directors of the companies involved in takeover or merger, to appoint an independent adviser who shall provide independent advice, so that, the shareholders can make an assessment on the merits and demerits of the offer (Code on Takeovers and Mergers 2016 (Malaysia), General Principle, 4). Malaysia's takeover and merger laws emphasis on the role of independent advisers and specify the duty of the board of directors to appoint an independent adviser. Malaysia's takeover and merger laws have defined independent advisers and laid down criteria of their role and responsibilities in clear terms (Rules on Takeovers, Mergers and Compulsory Acquisitions 2016 (Malaysia), Rule 3.6). Malaysia's laws offer comprehensive guidelines to determine the independence of advisers (Rules on Takeovers, Mergers and Compulsory Acquisitions 2016 (Malaysia), Rule 3). In Malaysia, the Bursa Malaysia has broadly favoured

the Australian position for takeovers and regards 'fair' and 'reasonable' as two distinct criteria (Securities Commission of Malaysia, n. 8 (January 28, 2011)).

In Malaysia, where shareholder's approval is required, the independent adviser is obliged to comment on its report as to whether the transaction is fair and reasonable so far as the shareholders are concerned (Bursa Malaysia's Listing Requirements, 10.08(3)(a)(i)). An offer is regarded as 'fair' if the value of the offer price is equal to or greater than the value of the securities that are subject of the offer, assuming 100% ownership of the target (Wan, 2012). Moreover, the offer is 'reasonable', if it is fair but it may also be 'reasonable' if, even though it is 'unfair'. There are sufficient reasons for the shareholders to accept the offer in the absence of any higher bid before the close of the offer. There are only three combinations: 'fair and reasonable', 'neither fair nor reasonable,' or 'not fair but reasonable'.

One of the classic examples of employing a fair and reasonable test in the recent times is the opinion given by the AM Investment Bank as independent adviser of the Lafarge Malaysia on the mandatory offer made by the YTL Cement which is emerged as the single largest shareholder in Lafarge Malaysia after acquiring the 51% stake from Associated International Cement Ltd. (The Edge Financial Daily, June, 4, 2019). The deal triggered a mandatory takeover at RM 3.75 apiece for all the shares it does not own in Lafarge Malaysia. AM Investment Bank in its independent advice circular filed with Bursa Malaysia on June 3, 2019, recommended the minority shareholders of Lafarge Malaysia to reject the offer and stated that the offer made by the YTL Cement was not fair because the offer price of RM 3.75 represents a discount of between 2.2% and 18.5% over the fair values of between RM 3.83 and 4.60 per Lafarge Malaysia shares. Moreover, the offer is not reasonable due to YTL Cement's intention to maintain Lafarge Malaysia's listing, unless the former or its associates hold more than 90% of Lafarge Malaysia's shares which will result in the group not complying with the public spread requirement.

The role of investment banks as an independent adviser has been investigated from various perspectives in Malaysia. Khan *et al.* (2014) asserted that a recommendation on a takeover offer made by an independent adviser must contain adequate information and be meaningful and useful to the shareholders of the target companies in making an informed decision as to the merits of the takeover offer. The advisers shall be responsible for all of their comments, opinions, information and recommendations contained in their circular issued to either the bidder shareholders or target shareholders.

Rachagan study to provide additional evidence to the mixed literature by exploring the role and determine to comply with an investment bank as a financial adviser in

Malaysia M&A market. In this study, 1695 M&A transactions completed in Malaysia in the period 1995 to 2012 were taken into the investigation to test whether the participants in takeover market in a multi-religious nation behave differently in comparison with those in other countries. He found that in the period from January, 1995 to December, 2012, approximately 38.6% of the Malaysian acquirers hire an investment bank when conducting M&A transactions. On the other hand, 23.8% of the target firms employ at least one investment bank as a financial adviser when dealing with Malaysian bidders.

The findings reveal that both participants tend to hire an investment bank when the acquirer operates in the technology sector, the deal takes place in the crisis period and the value of the transaction is high. Acquirer who has a high debt ratio is less likely to employ an investment bank and a publicly-traded target is more likely to employ an investment bank in their M&A transactions. Moreover, the results show that employing investment banks as financial advisers have no impact on the valuation of the targets.

In Pakistan, corporate takeovers and mergers are not given much attention. Therefore, minimal literature is available on corporate takeovers and mergers and its ancillary subjects. It can be stated with reasonable certainty that the lack of literature may be a result of minimal takeover and merger activity in Pakistan. There are many discouraging factors to corporate takeovers and mergers activity in Pakistan, apart from undeveloped corporate laws. The few critical barriers include the less significant synergistic operative economy which negates the benefit that may accumulate because of takeover and merger, complex procedures, lack of motivation by the shareholders, small industrial base which limits the opportunity for diversification, lack of leveraged buyouts, harsh reality of insider trading and information constraint. However, nothing is more discouraging for takeovers and mergers in Pakistan than the incomprehensible and undeveloped corporate laws and less effective regulatory bodies. Khalid Mirza, the founding chairman of SECP and CCP, asserted during his speech that in Pakistan, takeover and merger activity is still in its infancy stage and the total deals done are negligible as compared to developed countries and even countries in South East Asia. He emphasised the need for a comprehensive takeover code which would lay out the ethical and social responsibilities of the parties involved in the takeover and merger exercise.

The takeover and merger control regime in Pakistan has seen a little development to bring it in line with international practices with the establishment of the CCP. However, it is still lagged if compared with developed countries. Pakistan's Takeover Ordinance, 2002 has received criticism from legislators and industry



experts for being not compatible with the laws of developed countries. The corporate laws are inadequate in facilitating takeovers and mergers and it ought to be simplified and overhauled and need revamping.

The regulatory bodies regulate the market as per the powers and guidance provided by the laws and regulations. Currently, the undeveloped corporate laws of Pakistan are unable to guide in various critical corporate matters including the restructuring of companies through takeovers and mergers. The lack of legislative support cripple the regulatory authorities, rendering them incapable of carrying out their supervisory duties at par with the regulators of developed countries.

In Pakistan, before undertaking a takeover or merger transaction, approval of various authorities is mandatory. The SECP and CCP are the primary authorities to sanction a takeover or merger transaction. The role of courts in approving takeovers and mergers under the Companies Act, 2017 of Pakistan is also of critical importance. It laid down the principle that the scheme amalgamation, including takeover or merger, must receive the sanction of the court. The Banking Companies Ordinance, 1962 govern takeovers and mergers of banking companies. Therefore, in case of a takeover or merger of any banking company, approval of the SBP is also mandatory (Banking Companies Ordinance 1962, Section 48).

## **MATERIALS AND METHODS**

The research methodology is a strategy of inquiry which moves from the underlying assumptions to research design and data collection. The type of methodology adopted by any research depends upon the objectives of the research. Studies confirm that the qualitative research methodology typically answers the questions, e.g., where what, who and when. However, it does not adequately explain why and how a phenomenon occurs. Qualitative methodology is selected to undertake this research given the social nature of the subject, the minimal number of takeover and merger transactions in Pakistan and no transaction which could qualify the criteria of this research.

In qualitative research, the qualitative data is collected and analysed to support the research objectives. Qualitative data are an in-depth description of circumstances, people, interactions, observations, events, attitudes, thoughts and beliefs and direct quotes from people who have experienced or are experiencing the phenomenon (Patton, 2002). Domegan and Fleming (2007) defined qualitative research as a kind of research which aims to explore and to discover issues about the problem at hand, because very little is known about the problem and there is usually uncertainty about dimensions and characteristics of the problem. Hence, qualitative

research is one of the adequate methodologies to study the role of the independent adviser in takeovers and mergers in Pakistan which is never being studied in Pakistan.

The research is based on a non-doctrinal approach for revealing and explaining the concerned laws, regulatory system and the impact of the legal phenomena on the takeover and merger activity in Pakistan. Doctrinal research which is one of the most common methods to study legal proposition, focusses on legal principle generated by the courts and the legislature (Bartie, 2010). However, to explore the role of investment banks as an independent adviser in takeovers and mergers in Pakistan, there are no legal provisions or principles derived by the courts from those statutory provisions to study or refer to. The research methodology for this study is descriptive and interpretive which is analyzed through qualitative methods. Observations of participants of takeovers and mergers, interviews and survey of various takeover and merger cases during the period under review have been primary resources to collect data for this research.

In comparison to Pakistan, Malaysia has more developed corporate laws; therefore, Malaysia's takeover and merger laws are used as a reference point. References from laws and regulations of Malaysia related to takeovers and mergers, especially on the role of independent advisers in takeovers and mergers are discussed to give a comparative review. The research objectively compares the corresponding provisions of Malaysia's takeover and merger laws with the provisions of Pakistan's takeover and merger laws. References from other jurisdictions are also made when necessary. The research is explanatory and descriptive which critically analyses the corporate laws of Pakistan that govern takeover and merger activity in Pakistan, especially, the role of independent advisers in takeover and merger exercises.

The research has brought various reference of studies from other jurisdictions to support the point raised in this research, that the investment banks can play a useful role in takeover and merger transactions, to meet the desired results and increase the efficiency of the transaction while safeguarding the interest of the shareholders. This in a result, can encourage the takeover and merger activity in any market. It is a multi-method research strategy which supports the exploratory and descriptive nature of the research and enables it to achieve its objectives.

The research is found in the data mediated directly or indirectly by documentary evidence and semi-structured interviews of the participants and observers of the takeover and merger exercise. It analysis the record of takeovers and mergers that took place in Pakistan during the period from January, 1995 till December, 2017. The data related to takeovers and mergers have been obtained from the data corporation of SECP. All takeovers and mergers involving Pakistani companies during the period

under review have been identified and a subset of deals has been obtained consisting of those takeovers and mergers, in which either the target or the acquirer is a listed company. The research methodology is based on the combination of the following factors which further characterized the research strategy:

**Qualitative research:** The research is based upon the qualitative data of takeovers and mergers which took place in Pakistan during the period starting from January, 1995 unto December, 2017. The approach of the research is oriented towards discovery, descriptive and holistic understanding of the role of independent advisers in takeovers and mergers.

**Case study:** The case study is helpful to analyse the existing corporate laws of Pakistan in comparison with laws of developed countries, particularly the laws governing takeover and merger activity. In Pakistan, there are few numbers of takeovers and mergers but comparatively more cases of privatization and nationalization, wherein customized strategies of the takeover and merger are employed.

In nationalization, the government transforms the private companies into public companies, by bringing them under the public ownership of a national government or state. The privatization is a process to reverse the nationalization. Privatization is a policy impulse which seeks to change the balance amongst the private and that of the public responsibilities in the policies of the government. The cases of privatization and nationalization are not part of this research.

To include in this research a contestant/transaction must meet the criteria: any one company among the companies involved in takeover or merger is listed on PSX, the transaction is not a self-tender offer, the takeover or merger is regulated under the governing laws of Pakistan and investment bank played the role of the independent adviser either for the acquirer or the target company.

All transactions of takeovers and mergers which happened during the period under review were identified; however, none of the transaction satisfies the selection criteria. In all these transactions of takeover and merger, either the law firms or accounting firms had provided consultancy to the target and acquirer companies. There is not even a single transaction where the investment banks have played the role of independent adviser for a complete transaction or any part thereof, either for the acquirer or the target company. Hence, none of the deal qualifies the criteria to participate in this research.

**Interviews:** Interviews provide a way of collecting information and finding facts of the transactions which the researcher cannot directly observe. The interview is not

only an essential technique for data collection in case studies but itself a site for the production of data and can become a focus for enquiry in its own right (Elliott, 2006). Since, the case study is about human affairs, hence, for a better understanding of human affairs shall be reported and interpreted through the eyes of participants. Therefore, the well-informed respondents who can provide essential insights into the process of takeover and merger being direct participants were selected for interviews.

The research is based upon the guided interviews of legislators, regulators, shareholders, directors, corporate advisers (lawyers and accountants), management, investment bankers and all the parties typically involved in the process of takeover and merger activity in Pakistan. The interviews were semi-structured and categorized as informal, conversational interviews. The research consists of a series of meetings that outline a set of issues and questions, crafted accordingly. The researcher had been flexible and responsive to unexpected responses from the interviewers and surprising discoveries during the interviews. Comfort was provided to the interviewees to establish a conversational style, albeit the focus remains on the predetermined subject of adviser's role in corporate takeovers and mergers.

The researcher conducted the interviews of senior officers of SECP, CCP, SBP, members of the judiciary, top lawyers, accountants, bankers, shareholders and the board members of the companies involved in takeovers and mergers. In each category of the interviewees, not less than five people were interviewed to have comprehensive views. Before conducting these interviews, the respondents were informed regarding the context of the research and its purpose and given assurance of ethical principles such as anonymity and confidentiality.

The prime objective of the interviews was to explore views and experience of the direct participants in corporate takeovers and mergers, especially, in the context of the adviser's role in such transactions. The semi-structured interviews had questions that were likely to yield as much information about the role of advisers as possible and address the aims and objectives of the research. Therefore, a different set of questions were asked to each category of interviews. With respect to the takeover and merger laws of Pakistan, the general opinion of the interviewees is that the current laws are not sufficient to ensure good corporate governance and provision of adequate information to the shareholders to make an informed decision about a takeover or merger offer.

The regulators express concerns on the current takeover and merger laws, wherein the director's duties to exercise the due care and act in good faith for its

shareholders while recommending a takeover or merger offer is voluntary. They stated that, since, the takeover and merger laws do not impose an obligation on the board of directors to obtain independent advice to make an informed decision or undertake a due diligence exercise to evaluate the merits of the deal. Hence, it is very challenging for the regulators to hold the board of directors accountable for any promises or recommendation made to the shareholders regarding a takeover or merger deal without exercising the due care. The regulators stated that in the absence of the adequate provisions of takeover and merger laws, they have minimal powers to ensure that the shareholder's interest is safeguarded in takeover or merger transaction by providing them with the required information and expert advice in making an informed decision about the deal.

With respect to the bank's role as an independent adviser in takeovers and mergers in Pakistan, the regulators found their opinion on the findings of the study by Khalid and Hanif (2005) that the SBP has organized its role as a regulator and supervisor, making the central bank relatively more effective. Moreover, the legal and regulatory structure governing the role and functions of banks has been restructured. The banks operating in Pakistan have the potential to play a useful role in takeovers and mergers as a deal adviser due to the expertise and information available to banks. However, in the absence of the provisions of law and custom, the banks are generally not engaged as an independent adviser in large or complexed transactions.

The bankers were of the view that the banks are ready to perform the role of the independent advisers in takeovers and mergers as effectively as the banks of developed countries perform in various corporate deals, including takeovers and mergers. However, they stated that it is challenging for banks in Pakistan to establish their role as a deal maker or independent adviser. Few of the major challenges that the banker's highlight are that the banks ensure compliance with good corporate governance and charge a higher fee as compared to the accounting and legal firms. Besides, in Pakistan as a matter of practice, the shareholders of merging companies negotiate and agree on the critical terms and conditions of the deal first; later they engage advisers to recommend that pre-negotiated deal.

In the absence of legal provisions to govern the role of an independent adviser, the accounting and legal firms can show this leniency as the advisory firms are not as regularised as the banking industry in Pakistan. The supervisory role of the SBP ensures that if the banks are engaged in any takeover and merger transaction as an independent adviser, they must undertake independent due diligence exercise and financial evaluation which discourages the shareholders from appointing the banks as an independent adviser. Hence, the law shall impose a

duty on the board of directors to appoint an adviser before undertaking a takeover or merger exercise, who shall fulfil the criteria of independence, thus, defined by the law.

The general views of the directors who were interviewed in the course of this study are that the current takeover and merger laws of Pakistan provide no or minimal guidance to the directors to perform an effective role in takeovers and mergers. Often the deals are not initiated and negotiated by the board of directors; instead, the boards often endorse the decision already made by the significant shareholders and conduct very limited due diligence to satisfy the minority shareholders. Therefore, the need to engage independent advisers never arises to provide expert and independent advice to evaluate the merits of the deal before recommending it to the shareholder.

One of the prime concerns that the member of judiciary expressed is lack of knowledge and training of the judges to understand corporate transactions and address issues related thereto. The members of the judiciary and the lawyers who were interviewed in this study have a unanimous view that the mandatory requirement to obtain prior approval from the court to undertake a corporate takeover or merger has no utility to the overall process of takeover and merger. The sanctioning powers granted to the courts invariably cause a significant delay in the process of takeovers and mergers without adding value, instead, it adds in the overall cost of the transaction.

Almost all the interviewees shared the views that Pakistan needs to reform its takeover and merger laws to bring them on par with the laws of developing countries. The role of the independent adviser is extremely critical for ensuring that the investors and shareholders are provided with the required information and expert advice to make an informed decision about a takeover or merger deal. Therefore, Pakistan's takeover and merger laws need amendments to impose an obligation to the board of directors to appoint independent advisers to provide independent and expert advice to the shareholders regarding merits of the takeover and merger deal. The law shall also provide the criteria to evaluate the independence of the adviser and guidelines for advisers to perform their role.

The legislators, regulators and the bankers strongly recommend supporting the role of the banks as an independent adviser in takeovers and mergers by the provision of law. They are of the view that in Pakistan, the banking industry is one of the most stringently regulated sectors. The banks, generally, access relevant information of various corporate entities during the course of banking business and the human expertise available to banks enable them to perform an effective role in takeovers and mergers as a deal maker and the adviser.

**Data collection procedures:** The SECP maintains the data of takeovers and mergers of listed companies. For this research, the original data of takeovers and mergers of listed companies during the period under review was obtained from the SECP. The second important source of data collection was interviews of the direct participants of such corporate takeovers and mergers. Those semi-structured interviews enabled the interviewer to understand participant's perceptions, observations and experience.

## RESULTS AND DISCUSSION

**Findings of the research:** This research has examined the role of advisers in takeover and merger transactions in Pakistan, particularly the prospective role of investment banks as independent advisers on takeovers and mergers. Previous researchers have already provided various advantages of employing independent advisers in takeover and merger transactions to provide expert advice (Kale *et al.*, 2003). Various studies have documented the significance of appointing investment banks as independent advisers to a takeover or merger exercise and its impact on increasing the efficiency of the transaction.

The finding suggests that in Pakistan, this area of research is wholly neglected, neither the role of advisers in takeover and merger transactions is ever discussed, generally, nor the bank's role as an independent adviser is discussed particularly. There is no mention of the term 'independent adviser' in Pakistan's corporate laws. In Pakistan, the companies involved in takeover and merger transactions are not bound by law to appoint an independent adviser to assess merits of the transaction independently and provide appropriate and expert advice to the shareholders to make an informed decision.

The investigation suggests that, if Pakistan's corporate laws would be revised to introduce the role of independent adviser, criteria of its independence, scope of work, guidelines for independent advisers, accountability in case of defective advice, minimum content of independent adviser's report etc., it will provide better protection to the shareholders and thus, encourage takeover and merger activity in Pakistan. When the role of advisers is appropriately regulated, it can safeguard the interest of the shareholders effectively by providing them with an insight into the deal and offering them expert advice about merits and demerits of the transaction.

The banks enjoy ultimate trust in any economy globally. Likewise, the banking industry of Pakistan is the most reputable in the country. In Pakistan, the SBP has taken all possible measures to ensure that the trust which creditors and public reposed on financial institutions shall be honored in any circumstances. SBP has a reputation of

being one of the most stringent regulators. This research indicates that the credibility and availability of the experienced human resource, enables the investment banks to perform a better role as an independent adviser in takeover and merger transactions to find best deals, plan it comprehensively and execute it efficiently.

This research offers an exciting insight into the incentives of encouraging the investment bank's role in takeover and merger transactions. The findings of this research are essential steps toward understanding the critical and effective role that the investment banks can play in Pakistan as independent advisers in takeovers and mergers to increase the efficiency of the transaction and encourage the activity of takeover and merger in the market. The role of investment banks as independent advisers will enhance the confidence of foreign investors to plan strategic takeover and merger in Pakistan to benefit from this prospective market.

The majority population of Pakistan is Muslim and naturally very cautious about the *Shariah*-compliant business. Consolidating business through takeover and merger is often not appreciated by those investors who are concerned about a *Shariah*-compliant aspect of any business. Generally, the companies do not have the in-house expertise to ascertain the validity of the target's business, develop a *Shariah*-compliant transaction structure and select an Islamic mode of financing to finance the transaction. Islamic banks in Pakistan can address all these concerns of investors methodically as they have the scholarly expertise on their board as well as in their *Shariah* departments.

## CONCLUSION

This research has attempted to explain, among others, the fundamental importance of having an independent adviser and the role played by an investment bank in takeover and merger exercise. The purpose of this research was to analyze Pakistan's corporate laws that govern takeover and merger activity in the country, to suggest amendments in Pakistan's takeover and merger laws to introduce the role of the independent adviser in takeovers and mergers to bring them at par with laws of developed economies and to suggest the benefits of promoting the banks role as one of the most suitable independent advisers in takeovers and mergers.

## LIMITATIONS

The research, however, has some limitations. The study is limited to the takeover and merger transactions that have taken place in Pakistan, defining its geographical boundaries. The discussion is further limited to the companies whose shares are listed on the Pakistan

stock exchange, reducing the data substantially. The data is further summarized because this research includes takeover and merger transactions that took place in Pakistan during 22 year's time span, starting from January, 1995 till December, 31, 2017.

One of the significant limitations of the research is partial access to the relevant data as the private and confidential policy of companies was a barrier to get complete and accurate information. There is no database maintained at an institutional level such the SECP, PSX and CCP. The individuals who have played vital roles in the takeover and merger exercise such as the stakeholders of acquirer and target companies, legal and financial advisers and officers of regulatory authorities having firsthand information related to the transactions were interviewed during this research.

### **RECOMMENDATIONS**

Takeovers and mergers are strategies persuasive to change the competitive structure of a market radically. In Pakistan, the takeover and merger activity is still in its primitive stage, due to various regulatory and transactional constraints. However, the market has great potential for growth through takeovers and mergers. This research recommends that to utilize the potential of the market entirely, the legislators and regulators must reform the takeover and merger laws of Pakistan to bring them on par with the laws of developed economies.

In Pakistan, the corporate laws governing takeovers and mergers need reform to include the role of an independent adviser to provide independent advice to the shareholders of the companies involved in takeovers and mergers to enable them to make a well-informed decision as to the merits of the offer. Pakistan needs a balanced takeover and merger laws to instil confidence in the legal and regulatory system of the country which governs corporate takeovers and mergers.

The fundamental reforms are required in Pakistan's takeover and merger laws to bind the board of directors of the companies involved in takeovers and mergers to appoint independent advisers to conduct due diligence of the counter party and provide a report to the board of directors and shareholders to make an informed decision as to the merits of the transaction.

The takeover and merger laws shall provide the eligibility and independence criteria which shall be compliant by the advisers to act as the independent advisers and it may be linked with a licence. The proposed criteria of the adviser's independence may include that with respect to a takeover or merger, an adviser shall not be regarded independent unless it manifest and confirm: not to have a current or potential conflict of interest which may include the cross-shareholding and directorship, its adherence to the fundamental value of transparency by disclosing its earlier and existing relationship with the

parties along with their critical terms, e.g., fee, not to have any financial interest in the outcome of the transaction such as success fee, not to finance the entire transaction or any part thereto, not to be a substantial creditor of the transaction, not to be the strategic adviser of the parties thereto and not to be in possession of the confidential information of any party involved in the transaction. The data of the independent advisers shall be prepared and maintained by the SECP.

The law shall provide comprehensive guidelines to the advisers to perform their duties with good faith and due care, to ensure that the transaction shall achieve its desired objectives. Provisions of law shall be there to ensure that the independent advisers shall be held accountable for defective advice and negligence while advising the companies on a takeover or merger offer. For a balanced approach, the law shall also offer certain provisions of defense to the independent advisers against any claim made by the shareholders or indirect liability if they discharge their duties with due care and good faith. The law should dictate the minimum content of a takeover offer, aspects and scope of the independent report/advice circular and minimum contents of adviser's report. The provisions of law shall bind the independent adviser to evaluate soundness, fairness and reasonableness of the terms of any takeover and merger transaction and provide independent expert advice on merits of the offer, enabling the shareholders to make an informed decision.

A proper process of due diligence is vital for the accurate evaluation of the target company for seizing synergy through acquisition. The due diligence exercise is neither mandatory in Pakistan by law nor a common commercial practice. The companies while undertaking a takeover and merger, appoint accounting firms to conduct due diligence if the transaction is complex or extensive and legal firms to assist in transactional documents for translating the shareholders understanding in writing. However, this due diligence is generally limited to the investigation of financial figures only. The takeovers and mergers are albeit driven by the strategic intent instead of financial logic. The exercise of due diligence should not be limited to accounting; instead it shall include the realistic assumption regarding proposed synergies between the merging companies.

Pakistan's takeover and merger laws need reforms to impose an obligation on the companies to undertake due diligence exercise by the independent advisers before entering into a takeover and merger transaction. The provision of laws shall also specify the scope of the due diligence exercise, duties of the independent advisers to undertake the due diligence exercise with due care and minimum content of the due diligence report. The complete regulatory process of acquiring control of corporate entities needs to be made more accessible, centralized and investor-friendly, unlike the current

complex and time-consuming process which is a significant demotivation for the companies that are pursuing the strategy of a takeover or merger for external growth.

Amendments are required in Pakistan's corporate laws to bring them at par with laws of developed countries to enable Pakistan to compete regionally and internationally. This research proposes that Pakistan's corporate laws need to be revamped to include provisions to ensure that the shareholders are given sufficient information and expert advice enabling them to reach an informed decision about any takeover or merger deal. No relevant information should be withheld from shareholders and the information so provided shall be accurate, complete and shall not be misleading.

The directors shall be duty-bound by law to must act only in the best interest of the shareholders and shall disclose if they have any conflict of interest in the takeover and merger transaction or any part thereto. The board of directors shall be obliged to provide their comments on reasonableness and fairness of the offer, along with its reason for forming its opinion and recommendation to the shareholders.

As discussed earlier, many researchers have proved that the reputation of an adviser has a significant effect on the efficiency and outcome of the transaction. The banks enjoy the status of credible institutions worldwide and have high relatedness to the process of acquisition. In the context of takeover and merger activity in Pakistan, the investment banks can play a critical role in structuring and facilitating the transactions related to the acquisition of control over corporate entities. The expertise that is available to banks in Pakistan qualify them to handle all primary functions associated with enterprising a takeover and merger including identifying the target, conducting due diligence, preparing transactional documents, evaluating the worth of the companies to assess the fair value of the transaction and planning integration.

Islamic banks in Pakistan have a *Shariah* supervisory board and the resident *Shariah* adviser to ensure governance of Islamic banks. SBP provides guidelines about eligibility criteria and monitors their contribution as well. The knowledge and expertise of *Shariah* scholars enable them to offer expert advice with regards to the transactions to acquire control over corporate entities through *Shariah*-compliant takeovers and mergers. The decision to engage any Islamic bank as an independent adviser in takeovers and mergers to ensure that the transaction is entirely *Shariah*-compliant will extend comfort to Islamic shareholders and investors. Alliance of *Shariah* advisers with banking experts will give the investor confidence that not only their interest is safeguarded but the transaction serves to achieve the *Maqasid al-Shariah*

There are logical arguments to suggest that if provisions of law would support the role of investment banks as an independent adviser in takeovers and mergers, it will provide greater confidence to the shareholders by offering them one-window service, expert advice and relevant informed to enable them to make an informed decision as to the merits of the takeover or merger offer. As a result, the takeover and merger activity will increase in Pakistan, especially, the strategic takeovers and mergers which is extremely crucial for the country's economic growth.

**Further research:** This study is theoretical which triggers the call for further research to complement this pioneering work on investment bank's role as an adviser in takeovers and mergers in the context of Pakistan. To explore the subject further and to support the findings of this study, empirical studies are useful. Further research can be done on legislative and regulatory reforms required to encourage takeover and merger activity in Pakistan.

This research provides a foundation to conduct further research on several supplementary subjects such as the role of legal and accounting firms as advisers in takeovers and mergers in Pakistan, competence and readiness of Pakistani investment banks to provide advisory services in takeovers and mergers, benefits to have one-window takeover and merger operation, effect of Pakistan's decentralized sanctioning authorities to increase complexity of the takeover and merger process, duties of board of directors in corporate takeovers and mergers, etc. An extremely critical subject to investigate in future is the relevance of court's powers to sanction a takeover and merger transaction, especially when it is a technical matter and only people of specific expertise can evaluate merits and demerits of the transaction.

The ministry of finance, with the collaboration of investment banking personals, business schools, management consultants and the experts of takeovers and mergers shall sponsor comprehensive research on independent adviser's role in takeovers and mergers, precisely the investment bank's role as independent advisers. The research should specify the legislative and regulatory reforms that are required to bring Pakistan's corporate laws on par with the laws of developed countries. The Research shall recommend specific provisions to be included in the law to introduce the role of advisers to assist the stakeholders in all critical decisions including takeovers and mergers.

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