MATERIAL ADVERSE CHANGE CLAUSE

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Abstract

A Material Adverse Change (MAC) Clause is a contingency provision specifically inserted in venture finance contracts, merger and acquisition agreements, and lending agreements that gives the acquiring or funding parties, buyers or sellers, the right to back out from implementing the agreement, or seek a change of conditions when there is a substantial adverse change in the company or its prospects or business condition affecting the parties to the agreement. This provision is also often called as material adverse event or material adverse effect. This legal provision is important and essential because between the date of the agreement and the final completion and closing of the complete transaction, considerable time can lapse due to regulatory procedures, and if any material changes occur in the meanwhile, making the funding or acquisition or the material under rate contract less attractive, the venture capital provider or the acquirer or any party to agreement, must have the option to back out from the agreement or seek appropriate revision of terms and conditions in some cases.

Introduction

The global economic environment in which business houses operate is extremely volatile due to severe credit crisis, unpredictable equity markets, shortfalls in corporate profits and a sharp rise of commercial and investment disputes. The impact of the economic crises in the years 2007, 2008 and 2009 on global business environment made it worse for corporate houses to enter into financial deals and business transfers including Mergers & Acquisitions (M&A) transactions. The risks associated with the operations, financial conditions and expected performance of the acquisition targets led business enterprises and industry participants to devise a way in which they could walk

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out of a deal without facing any contractual liability. M&A transactions are at the end of the day nothing but mere contracts entered for transfer of business and assets between two entities and the most favorable way to walk out of such an arrangement without incurring a breach is to have a clause in the contract that can serve as a resort to either of the parties against unforeseen, unpredictable material changes that have a negative impact on the overall intended transaction and by virtue of that particular clause, one can close the deal without being liable for contractual breach. These clauses which are very commonly found in contractual and financial commitments are popularly called Material Adverse Effect (MAE) Clauses or Material Adverse Change (MAC) Clauses. MAC Clauses are particularly enforced in the time period between signing and closing of the deal with a view to allocating interim risk of adverse changes that might affect either of the parties. In the absence of the same, a party to such a transaction has warranties and certain representations that he has to fulfill in order to consummate the deal. The main challenge in this regard which makes the nature of these MAC Clauses unambiguous is in determining as to what would constitute as a 'material change'. In other words, it needs to be established beyond doubt that the conditions or the circumstances in which the buyer wants to withdraw before closing a deal amount to 'material adverse changes' and negatively impacts the buyer if he continues any further. Although in a typical MAC Clause, the definition of 'material adverse changes' includes description of general and specific events that provide excuses in some form to either party to terminate the transaction; however the ambit of such clauses are kept as broad and wide as possible in order to protect either parties against unforeseeable and unexpected material changes, and drastic market fluctuations, and because of this wide ambit, these clauses are often subject to multiple interpretations giving rise to disputes.[1]

Anticipating issues associated with the 'MAC' clauses and interpreting 'materiality'

One of the structural features of a typical MAC Clauses is the provision for allocation of risk between the buyer and seller in the period between sighing and closing of the deal. Even though these clauses are drafted in a manner whereby a general description of certain circumstances are provided whereby the MAC Clause on can be enforced, along with mention of certain specific

[1]Lee C. Buchheit, *How to Negotiate the Material Adverse Change Clause*, 13 INTER NATIONAL FINANCIAL LAW REVIEW 9 (1994).

events that are expressly excluded from the ambit of the same, the main point of negotiation that is raised in a dispute relates to what constitutes 'material' to the deal or its parties. It is the interpretation of this term that makes these clauses so heavily negotiable in merger agreements. If we consider 'material' to be largely a quantifiable concept, then it becomes very difficult for courts to decide whether the particular incident in the event of which the MAC is alleged to be enforced is material or not. Even after being aware of this ambiguity, the parties shy away from defining what in material in the merger agreement for two reasons: Firstly, if material is considered and defined as a quantifiable unit or number, then an objectively low threshold which brings out the same impact on the transaction is outside the ambit of the clause, and there is always an inhibition that either party might hide something below the proposed threshold. Secondly, as a consequence to the above, the absence of such a definition gives more leverage to both parties at the time of negotiating the same.[2] While the seller in a merger agreement would prefer a narrow interpretation of the term so as to limit the scope of the buyer to walk out of the deal, the buyer on the other hand seeks the opposite. The broader the ambit of a MAC Clause, the more chances it gets to terminate the transaction by showing any adverse effect that he or the deal might face.

A certain corollary of this interpretation suggests that MAC Clauses can somewhat be equated with *Force Majeure* Clauses in a contract; however the most notable difference between the two is that while the MAC Clauses are more vague not specifying the triggering event for enforcing the same, the *Force Majeure* Clause specifies certain circumstances that will excuse performance of the contract. This in a lot of ways makes the interpretation of the later easier. This to an extent is based on the contractual doctrines of impossibility or frustration of purpose where a party to a contract is excused from discharging his obligations if the performance of the transaction is practically impossible.[3] In the absence of a definite threshold for quantifying materiality, the courts through years of judicial pronouncements have tried their best to remove the uncertainty so as to make enforcement of this clause easier. It is pertinent here to note that materiality tests are not just the subject matter of MAC Clauses in a merger agreement but also find its legitimacy in other contexts such as material standards in respect of

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[2]Chestor Franklin, *Delaware Chancery Court Addresses Default Interpretation of Broadly Written Material Adverse Effect Clauses in re IBP, Inc. Shareholders Litigation v. Tyson Foods,* 115 (6) HARVARD LAW REVIEW 1737 (2002).

[3]Andrew A. Schwartz*, A Standard Clause Analysis of the Frustration Doctrine and the Material Adverse Change Clause,* 57 UCLA LAW REVIEW 789(2010).

disclosure requirements in a public takeover, misstatement under general accounting principles and most importantly while determining 'material breach' of contractual obligations under general contract principles. Another interpretive hurdle in front of the court is to determine in what context or meaning is the 'materiality' used in the MAC Clause; in other words whether the materiality is to be decided in respect of its understanding to a reasonable buyer or in respect to the person who has invoked the provision.[4]

Is the ambiguity in a MAC Clause intentional?

The ambiguity existing in interpreting MAC Clauses is without a doubt the most common downside of it as any vague contract provision invites conflicting and self interest driven interpretations and serves as an unfair incentive to the party who is in a better position either financially or otherwise, to negotiate. Due to this uncertainty, these MAC Clauses are often considered unethical to effective business decision making. Although a vague MAC Clause *prima facie* creates a burden and undue expense on parties and courts, it is imperative to note that by keeping the ambit of MAC Clause ambiguous, it gives a major advantage to the buyer when he wants to not finish his part of the obligation even with a slight change in circumstances in which the deal was first entered into.[5] Since the term 'material' is not defined, it gives both parties a wider range of opportunities to contest if the pertinent event triggering its enforcement has occurred or not. Further, it can be said that the litigation that arises from vague provisions functions as an ex post signaling device that promotes efficient renegotiation and augments the bargaining power of the buyer. When a greater scope of negotiation lies in respect of a particular provision, it encourages parties to execute a business deal in contrast to a situation where the MAC Clause is so strictly constructed that either party cannot terminate the deal except in the specifically mentioned instances and there is no opportunity of deliberating thesame.[6]

Since a MAC Clause gives the buyer in an acquisition or business combination agreement an option to exit the deal, it in a way encourages the seller as the value of the target or the representations and warranties associated with it do

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[4] Ronald J. Gilson and Alan Schwartz, *Understanding MACs: Moral Hazard in Acquisitions,* 21 (2) JOURNAL OF LAW, ECONOMICS AND ORGANIZATION 330 (Oct., 2005).

[5] Kenneth A. Adams, *A Legal-Usage Analysis of Material Adverse Change Provisions,* 10 FORDHAM JOURNAL OF CORPORATE AND FINANCE LAW 9 (2004).

[6] Fredric D. Tannenbaum and Marilyn S. Spracker, *It's Time to Talk Turkey: Seller Strategies to Prevent a Buyer from Wriggling Away,* 10 (3) BUSINESS LAW TODAY 18.

not fall or reduce between the signing and closing date. However, low value realization is not always subject to a seller's actions or inability to adhere to the requisite representations in the contract. The intended outcome of a merger is also exposed to exogenous risks cannot be controlled by the seller. This can be change in policy considerations of the State, in the economy, legal framework validating such merger and other such instances that will have an equally adverse effect on the business transaction. It is thus important to have a clear distinction between the above two situations as in the later, it will not be correct to enforce a MAC Clause with external risk out of either parties'control.[7]

Theories explaining the purpose of a MAC Clause

a) Symmetry Theory

This theory is used to explain the purpose of a MAC Clause in a merger agreement. In a traditionally drafted merger agreement, if the seller's value in the interim period between signing and closing the deal increases, then it can accept higher bids or better offers. However if the seller's value decreases, the buyer may still be bound by agreement to complete the transaction. Thus in the absence of a MAC Clause, the buyer assumes the risk that is allocated to him if the seller's value decreases but the seller does not have to bear the risk if his value increases in that time span. Thus the risk of failure of a business deal is not allocated symmetrically between both parties in the absence of a MAC. Thus a MAC Clause is understood as a contractual readjustment of this asymmetric risk allocation. In order to rectify this imbalance of risk allocation that works as a disincentive to acquirers, a well drafted MAC Clause needs to be incorporated in the mergeragreement.[8]

b) Investment Theory

This theory purports another possible explanation behind the existence of a MAC Clause. It suggests that in the absence of a MAC Clause, the seller is not given enough incentive to make synergistic investments which might reduce the stand alone value of the seller, in the interim period. Thus an efficient MAC Clause encourages a seller to undertake investments that

[7] Kari K. Hall, *How Big Is the Mac: Material Adverse Change Clauses in Today's Acquisition Environment*, 71 UNIVERSITY OF CINCINNATI LAW REVIEW 1061 (2003).

[8] David J. Denis and Antonio J. Macias, *Material Adverse Change Clauses and Acquisition Dynamics*, 48 (3) THE JOURNAL OF FINANCIAL AND QUANTITATIVE ANALYSIS 819 (2013).

would prevent a decrease in its value in the interim period. It is questionable that if the purchaser seeks to encourage the seller to make such investments in the interim period between signing and closing, it is unlikely that they would use the MAC Clause to accomplish that purpose. Indeed, the MAC Clause would be a circuitous method of encouraging the seller to make investments, especially considering that M&A agreements often include direct and explicit covenants regarding the operation of the business in the interim period.[9]

Judicial Approach to interpreting 'Material Adverse Change' by USA Courts

The standard or threshold for 'materiality' in MAC Clauses of business combination agreements has always been high which has rendered enforcement of these provisions very limited and raised questions regarding the time and expense in the negotiation and drafting of these provisions. Through decades the MAC Clause has been the focal point of interpretation by the US Courts. This section will discuss in details some important cases which highlight the major issues associated with MAC Clauses.

IBP, Inc. v. Tyson Foods, Inc.[10]

This case was related to the acquisition of IBP, USA's largest beef and pork producer by Tyson, the country's largest chicken producer with an aim to becoming an enterprise that would be the largest producer of meat in the world. Both the acquirer and the target entities were incorporated in the laws of Delaware, yet the merger agreement stated their choice of law in the matter of any dispute would be that of New York and there was no contest inthat regard. Tyson contended that IBP's revised projections deviated materially from performance in past years in the interim period between signing and closing the deal and as such, a 'material adverse change' has occurred that has affected the intended outcome of the deal and by virtue of the MAC Clause in the merger agreement, Tyson chose not to carry forward with the transaction. The Court while interpreting the 'materiality' of a MAC Clause and the legitimacy of Tyson's claim stated that *"A short-term hiccup in earnings should not suffice [to invoke a Material Adverse Effect exception to its obligation to close]; rather the*

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[9] *Ibid.*

[10] In Re IBP, Inc. Shareholders Litigation v. Tyson Foods, Inc., No. 18373, 2001 Del. Ch. LEXIS 81 (June 15,2001).

Material Adverse Effect should be material when viewed from the longer-term perspective of a reasonable acquirer." The Court further contended that the decline in projections was due to the cyclical nature of the beef industry and that such projections were not indications of any potential future failure of business. Interpreting 'materiality' the court concluded that a change can be deemed to be adverse and material if it *"substantially threatens the target's earning potential within a particular duration in a significant manner."*[11]

Frontier Oil Corp. v. Holly Corp.[12]

The Court in this case refused to accept the acquirers contention that a toxic tort lawsuit filed against the target company imposed serious threats to the deal and could prove to be financially catastrophic, triggering the enforcing of a MAC Clause. The Court following trationale of IBP, *Inc. (supra)* concluded that unless litigation is so certain to have negative consequences that to a prudent observer the likely outcome would be material and adverse, it would not be right to allow the acquirer to use the protection of a MAC Clause.[13]

Hexion Specialty Chemicals, Inc. v. Huntsman Corp.[14]

This case too, like the above two, poses a classic example where high standards of materiality were upheld by the Court. Court refused permission to Hexion to walk out of its deal with Huntsman. The latter's poor performance of several business lines and increase in debt was not sufficiently material and was held to be too narrow a change to be called adverse in the opinion of the court. The Court concluded its reasoning by asserting that *"several poor quarters of performance are an insufficient MAC trigger."*[15]

[11] *Ibid* at para.2.

[12] Frontier Oil Corp. v. Holly Corp., No. Civ. A. 20502, 2005 WL 1039027, (Del. Ch. April, 29, 2005).

[13] Adam B. Chertok, *Rethinking the U.S. Approach to Material Adverse Change Clauses in Merger Agreements,* 19 UNIVERISTY OF MIAMI INTERNATIONL AND COMPARATIVE REVIEW 99 (2011)..

[14] Hexion Specialty Chems., Inc. v. Huntsman Corp., 965 A.2d 715, 738 (Del. Ch.2008).

[15] *Ibid*.

Osram Sylvania Inc. v. Townsend Ventures, LLC[16] – Change in the judicial position

Before this case, the Courts have always showed a tendency to not allow enforcement of a MAC Clause by relying on strict and high threshold for the same. This was one of the first case before the Court where the acquirer was successful in enforcing a MAC Clause and walk out of the deal by reason of the target's non disclosure of pertinent financial information prior to signing of the agreement. Considering such action on the part of the target to be fraudulent and sufficient to trigger MAC, the court stated that *"Osmania(OSI) had plead the elements of fraud with sufficient particularity to satisfy the heightened pleading standards applicable to common law fraud claims and also pleaded a claim for negligent misrepresentation based on the sellers' alleged manipulation and concealment of financial information before the closing. As to OSI's equitable fraud claim, however, the court determined that OSI did not make the necessary allegations of any special relationship of trust or confidence between OSI and the sellers, and therefore granted sellers' motion to dismiss as to OSI's equitable fraud claim."*[17]

MAC Clauses in the Indian Merger Regime

The Indian Merger Regime is quite different from that of USA and UK. While in most foreign jurisdictions in the world, contractual mergers are commonly in practice, in India till date, M&A are mostly governed by elaborate court (tribunal) processes under Section 230 to 240 of the Companies Act, 2013,[18] and applicable rules, and prominent guidelines of the sectoral regulator of the nation, the Securities and Exchange Board of India (SEBI). Even though some forms of business and asset transfer including slump sales and joint venture can be executed by virtue of a contract between the two parties to a deal, most M&A transaction schemes require tribunal approval, hence there is little scope of a MAC Clause in the same. Irrespective of that uncertainty clouding the scope of MAC in India, it has found its place off late in share purchase agreements and disputes. In this section, the author has attempted to capture the attitude of the Indian judiciary towards MAC

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[16]Osram Sylvania Inc. v. Townsend Ventures, LLC, C.A. No. 8123-VCP (Del. Ch. Nov. 19, 2013).
[17]Y.Carson Zhou, *Material Adverse Effects as Buyer-friendly Standard,* 91 NYU LAW REVIEW 171 (2016).
[18] Chapter XV, The Companies Act, 2013.

Clauses in terms of its statutory legitimacy coupled with important judicial pronouncements.

It was first attempted to statutorily recognize a MAC Clause in the SEBI Regulations, 1997 wherein Regulation 27(1)[19] allowed an acquirer to withdraw his takeover offer on satisfying the three conditions – refusal of statutory approval, death of sole acquirer and circumstances convincing SEBI that withdrawal can be made. As regards the first two conditions, they are very specific to a situation that can render an offer and its associated obligations impossible. Thus, owing to impossibility of performance an acquirer is given an opportunity of withdrawing his offer. As regards the last condition, it is incumbent upon SEBI to decide that the circumstances are such that a withdrawal of a takeover offer can be merited. This is derived from the Doctrines of Impossibility and Frustration of purpose which is incorporated in Sec. 56 of the Indian Contract Act, 1857.[20] Further, it is to be noted that the rationale behind laying down these exceptions where an offer can be withdrawn is best explained with the help of the 'Basic Assumption Test'. The test implies that at the time of entering into a business acquisition or merger agreement, the party considers certain events, the non occurrence of which is a basic assumption on which the contract is entered into. If any of these assumptions turn out to be incorrect without any fault of his, then the court needs to discharge the party of his performance obligation and fill in the gap by determining which party was allocated the risk of the assumption's failure.[21] This provision became a ground for interpretation in the case of

[19]Securities and Exchange Board of India (Substantial Acquisition of shares and Takeovers) Regulations, 1997.Regulation 27(1)-Withdrawal of offer- No public offer, once made, shall be withdrawn except under the following circumstances:— (a) 1 [***] (b) the statutory approval(s) required have been refused; (c) the sole acquirer, being a natural person, has died; (d) such circumstances as in the opinion of the Board merit withdrawal.

[20]The Indian Contract Act, 1872. Section 56 states as follows: Agreement to do impossible act. "An agreement to do an act impossible in itself is void. Contract to do an act afterwards becoming impossible or unlawful.—A contract to do an act which, after the contract is made, becomes impossible, or, by reason of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful.1 Compensation for loss through non-performance of act known to be impossible or unlawful.— Where one person has promised to do something which he knew, or, with reasonable diligence, might have known, and which the promisee did not know, to be impossible or unlawful, such promisor must make compensation to such promisee for any loss which such promisee sustains through the nonperformance of the promise."

[21] Nathan Somogie, *Failure of a Basic Assumption: The Emerging Standard for Excuse under MAEProvisions,* 108 (1) MICHIGAN LAW REVIEW 81 (2009).

Nirma Industries Ltd. and Anr. v. Securities & Exchange Board of India.[22] The Supreme Court while rejecting Nirma's application to withdraw its offer on the ground of financial nondisclosure relating to poor performance of the target, discussed the three conditions in Regulation 27(1) in detail. The Court suggested that the first two conditions refer to legal impossibility and natural impossibility respectively and since both the exemptions are within the same genus of impossibility, the third exception has to be read *ejusdem generis* and would have to be naturally construed in terms of the other two exemptions. Again in another case, SEBI v. Akshya Infrastructure Pvt. Ltd.[23], Supreme Court was faced with the question, "*an offer voluntarily made through a Public Announcement for purchase of shares of the target company can be permitted to be withdrawn at a time when the voluntary open offer has become uneconomical to be performed under Regulation 27(1)"*. Answering the same in negative, the Court applied the narrow interpretation and stated that economic difficulty to conclude an offer did not amount to an exception under Regulation 27(1) hence the offeror cannot be permitted to leave the takeover. The same ratio was again followed in the case of *Pramod Jain & Ors. v. SEBI*[24] wherein the Supreme Court held that inordinate delay of two years by SEBI to approve the draft offer and the target company becoming a sick company in those two years frustrating the object with which the offer was made were not sufficiently material to allow the acquirer to withdraw the offer.

If we analyze the above cases, it is explicitly clear that the judiciary is not in support of detracting any business combination or takeover offer once undertaken. They are hence showing a sharp tendency towards a very narrow interpretation of Regulation 27(1) of 1997 and there is little scope for enforcing any MAC Clause in such an acquisition agreement. While in *Osram Sylvania Inc. (supra)*, fraudulent non disclosures became a ground for enforcing a MAC Clause, the same reason was not considered 'material' enough in *Nirma Industries (supra)* to withdraw the offer under Regulation 27(1) on the ground that fraud was not an impossibility. There is clear distinction in interpreting and the approach of the court towards a MAC Clause. The Supreme Court of India has adopted an extremely narrow interpretation and attitude towards the same and given little or almost no

[22]Nirma Industries Ltd. and Anr.v. Securities & Exchange Board of India, (2013)] 121 SCL 149 (SC).

[23]SEBI v. Akshya Infrastructure Pvt. Ltd., (2015) 1 WBLR (SC) 638.

[24]Pramod Jain & Ors. v. SEBI (2017)1CompLJ184 (SAT).

scope to an offeror to withdraw his offer.[25]

In 2011, SEBI Regulations, 1997 was replaced by SEBI Regulations, 2011 whereby in place of Regulation 27, Regulation 23(1)[26] has incorporated another ground in addition to the grounds mentioned in Regulation 27(1) for allowing withdrawal of offer in clause (c). It states that an offer made can be withdrawn if a condition mentioned in the acquisition agreement which trigger the offer obligations is not satisfied for reasons beyond the control of the offeror. A plain reading of the said provision raises a very basic question in as to whether the legislature has intended by addition of such clause, to broaden the ambit of withdrawal and somewhere encourage the enforcement of MAC Clause in that regard. This came up in the matter of *Jyoti Private Limited*,[27] where the acquirer wanted to withdraw its offer to take over the target company due to the latter's involvement in a BIFR proceeding and no change in control and management of the same was allowed until the pendency of the proceeding. The acquirer was of the view that due to this delay, the object of the offer was frustrated and they should be allowed to withdraw it under Regulation 23(1). The Court gave a very uncertain interpretation to the Regulation 23(1) whereby it completely ignored the intention behind incorporation of clause (c) and held that it is similar to Regulation 27(1) of the Takeover Code, 1997 and hence the decisions in respect of that still hold good. Thus the Court applied the ratio in Nirma Industries *(supra)* and concluded that for withdrawal under Regulation 23(1), the reason has to qualify the threshold of impossibility

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[25]Tushit Mishra, *Analysisof the Material Adverse Change Clause in the Indian Context*, (August 13th, 2017) https://indiacorplaw.in/2017/08/analysis-material-adverse-change-clause-indian-context.html.

[26]Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.Regulation 23.(1)- Withdrawal of open offer-An open offer for acquiring shares once made shall not be withdrawn except under any of the following circumstances,— (a) statutory approvals required for the open offer or for effecting the acquisitions attracting the obligation to make an open offer under these regulations having been finally refused, subject to such requirements for approval having been specifically disclosed in the detailed public statement and the letter of offer; (b) the acquirer, being a natural person, has died; (c) any condition stipulated in the agreement for acquisition attracting the obligation to make the open offer is not met for reasons outside the reasonable control of the acquirer, and such agreement is rescinded, subject to such conditions having been specifically disclosed in the detailed public statement and the letter of offer; or (d) such circumstances as in the opinion of the Board, merit withdrawal.

[27]Jyoti Private Limited before SECURITIES AND EXCHANGE BOARD OF INDIA (WTM /SR/CFD/39/08/2016), available at https://www.sebi.gov.in/sebi_data/attachdocs/1470054168949.pdf.

previously well settled by law.

In another 2011 case of *Atul Chopra & Ors v. Tecnotree Corporation & Ors*,[28] there was dispute regarding whether there was MAE on the business transfer between the parties by virtue of the MAC Clause incorporated in the share purchase agreement. The Court held that the defendants committed fraud by not informing the plaintiff about the decrease in the financial health of the defendant company which was one of the pre-requisite conditions for closure of the deal. The Court finally concluded that such non disclosure on their part amounted to invoking the MAC Clause and issued an interim injunction against the defendant.

MAC Clauses are a part of M&A agreements consisting of representations and conditions which are essential for closing of the transaction. A distinction has to be drawn between a pre-closing condition and a pre-closing covenant. While the former if unfulfilled allows an aggrieved buyer to walk out of the transaction without closing the deal, the breach of the later only allows him to claim monetary damages. Since these transactions are nothing but legally enforceable contracts at the end of the day, it is subject to the jurisdiction of the Indian Contract Act, 1857. Sections 73[29] and 74[30] of the Act states that the person aggrieved from the breach of a contract is entitled to compensation and damages arising from direct loss and not from any indirect or remote cause. MAC Clauses can be somewhat said to have developed on these principles. Here, a party to a merger/ acquisition agreement is discharged of his duty to carry forward with the transaction if the opposite party fails to discharge the contractual obligations resulting in a MAE on the entire deal or on the purpose sought to be achieved through the same.

Another point of determination that needs attention is whether specific

[28]Atul Chopra & Ors v. Tecnotree Corporation &Ors., 2012(3) ArbLR275 (Delhi).

[29] The Contract Act, 1872, Section 73 states that: Compensation for loss or damage caused by breach of contract.When a contract has been broken, the party who suffers by such breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage caused to him thereby, which naturally arose in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it. Such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach. Compensation for failure to discharge obligation resembling those created by contract.—When an obligation resembling those created by contract has been incurred and has not been discharged, any person injured by the failure to discharge it is entitled to receive the same compensation from the party in default, as if such person had contracted to discharge it and had broken his contract. Explanation.—In estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account.

performance can be awarded by courts on parties who choose to walk out of a business transaction by taking help of a MAC Clause. In *Genesco, Inc. v. The Finish Line, Inc.*,[31] the acquirer was not allowed to invoke MAC Clause due to decline in the overall sales of the target because it was not found to be materially significant enough to cause any adverse change and was due to an exogenous risk of deterioration of economic conditions which was one of the 'carve-outs' of the MAC Clause. At the same time, the court awarded specific performance in favor of the target and compelled the acquirer to complete the transaction. However the same relief could not have been granted had the situation would have arisen in India. Section 14(1)(c) of the Specific Relief Act, 1963[32] states that specific performance cannot be enforced in contracts which are by nature determinable. While interpreting and explaining the meaning of the term 'determinable' the court in *Rajasthan Breweries v. Stroh Brewery Co.*[33] held that if a contract contains a termination clause, then it is by nature determinable and not subject to injunction or specific performance.

[30] The Contract Act, 1872, Section74 states that: Compensation for breach of contract where penalty stipulated for. (1) [When a contract has been broken, if a sum is named in the contract as the amount to be paid in case of such breach, or if the contract contains any other stipulation by way of penalty, the party complaining of the breach is entitled, whether or not actual damage or loss is proved to have been caused thereby, to receive from the party who has broken the contract reasonable compensation not exceeding the amount so named or, as the case may be, the penalty stipulated for. Explanation.—A stipulation for increased interest from the date of default may be a stipulation by way of penalty.] Exception.—When any person enters into any bail-bond, recognizance or other instrument of the same nature, or, under the provisions of any law, or under the orders of the 2 [Central Government] or of any 3 [State Government], gives any bond for the performance of any public duty or act in which the public are interested, he shall be liable, upon breach of the condition of any such instrument, to pay the whole sum mentioned therein. Explanation.—A person who enters into a contract with Government does not necessarily thereby undertake any public duty, or promise to do an act in which the public are interested.

[31]Genesco, Inc. v. The Finish Line, Inc., Dec. 27, 2007 Memorandum and Order, Case No. 07-2137-II(III) (Tenn. Ch. 2007).

[32]Specific Relief Act, 1963. Section 14 states that: Contracts not specifically enforceable.—(1) The following contracts cannot be specifically enforced, namely:— (a) a contract for the non-performance of which compensation in money is an adequate relief; (b) a contract which runs into such minute or numerous details or which is so dependent on the personal qualification or volition of the parties, or otherwise from its nature is such, that the court cannot enforce specific performance of its material terms; (c) a contract which is in its nature determinable; (d) a contract the performance of which involves the performance of a continuous duty which the court cannot supervise.

[33]Rajasthan Breweries Ltd. v. Stroh Brewery Company, AIR 2000 Delhi 450.

By virtue of that ratio, we can conclude that MAC Clauses, part of M&A agreements are basically mechanisms by which either party can terminate the agreement in the event of any MAE taking place and hence, by nature these are determinable contracts, outside the scope of Section 14 of the Specific Relief Act, 1963. Thus specific performance cannot beinduced.

We also need to remember that the court does not have a standing on the legal validity of a MAC Clause in acquisition agreements under the Takeover Code, 2011 or general contract principles only, but since most M&A in India are part of a scheme of arrangement which is subject to approval by National Company Law Tribunal (NCLT) under Sections 230 to 240 of the Companies Act, 2013, any MAC Clause forming part of the scheme can be *suo moto* taken up for adjudging its validity and dispute with regard to it can be decided by NCLT by virtue of its inherent powers under Rule 11 of National Company Law Tribunal Rules, 2016.[34]

MAC Clause also found mention in RBI Notification dated January 13, 2000 whereby the Basel Committee discussed the 'Framework for Measuring and Managing Liquidity'[35] and the trend followed by international banks all over the world in order to manage their liquidity on a day to day basis. It has been suggested in this report that banks need to enter into funding arrangements which are of such commercial commitments in the absence of a MAC Clause, whereby the bank may not be legally able to turn their face away from the funded client even if the latter's financial health deteriorated. Although there is little significance of this report in merger/acquisition agreements taking place under Companies Act, 2013 and SEBI Takeover Code, 2011 it is often seen that major corporate M&A take place with the help of funds taken by the acquirer from these commercial banks. Hence, RBI's take on a MAC Clause in the agreement between the acquirer and his financing bank might be of some importance.

[34] National Company Law Tribunals Rules 2016, Rule 11 states that: Inherent Powers.- Nothing in these rules shall be deemed to limit or otherwise affect the inherent powers of the Tribunal to make such orders as may be necessary for meeting the ends of justice or to prevent abuse of the process of the Tribunal.

[35] RBI Notification dated January 13, 2000 on 'Framework for Measuring and Managing Liquidity.'

Conclusion

The author in this paper has attempted to bring into focus the limited scope of a MAC Clause in the Indian merger regime with regard to its legal validity and enforceability. The author has mentioned the judicial attitude towards MAC in a country like USA and hereby suggests that the recognition of a MAC Clause would encourage businesses to undertake more M&A activities because they would not have inhibitions about closing a deal which might turn out to be a loss post signing of the same. It is not right to comment that Indian law does not have scope for validating MAC in a wide scale but it is the judicial pronouncements over the recent years that have not shown a very friendly response towards enforcing such provisions and there is a sharp tendency to not let acquirers terminate a deal or discharge him of the obligations to consummate the same even if circumstances make the transactions a total loss for the party for reasons beyond his control. Additionally, the absence of contractual mergers unlike in foreign countries still allow court intervention for a step by step approval thus making the M&A deals in the country more in the nature of a public transaction. Even if amendments are brought in the new Takeover Code of 2011 and MAC Clause finding a place in most share purchase agreements, the enforcement and implementation of the same lacking the force of law, the entire purpose becomes pointless. It is thus suggested time and again that in the light of keeping up with the global M&A practice in order to attract more and more investors, it is the need of the hour that these MAC Clauses are given due importance. Recently, India's largest tyre manufacturer Apollo was able to walk out of a deal with Cooper Tyres using a MAC Clause because the later could not arrange financing that it initially promised for the execution of the deal and the delay had a negative impact on the shares of Apollo both in the home and international market. The Court at Delaware gave Apollo the chance to terminate a deal that would have otherwise proved to be a financial loss for it.[36] The one lesson from this is that if an Indian company is given such ease and flexibility of doing business in a US market, the same ease should be afforded to the foreign investors who wish to pursue an acquisition with an Indian company or have a joint venture with the same, whatever be the case.