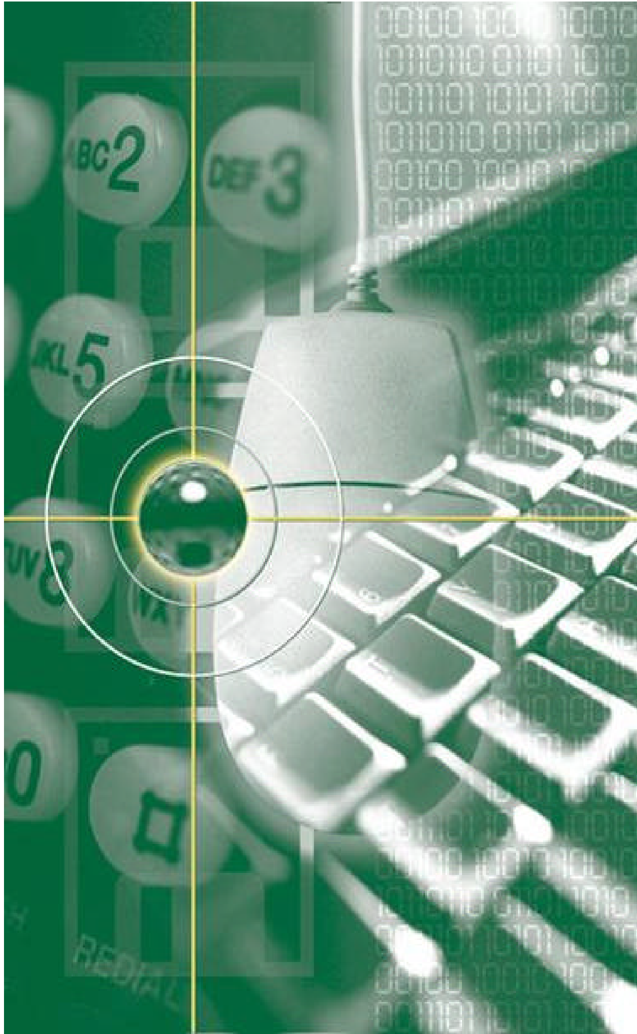

M&A LAB

HCL – Axon Deal Dissected

Dissected by – Team M&A

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December 19, 2008

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PROLOGUE

The website of HCL Technologies Limited was promptly changed to proudly mention "***I am HCL Axon***" on December 15, 2008, immediately after the High Court of Justice in England and Wales ("**High Court**") confirmed the approval of the 'scheme of arrangement' (the '**Scheme**") for the acquisition of the Surrey (UK) based Axon Group plc in an all cash deal worth GBP 441 million to be paid to its shareholders by HCL Technologies' UK based indirect wholly owned subsidiary, HCL EAS Limited.

This M&A Lab dissects the commercial, legal, tax and regulatory aspects of this historic acquisition which clearly is – the largest acquisition in the tech space ever by any Indian company overseas.

Parties Involved

*HCL Technologies Limited ("**HCL**")*: 5th largest Indian global IT services company and listed on the Bombay Stock Exchange; HCL, along with its subsidiaries, had consolidated revenues of USD 2 billion as on 30th September 2008[1].

*HCL Bermuda Limited ("**HCL Bermuda**")*: A private company wholly owned by HCL. HCL Bermuda acted as the acquisition vehicle of HCL for overseas acquisitions in the past. We understand that *Control Point Solution, Inc.* (USA) and *Liberata Financial Services Limited (LFS),* (UK) were acquired by HCL Bermuda.[2]

*HCL EAS Limited ("**HCL EAS**")*: A private company wholly owned by HCL Bermuda, HCL EAS was incorporated in the United Kingdom for the sole purpose of acquisition of Axon Group plc.

*Axon Group plc ("**Axon**")*: Listed on the prestigious London Stock Exchange, Axon is one of the leading players in the enterprise application services ("**EAS**") segment. Axon caters to needs of organizations that have chosen System Application Products ("**SAP**") as their strategic enterprise platform. Axon has offices across Europe, Americas and the Asia Pacific.

*Standard Chartered Bank, UK ("**SCB**")*: SCB has agreed to advance a loan of GBP 400 million to HCL EAS for acquisition of Axon.

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[1] Source: Website of HCL (www.hcltech.com) and HCL (www.hcl.in)
[2] Source: Disclosure made on the website of Bombay Stock Exchange (www.bseindia.com)

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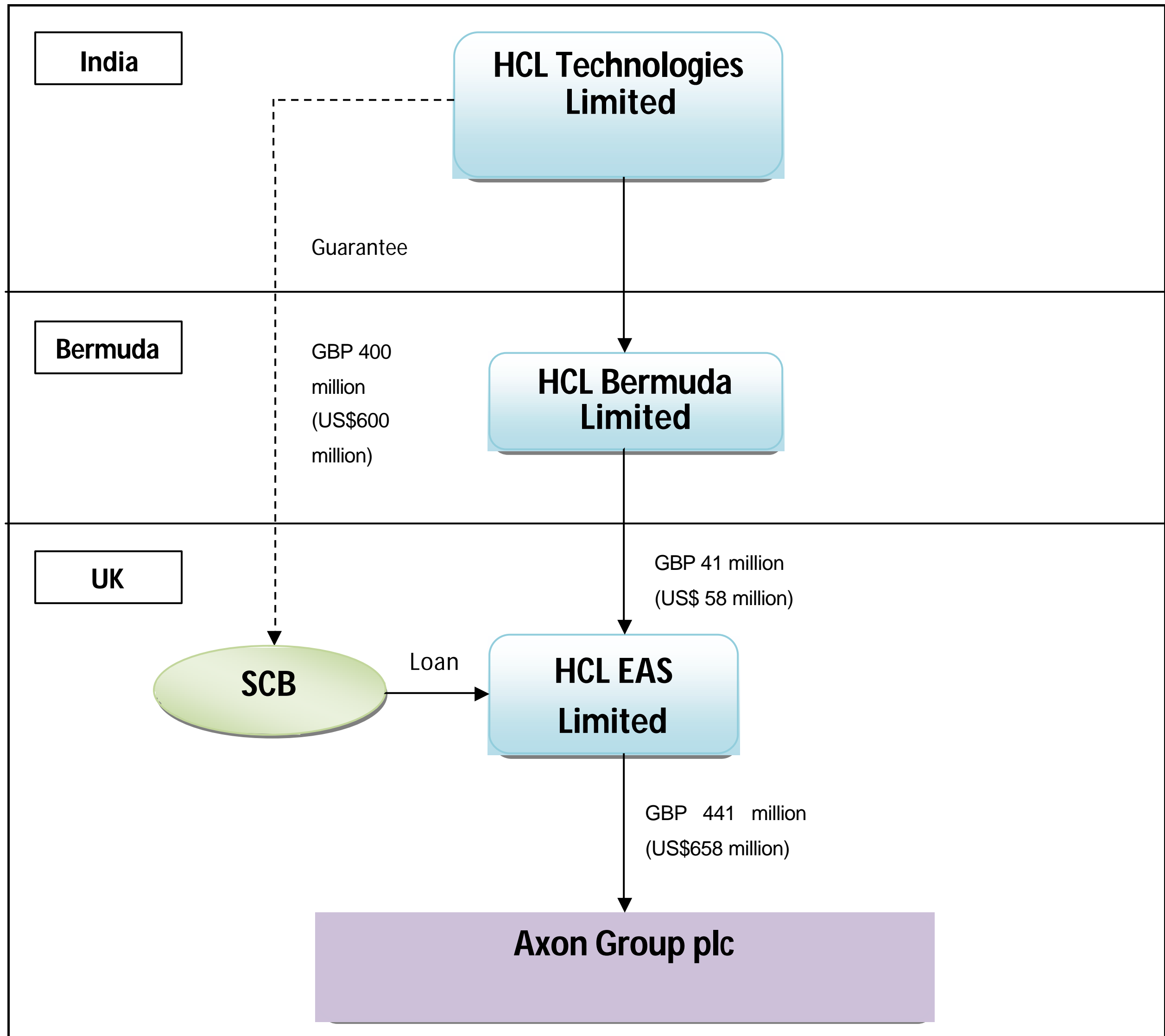
The diagrammatic representation of the HCL's acquisition of Axon is as follows:



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Chronology of key events

The chronology of key events is summarized as follows:

Date	Events
January 2008	HCL initiates negotiations for acquisition of Axon.
August 25, 2008	Formal bid made by Infosys for acquisition of Axon for GBP 407.1 million (600 pence per share). Implementation agreement concluded and board of directors of Axon ("**Board**") recommends the offer to the shareholders of Axon.
September 20, 2008	Publication of the Scheme document for proposed acquisition by Infosys.
September 26, 2008	HCL announces a formal bid to acquire Axon for GBP 441.4 million.
September 29, 2008	60 hours mandatory reaction window for Infosys to make counter bid lapses and Infosys does not revise its offer.
October 2, 2008	Board decides to withdraw recommendation for Infosys bid and extend fresh recommendation to HCL.
October 8, 2008	HCL EAS purchases 301,623 Axon shares, which represent 0.47% of the paid up share capital of Axon, through open market.
October 10, 2008	Infosys officially withdraws its bid and HCL decides to implement the offer by way of a Scheme.
October 12, 2008	HCL EAS purchases 6.71 million shares, which represent 10.43% of Axon's paid up share capital, through open market.
October 24, 2008	Publication of the Scheme document for proposed acquisition by HCL EAS.
November 24, 2008	Axon shareholders approve HCL's bid by voting in court meeting approving the Scheme and in the extraordinary general meeting (99.9% votes).
December 10, 2008	Hearing by the High Court for sanctioning the Scheme.
December 15, 2008	High Court approval obtained and HCL announces the successful closing of the acquisition of Axon.
December 29, 2008	By this date, Axon shareholders should receive the full consideration.

THE COMMERCIAL FRAMEWORK

Who made the first offer – HCL or Infosys Technologies Limited?

It all began, way back in 2005 when HCL identified EAS as a focus area for its business expansion and targeted Axon, one of the key global players in the EAS spectrum, as its strategic business alliance partner in the global arena.

Apparently, Axon remained top priority for HCL ever since, and HCL even made an offer for acquisition of Axon earlier this year when the share value of Axon was pegged at a whopping 900 pence per share as against the 650 pence per share at which HCL finally acquired Axon. However, for reasons best known to the parties, the negotiations for acquisition of Axon never culminated.

Subsequently, the markets fell and the financial slowdown severely affected the valuation of Axon. It was at this time that Infosys Technologies Limited ("**Infosys**") made an offer to acquire Axon at a price of 600 pence per share payable to Axon shareholders.

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HCL promptly made a higher counter offer of 650 pence per share which outbid Infosys and laid foundations of the current HCL Axon[3].

Is Axon that special?

The cutthroat competition in the relevant market reveals the actual worth of EAS for software companies and probably the reason behind the keenness of both Infosys and HCL to acquire Axon.

Axon being a midsize pure play SAP service provider with enviable track record of reported growth at the rate of 35% CAGR (Compound Annual Growth Rate) in the past 5 years, an operating margin of 16% (commendable for a consultancy firm) and a reported PBT of GBP 29.5 million with revenues of GBP 204.5 million for the year ended December 2007 undoubtedly made it an enviable target, particularly in light of the rapidly growing demand for EAS.

Is the acquisition a prudent investment for HCL?

If acquisition of Axon was a strategic business move for Infosys, it was nothing short of a lifeline for HCL. EAS was always a focus area for HCL where it had to necessarily gain expertise to stand against the proficiency of its competitors in the market in the light of the fact that HCL draws only 11% (USD 200 million) of its revenues from EAS which is far lesser than 30-35% (USD 1 billion) of Infosys.

If HCL had to make positive strides of development, it was inevitable for it to expand its EAS spectrum for which the best possible way was to inorganically grow through acquisition of Axon. Under these circumstances, it would have been fatal for HCL's business ambitions and a grave business failure for HCL, to let Infosys acquire Axon.

Well aware of the commercial consequences of Axon falling into the hands of Infosys, HCL was well prepared to make a higher counter bid for Axon if Infosys had made any counter offer. Reports suggest that HCL would not have hesitated to cross all barriers for acquiring Axon.

Newspaper reports suggest that the strategy adopted by HCL to stand up against a much bigger and wealthier Infosys was flawless, particularly in light of the fact that HCL availed of a loan of GBP 400 million from SCB[4] for acquisition while keeping its free reserves (of INR 8033 crores)[5] intact. As against this, Infosys was banking exclusively on its free reserves (of INR 14,491 crores)[6] for the acquisition. Therefore, while having smaller cash reserve comparatively, HCL had tried its best to equip itself to make higher counter bids if Infosys did make a counter bid. Interestingly, HCL exhibited splendid foresight by purchasing 10.90% Axon shares (in two tranches of 0.47% and 10.43%) from the open market during the offer period sending a very strong message of its intention to acquire Axon across the market and to deter any other company from eyeing any interest in Axon. It was made explicit that the company under no circumstance will regress from its decision to acquire Axon.

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[3] 'HCL AXON' is the new entity post successful acquisition of Axon by HCL.

[4] HCL leveraged itself to fund the acquisition of Axon by availing of a loan of GBP 400 million from SCB at USD LIBOR rate of 6.5% interest. HCL EAS has entered into a senior facility agreement with SCB as being the original lender, HCL EAS as original borrower, HCL as original guarantor and HCL Bermuda as parent. Under the terms of the senior facility agreement, neither the payment of interest nor the repayment nor any liability for HCL EAS will depend on the business of Axon. (Source: Scheme document).

[5] Source: http://www.businessworld.in/index.php/Information-Technology/Race-To-The-Finish.html

[6] Id

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Axon and HCL are likely to make a cohesive blend on account of at least the following factors:

- Vision and the policies of both complement each other.
- Minimal overlap of customers, service territories and business.
- Client base of Axon in UK will efficiently complement HCL's strong client base in USA.
- Axon has strong customer base in the UK public sectors and defensive sectors like utilities, oil & gas, chemicals, etc whereas HCL has no such customer base.
- While more than 60% of HCL's revenue comes from application management, Axon draws 88% of its revenues from business consulting, and implementation services effectively reducing business overlap to bare minimum.
- HCL can leverage upon its time tested business global relation with SAP inasmuch as HCL's strong SAP presence in the US and Asia will definitely complement Axon's excellent SAP position in the UK.

Newspaper reports suggest that the market has a lot of hopes pinned on this new combination of the two leading global SAP players as offshore SAP market space is USD 7.5 billion whereas the share of Indian players is just about USD 1.5 billion. HCL Axon, therefore, aims at exploiting the tremendous scope available here. Post acquisition, HCL Axon will catapult HCL straight into top 10 SAP service providers in the world from nowhere, with 4,500 consultants and estimated revenues of about USD 500-600 million[7].

<u>Why did Infosys not make a counter bid?</u>

We understand that pursuant to the counter offer made by HCL on September 26 2008, Infosys had 60 hours to react to the offer during which Axon was prohibited from revoking or amending the agreements already concluded with Infosys. Infosys, however, chose not to make a counter offer and let the reaction window expire.

> **Reaction Window:** *As a practice in UK, we understand that the target company and offeror usually incorporate a clause in the implementation agreement, subjecting itself to provide the offeror a window of 60 hours to react to any counter offer. The offeror, upon notification of such counter offer by the target company may or may not revise its offer. Such period of 60 hours is referred to as the "Reaction Window". During this Reaction Window, the board of the target company may be prohibited from revoking, amending or varying any agreement or undertaking it has already concluded. After the Reaction Window lapses, the option lies with the board of the target company to choose between the offer or the counter offer, as the case may be.*

While the reasons for not making a counter-bid are not known, there are views that Infosys refrained from revising its bid to higher than HCL's bid of 650 pence per share primarily because Axon merely enhanced its already existing EAS capability, which was not as critical for Infosys.

<u>Was Axon bound to accept Infosys' offer?</u>

It is believed that Infosys had obtained irrevocable commitments from the directors of Axon to accept the Infosys scheme and vote in its favour in the High Court meeting (as defined below) and general meeting. Though these commitments were irrevocable for Axon, they were terminated when the Infosys offer was withdrawn. Subsequently, fresh irrevocable commitments of the same nature were extended by the directors of Axon to HCL. It is mandatory to consult the Takoever Panel before irrevocable commitments are obtained, and once obtained a public announcement of the same is mandatory.

[7] Source: Public announcement made by the CEO of HCL – Mr. Vineet Nayar.

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***Irrevocable commitments**: Irrevocable commitments are defined under the Code to include commitments (a) to accept or not to accept or to procure that any other person accept or not accept an offer; or (b) to vote or to procure that any other person vote in favour of or against a resolution of an offeror or the target company or of its shareholders in the context of an offer, including a resolution to approve or to give effect to a scheme of arrangement. An irrevocable commitment is one of the criteria for determining whether a person is "acting in concert" for the purposes of the Code.*

LEGAL AND REGULATORY PERSPECTIVE

I. UK LAW IMPLICATIONS

UK City Code on Takeovers & Mergers ("Code")

What is the Code?

The Code is essentially a set of general principles and rules governing the conduct of takeovers and mergers of companies based in UK, the Channel Islands and the Isle of Man.

Unlike the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 ("**Indian Takeover Code**") which was designed to protect the interests of the incumbent promoters and public shareholders against hostile raiders, the principal intention of the Code is to ensure that shareholders are treated fairly and accordingly provides an orderly framework within which takeovers ought to be conducted. Takeovers guided by the Code are administered by the Takeover Panel in the UK, which is equivalent to the Securities and Exchange Board of India.

What were the ways available to HCL EAS for acquiring Axon?

The intention of HCL EAS was to acquire the entire share capital of Axon and make it a wholly owned subsidiary. Under the Code, HCL EAS could either acquire all the shares through a tender offer (contractual purchase) or under a court approved scheme of arrangement.

Tender offer route: Tender offer route essentially refers to the process whereby an offeror makes an offer to the shareholders of the target company without the intervention of the court. If HCL EAS had opted for the tender offer route, it would have been read to make an offer to all shareholders of Axon to purchase their shares at the fixed price of 650 pence per share, thereby establishing a contractual relationship between HCL EAS and Axon Shareholders.

*Interestingly, the Code requires any offeror intending to acquire control over a UK company to make an offer to board of directors of the target company ("**Board**"), which would in turn recommend or reject the offer based on independent financial advice sought by the Board in this regard. If the Board does not recommend such an offer to the shareholders, the offer is regarded as a 'hostile bid'. Unlike the Code, the Indian Takeover Code does not require an acquirer to approach the Board for making an acquisition, and the acquirer is free to directly deal with the shareholders. Further, unlike the Indian Takeover Code, which mandates a public offer of only 20% additional shares, the Code requires an offeror (read acquirer) to acquire all the remaining shares of the target company, if at any time his voting rights in the company aggregate to 30% or more.*

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Scheme of Arrangement: Scheme of arrangement is a statutory procedure under Part 26 of the (UK) Companies Act, 2006 ("**Act of 2006**"), which provides a company to propose an arrangement to its shareholders or creditors (or any class of them). A Scheme can be used for any transaction wherein a company wants to ensure that all the shareholders are bound by the arrangement proposed by the company. There is no contractual relationship between the acquirer and the shareholders in such a case.

If HCL EAS opted for the Scheme, then under the provisions of Section 899 of the Act of 2006, HCL EAS would not only have had to procure consent of more than 75% shareholders in favour of the Scheme, but also approval of the High Court confirming the Scheme. The Scheme would then become binding on all creditors and shareholders of Axon, irrespective of whether they voted against or for the Scheme.

Under the Code, schemes can be of two types – transfer scheme and cancellation scheme. While, in case of a transfer scheme, the existing shares are transferred to the acquirer, in case of a cancellation scheme, the existing shares are cancelled and fresh shares are issued to the acquirer. Needless to say, both these schemes require prior approval of the High Court.

Why did HCL prefer to opt for the Scheme of Arrangement?

HCL EAS preference for the Scheme is homogenous to the recent acquisition trend in the UK in the past few years. HCL EAS preferred the cancellation Scheme route as against the tender offer route on at least the following two counts:

(a) *Isolated Shareholders*: Scheme reduces the burden of procuring shares from each shareholder; and

(b) Stamp duty: In case of a cancellation Scheme, as opted by HCL EAS in this case, there is no stamp duty or stamp duty reserve tax payable.

One reason why companies do not opt for scheme of arrangement for mergers and acquisitions in India appears to be the heavy stamp duty that is payable on the court order which confirms such a scheme. Debates on whether a court order can be an "instrument" stampable under the relevant state acts has now been settled in light of recent case laws, and court order is now required to be stamped.

Why didn't HCL EAS then opt for the Scheme in the first place?

We understand that the Takeover Panel does not permit an offeror to make an offer for acquisition of the target by means of a Scheme if another offer to be implemented by means of a Scheme is already in place.[8]

Therefore, since HCL EAS made its counter offer of 650 pence per share when Infosys' offer to acquire Axon by means of a Scheme was still in force, HCL EAS was not permitted to make the offer by means of a Scheme and accordingly compelled to make its offer by way of a tender offer.

[8] "*The Takeover Panel acknowledged this as the only example of a scheme having been proposed in competition with an existing scheme, where the acquisition of Corus by CSN, to be implemented by means of a scheme, was pre-conditional on the withdrawal of Tata Steel's offer for Corus, which was also to be implemented by means of a scheme."* – The Scheme by Malcolm Lombers and Mark Bardell of Herbert Smith LLP, March 2008, PLC Magazine.

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So, while HCL EAS made the offer under the tender offer route for acquisition of Axon, there was probably an inclination to switch to the Scheme for the advantages mentioned above. Naturally therefore, HCL EAS made the switch to the Scheme as soon as Infosys withdrew its offer to acquire Axon.

The Scheme - What was the procedure followed by HCL EAS to acquire Axon?

HCL EAS took the following steps[9] for the acquisition of Axon under the Scheme:

(a) *Announcement*: HCL EAS made an announcement of its intention to acquire Axon as required under Rule 2.5 of the Code[10];

(b) Application *to the High Court*[11]: Axon initiated proceedings for the Scheme filing a claim form (application) to the High Court;

(c) *First hearing of the claim form*: On October 23, 2008, the High Court on the application of Axon ordered a court meeting of Axon shareholders to consider and approve the Scheme ("**Court Meeting**"). The Court Meeting was scheduled for November 24, 2008 at 10 AM;

(d) *Scheme document*: On October 24, 2008, the Scheme document was published and circulated to Axon shareholders. The Scheme document stipulates conditions that have to be complied with by the shareholders for confirmation of the Scheme, which *inter alia* includes conditions stipulated by the High Court and the Code.

(e) *Approval of Scheme by shareholders*: In the Court Meeting to ascertain shareholder willingness to the Scheme, the Scheme was approved by 99.9%[12] shareholders and notice of such majority was then submitted to the High Court. A shareholders meeting was convened immediately after the conclusion of the Court Meeting to pass the resolution for capital reduction to give effect to the Scheme[13]. 99.9% shareholders voted in favour of the resolution. Thereafter, Axon made a public announcement of the minutes of the Court Meeting including the voting results. These events took place on November 24, 2008.

(f) *Court approval*: Pursuant to the approval of the Scheme by the shareholders, the Scheme was then approved by the High Court on December 15, 2008 thereby making it effective and binding on all the shareholders and the creditors of Axon. Axon was then required to make a public announcement of the outcome of the High Court hearing. Subject to the payment of the consideration, Axon became a wholly owned subsidiary of HCL EAS.

(g) *Consideration*: HCL EAS will now be required to pay the Axon shareholders the consideration of 650 pence per share within a period of 14 days from the date the Scheme becomes effective.

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[9] Supra No. 8

[10] An offeror should only announce a firm intention to make an offer after the most careful and responsible consideration. Such an announcement should be made only when an offeror has every reason to believe that it can and will continue to be able to implement the offer. Responsibility in this connection also rests on the financial adviser to the offeror.

[11] Section 896 of the Act of 2006.

[12] At least 75% of majority is required for the High Court to approve the Scheme of arrangement as per Section 899 of the Act of 2006.

[13] Section 135 of the Companies Act, 1985

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Did Axon pay an 'inducement fee' to Infosys?

It is understood that the implementation agreement concluded by Infosys and Axon had an inducement fee ("**Fee**") clause which obligated Axon to pay 1% offer price to Infosys as Fee if the board of directors of Axon recommended a counter offer. When Axon revoked its recommendation for Infosys and recommended the offer of HCL, Axon was obligated to pay 1% Fee to Infosys.

> ***Inducement Fee**: Inducement fee is a contractual arrangement prevalent in the UK where the target company may agree to pay certain stipulated percentage of the offer price offered by the outbid offeror, when the board of the target company recommends another offer to its shareholders. Rule 21.2[14] of the Code provides statutory sanctity for such an arrangement which the parties may incorporate in their implementation agreements. Without prescribing any quantum, the Code suggests that the Fee should be de minimis which is normally 1% of the offer price offered by the outbid offeror. The Fee is paid to compensate the outbid offeror for galvanizing a higher bid, which is advantageous to the shareholders of the target company. Such provision for Fee has not been carved out in the Indian Takeover Code.*

II. INDIAN LAW IMPLICATIONS

ODI Regulations

Any Indian company that wishes to acquire or invest in a foreign company outside India must comply with the Foreign Exchange Management (Transfer or Issue of any Foreign Security) Regulations, 2004 ("**ODI Regulations**").

Under the ODI Regulations, an Indian company is permitted to invest in a joint venture or a wholly owned subsidiary upto 400%[15] of the net worth of the Indian company, in the form of equity, loan or guarantee, as on the date of the last audited balance sheet without seeking the prior approval of the Reserve Bank of India ("**RBI**") *inter alia* if the Indian company:

a) is not on the RBI's caution list or under investigation by the Enforcement Directorate;
b) routes all the transactions relating to the investment in the joint venture or the wholly owned subsidiary through only one branch of an authorized dealer; and
c) files the prescribed forms with the RBI.

Regulation 13 of the ODI Regulations permits a wholly owned subsidiary set up by an Indian company to set up a step down subsidiary. Extant ODI Regulations are ambiguous on whether setting up further down line subsidiaries will require prior approval of the RBI.

[14] *"In all cases where an inducement fee is proposed, certain safeguards must be observed. In particular, an inducement fee must be de minimis (normally no more than 1% of the value of the offeree company calculated by reference to the offer price) and the offeree company board and its financial adviser must confirm to the Panel in writing that, inter alia, they each believe the fee to be in the best interests of shareholders. Any inducement fee arrangement must be fully disclosed in the announcement made under Rule 2.5 and in the offer document. Relevant documents must be put on display in accordance with Rule 26. The Panel should be consulted at the earliest opportunity in all cases where an inducement fee or any similar arrangement is proposed."* - Rule 21.2 of the Code.

[15] This ceiling is not applicable where the investment is funded out of balances held by the Indian party in its Exchange Earners' Foreign Currency (EEFC) account.

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<u>*Whether the acquisition was permitted under the ODI Regulations?*</u>

In the current structure, HCL was permitted to setup HCL Bermuda, a wholly owned subsidiary of HCL, which could permissibly setup a step down subsidiary HCL EAS. Creation of a further down line subsidiary by HCL EAS, as mentioned above, may require prior approval of the RBI in terms of the ambiguity in the ODI Regulations.

The question therefore is whether HCL sought permission of the RBI prior to acquisition of Axon by HCL EAS as Axon now became a wholly owned subsidiary of HCL EAS. (*Please refer to the structure mentioned earlier*)

There is a debate on whether an Indian company can set up wholly owned subsidiaries beyond two step down subsidiaries since Regulation 13 can be interpreted to cover multiple layers of step down subsidiaries. While the RBI's approach on such ambiguity is unclear, we understand based on the earlier precedents that RBI has recently been liberal and has permitted to allow Indian entities from setting up multiple layers of step down wholly owned subsidiaries.

<u>***FEMA Guarantees Regulations***</u>

For the loan facility obtained by HCL EAS from SCB for GBP 400 million, HCL has acted as the original guarantor. Under the Foreign Exchange Management (Guarantees) Regulations, 2000 ("**Guarantees Regulations**"), an Indian parent company is permitted to guarantee the obligations of its subsidiary if it is in connection with the subsidiaries' business, if this guarantee is in compliance with the ODI Regulations.

Accordingly, on account of the ambiguity in the ODI Regulations, there is a possibility that the guarantee provided by HCL to SCB on behalf of HCL EAS, which is an indirect wholly owned subsidiary of HCL may require prior approval of the RBI.

<u>***Anti Trust Laws***</u>

The Indian anti-trust laws are contained in the Monopolies and Restrictive Trade Practices Act, 1969 ("**MRTP Act**") which shall, in due course, be replaced by the Indian Competition Act, 2002 ("**Competition Act**"). Though the MRTP Act and the new Competition Act are concurrently in force; currently, the substantive provisions of the Competition Act relating to anti-competitive agreements, abuse of dominance and regulation of combinations have not yet been notified.

<u>*If substantive provisions of the Competition Act are notified, would it have a bearing on the current acquisition?*</u>

In terms of the Competition Act, parties to the proposed combination must determine whether the proposed transaction triggers the applicable threshold limits viz with respect to the size of the parties or the turnover as prescribed under Section 5 (c) of the Competition Act. Given the magnitude of the assets and/or turnover of the parties involved, it may have triggered the threshold limits, thereby, mandating HCL and Axon to notify to the Competition Commission of India ("**CCI**") providing the details of the proposed acquisition. Once such notification has been made to CCI, CCI shall do its due investigation on the basis of the criterion laid down under the Competition Act (*inter alia* level of combination of the market, market shares) to determine whether the acquisition causes or is likely to cause an adverse appreciable effect on competition within the relevant market in India and the CCI shall give its ruling within a maximum period of 210 days. Further, the Competition Act provides for extra territorial jurisdiction of the CCI to probe into an overseas acquisition if it causes or is likely to cause an adverse effect on competition in relevant market in India.

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TAX PERSPECTIVE

Why was the acquisition routed through Bermuda?

Bermuda, with its efficient tax regime coupled with an investor friendly business environment, has emerged as one of the preferred offshore jurisdictions in the world. It does not levy any income tax, capital gains tax, dividends tax, wealth tax, or inheritance tax.[16] Therefore any dividends paid by HCL EAS to HCL Bermuda or capital gains that accrue from the sale of shares of HCL EAS would not be taxable in Bermuda. Such dividends would also not be subject to any withholding tax in the UK. Further, capital gains derived by a non-resident company from assets situated in the UK are generally not taxable in the UK unless they are attributable to a permanent establishment in the UK.

It should be noted that Bermuda has not entered into any double taxation avoidance (DTAA) treaty with India or UK. Therefore dividends distributed by HCL Bermuda to HCL would be taxable in India at the rate of 33.99%[17] as per the provisions of the Income Tax Act, 1961.

In view of this, it would seem that the dominant intention in routing the acquisition through Bermuda is to park funds in Bermuda and use it for future overseas acquisitions probably within the European Union and the US.[18] We understand that HCL has used HCL Bermuda for overseas acquisitions in the past.

Why was HCL EAS incorporated in UK for the acquisition of Axon?

Overseas acquisitions of HCL in the past were routed through HCL Bermuda without incorporation of any new company for acquisition. Hence the implication of incorporation of HCL EAS in UK is worth probing. We believe that the incorporation is attributable to all or any of the reasons listed below:

- It would be reasonable to assume that SCB would be more comfortable with providing the loan to a UK company rather than a company based in Bermuda.
- HCL EAS would benefit from various incentives provided under the UK tax regime including the absence of withholding taxes on dividend payments and capital gains exemptions through the substantial shareholding regime.
- Having an intermediate company in the UK itself would also provide a good degree of flexibility in connection with future business reorganizations and tax planning.

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[16] Most of the revenue is generated in the form of various consumption taxes including customs duty, corporate service tax, payroll tax, land tax, stamp duty, hotel occupancy tax and passenger tax.

[17] Tax rate mentioned herein are inclusive of surcharge of 10% and education cess of 3%.

[18] Unlike most 'tax havens', Bermuda has been regarded as an active proponent of OECD's efforts to curb harmful tax competition and has implemented a number of measures to ensure transparency and effective exchange of information. Its recent bilateral agreement with the UK for the exchange of information for tax purposes is reflective of its commitment to become a responsible offshore financial center. The recognition it has been getting from the OECD and other countries could also be a factor that influenced HCL to use Bermuda as the intermediate jurisdiction.

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EPILOGUE

HCL's acquisition of Axon, in a worsening business environment worldwide, puts ambitious India Inc. in global limelight yet again. The deal which adds to the acquisition blitzkrieg by Indian Inc. intensifies the shift of balance of power and raises the question – has the age of reverse colonization really arrived?

While analysts continue to debate on the commercial viability of the deal on account of the global meltdown, need for preserving liquidity, SAP announcing an abrupt decline in sales and the recent CLSA research report suggesting Axon's growth will taper down from a CAGR of over 30 per cent seen over the last three years, HCL has not only stood by its investment, but also announced its intentions to continue with acquisitions in the coming year, economic recession notwithstanding. This indeed is a clear harbinger of the growth of the Indian economy, which is no longer limited to the historic Tata Corus or the Arcelor Mittal deals.

From a legal perspective, dissection of this deal has brought to fore some aspects of the takeovers regulations in the UK which merit import into the Indian Takeover Code. Even though the Indian Takeover Code is based on the Code, the Indian Takeover Code does not seem to adopt the concepts of the Code, which on certain counts, it probably should. Elaborate disclosure norms, recommendation of every offer to the board of directors, evaluation of the offer by an independent financial agency, treatment of hostile bids, mandatory open offer if more than 30% voting rights are acquired et al are certain concepts which are contained elaborately in the Code and may be considered in light of the Indian Takeover Code.

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