

Merger of Companies and its Impact on Partners and Shareholders

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Abstract

The present study deals with the reasons and importance of merger of companies in Palestine. The study approaches the issue in two sections: the first defines the concept of merger, focusing on its definition, forms, and scope of application. The second section examines potential impacts on partners and shareholders. It is divided into four subsections: partners' rights during merger; shareholders' right to manage the merging or the new company; partners' right to object to the merger proposal; and right to appeal against merger decisions.

The researcher concludes that, because company merger has not been sufficiently regulated by the Palestinian law, the applicable Jordanian Company Law No. 22 of 1997 is applied in Palestine. Regarding the issue of determining the shares of partners and shareholders, it is argued that more than one criterion should be considered, and that the exchange rate should not be restricted or determined by the shareholders.

Keywords: Merger of companies, merger in Palestine, competition law Palestine, companies Palestine

1. Introduction

1.1 Reasons and Significance of Company Merger

Economic activity growth, US corporate monopoly of modern technology, and the need for substantial financial resources caused a wave of mergers between US companies in the 1950s and 1960s. These mergers have led to the emergence of oligopolistic market structures across the USA. This served as a public policy, which was associated with a desire to undermine and declare bankrupt a large number of small and medium-sized companies (Al-Said, 1978; Al-Masri, 1986).

On the other hand, the USA established economic control over Western Europe and other countries. US investments were promoted, particularly in Britain, Germany, France, Italy, and Belgium. US companies managed to tighten their grip on European companies and acquire an increasing number of European industrial enterprises. Facing fierce competition, European companies were on the verge of collapse.

To cope with the control maintained by US companies, European companies opted for merger as a tool to support competitiveness, defend existence, remain competitive, and maintain independence.

Counter-mergers were not nationally limited to individual European countries. The European Economic Community (EEC) also promoted a merger policy that instructs mergers between companies of two or more EEC member states. A concerted effort was made to avoid challenges to market level mergers (Al-Said, 1978; Al-Masri, 1986).

Against this background, company merger is a tool of economic concentration¹ and conversion of small and medium-sized enterprises (SMEs) into large-scale corporations. Merged companies wish to collaborate and achieve integration by consolidating production tools to support competitiveness, increase productivity, introduce new products, improve the quality of goods, and reduce production cost and prices. Bringing about favourable and required conditions, mergers contribute to enhancing standards of living, boost national economy, and yield greater profitability for shareholders. By contrast, companies desire to control and exercise monopoly, negatively reflecting on the quality, prices, and availability of goods. It also disrupts SME emergence and continuity, whereby it is an unfavourable practice.²

This has prompted states to intervene and regulate company merger by legislative acts. In line with state interests, relevant regulations differ from one state to another in terms of the purpose of merger and other forms of economic concentration. These may exercise strict control over merger processes with a view to maintaining free competition, protecting national economy, and fighting monopoly and control. In contrast, states may devise rules to promote mergers (Fahim, 1976; Al-Masri, 1986).

In Palestine, the Company Law No. 12 of 1964 in force in the West Bank, as well as the Company Laws of 1929 and 1930 operative in the Gaza Strip, do not provide a detailed account of merger. As these laws are outdated, companies wishing to merge apply the process prescribed by the Jordanian Company Law No. 22 of 1997 as amended. However, this important issue has recently prompted the Palestinian Ministry of National Economy to develop a draft company law, which consolidates company regulations in Palestine and keeps pace with relevant legislative developments. Earlier, draft company laws were produced in 2005, 2008, and 2010. Articles 204-216 of the 2010 Draft Company Law address company merger. Developed in 2016, the last draft company law regulates merger of companies under Articles 186-206.

1.2. Research Problem

The present paper does not aim to review provisions or account for earlier literature on the merger of companies. Rather, the paper offers new solutions to the problem faced by interest holders and shareholders, whose rights are affected by the legal conversion of the forms of companies through merger. In addition, the paper contributes to improving the legal system in general, and the Palestinian legal framework in particular.

1.3. Research Methodology

This research paper is informed by a comparative approach. It presents the provisions of merger under the 2016 Palestinian Draft Company Law, a law in the making. The paper investigates the provisions cited by the 2016 Draft Company Law from other legislation, including Jordanian, Egyptian, and French laws. To this avail, the paper provides an overview of the current legal status (*lex lata*) and proposes legal solutions for potential predicaments. The 2016 Draft Company Law is the future law (*lex ferenda*), reflecting what the company law should be.

The paper is also informed by an analytical approach, which analyses and derives provisions from legal texts.

¹ Economic concentration emerged in the USA in 1865. The phenomenon was increasingly alarming as corporate monopolies controlled petroleum, mining, banking and other sectors. Wealth was concentrated in the hands of a few individuals, serving their own interests and purposes (Al-Saghir, 2016).

² Mergers also vest large-scale corporations with political and economic powers, causing discomfort to state authorities.

1.4. Research Plan

This research paper comprises two sections. Section 1 defines merger and provides an overview of the forms and scope of the merger of companies. Section 2 examines the impact of merger on partners and shareholders.

2. Definition, Forms and Scope of Merger

This section consists of two subsections. Subsection 2.1 defines and presents the forms of merger. Subsection 2.2 elaborates on the scope of application of merger.

2.1. Definition and Forms of Merger

2.1.1. Definition of Merger

Jurisprudence provides several definitions of merger³. All these revolve around the elements, conditions, and consequences of merger. For example, merger is a contract, according to which one or more companies are absorbed into another. The corporate personality of the merged company ceases to exist, and its assets and liabilities are transferred to the merging company. Two or more companies are consolidated, terminating the corporate personality of each. The assets and liabilities of both companies are transferred to a new company (Al-Masri, 1986). This definition unveils the characteristic features of merger:

1. It is a contract; i.e. it takes place between relevant management bodies at the companies participating in the merger.
2. It involves existing companies that enjoy corporate personality.
3. It results in the termination of the corporate personality of the merged company, transference of its assets and liabilities to the merging⁴ or new company resulting from the merger.

2.1.2. Forms of Merger

Forms of merger vary according to the perspective from which merger is viewed. In addition to the traditional classification, merger is divided along the lines of the nature of the operations of companies participating in the merger. It also varies according to management intervention in the merger process (Fayyad, 2013).

2.1.2.1. Traditional Classification of Merger

According to its definition and relevant regulations, merger is of two main types: (1) merger through absorption, and (2) merger through consolidation.

³ Shafiq defines merger as the “termination of one or more companies by another, or the termination of two or more companies and incorporation of a new one, to which liabilities of the terminated companies are transferred” (Shafiq, 1957). Others define merger as the “absorption of two or more existing companies, either by merging one into another, or by incorporating a new company in which the existing companies merge” (Taha, 2008, 1982; Ahmed, 2009; Al-Jubour, 2013; Al-Fiqi, 2017).

⁴ The Egyptian Court of Cassation confirms that merger, in its correct legal sense, occurs between companies that enjoy a corporate personality and independent financial liability. The personality of the merged company terminates and all its financial liabilities are transferred to the merging company. The latter legally replaces the former in terms of rights and obligations. The mere transference of a sector of a company’s activity to another as an contribution in kind to its capital is not considered as a merger. In this case, the first company continues to retain its corporate personality and financial liability in relation to potentially outstanding obligations. Egyptian Court of Cassation, Objection 679, Judicial Year 40. Session of 19 April 1976, Technical Office, Year 27, p. 977. Also Abdul Tawwab, 2000.

2.1.2.1.1. Merger through Absorption

Merger through absorption is a combination of one or more companies, called the merged company(s), into another, called the merging company, whereby the former become(s) part of the latter. In addition to losing its corporate personality, the first company's assets and liabilities are transferred to the second company, which continues to retain its corporate personality. The latter's capital increases in the amount of the merged company's assets.⁵ This form of merger (i.e. absorption) takes place by the termination of a company in the interest of the other, which increases in size (Ahmed, 2009). This is the most common form of merger (Zarrouq, 2014) due to easy procedures and low costs associated with the merger.

2.1.2.1.2. Merger through Consolidation

Merger through consolidation is a combination of two or more companies to form a new company. The corporate personality of the merged companies terminates. A new corporate personality arises, namely the company resulting from the merger. The merged companies' assets and liabilities are transferred to the merging company. As a general successor, the latter acquires all the assets, properties, debts, and liabilities of the merged companies.⁶

Merger through consolidation may reflect the true meaning of merger. In spite of consequent expenses and the time it takes, merger through consolidation highlights and explicates the content of this administrative process (i.e. merger). It leads to the incorporation of a new corporate body, rather than the absorption (or acquisition) of a weaker by a more economically powerful company (Mousa, 2010).

2.1.2.1.3. Merger through division and Absorption

This is another form of merger, provided by Article 255 of the Kuwaiti Company Law No. 1 of 2016.⁷ A company's liability is divided into two or more parts. Each part is transferred to an existing company.

2.1.3. Merger as per the Nature of the Operations of Merged Companies

In mergers through absorption and consolidation, the operations of merged companies are either similar, complementary, or different (Abu Zeinah, 2012).

2.1.3.1. Horizontal Merger

A horizontal merger takes place if the objectives of merging companies are similar or when companies conduct the same business, such as producing and marketing the same goods in the same markets. For example, two banks, pharmaceutical companies, or food processing companies merge. The merging company (i.e. resulting from the merger) continues to operate in the same space, but at a larger scale.

Horizontal merger aims at concentrating financial liquidity of the merging companies to deliver one high-quality service. For instance, in 1998, Exxon and Mobil energy companies signed a \$78900000 merger agreement, forming a new company called Exxon Mobil (Mayu, 2015).

⁵ Article 186 of the 2016 Draft Company Law provides that "companies provided for under this Law merge... (1) through the merger of one more companies with another company(s), which is called the 'merging company'. The other merged company(s) is terminated and the corporate personality of each ceases to exist. All the rights and liabilities of the merged company are transferred to the merging company after registration of the merged company is crossed out..." According to merger through absorption, the Egyptian Court of Cassation ruled that the "the impact the merger of a company through absorption is that the merging company replaces the merged company in terms of rights and obligations." Egyptian Court of Cassation, Objection 9721, Judicial Year 65, Session of 10 June 2002, Technical Office, p. 942.

⁶ According to Article 186(2) of the 2016 Draft Company Law, "[b]y the merger of two or more companies to incorporate a new company, which is the company that results from the merger. The companies that merge into such company are dissolved and the corporate personality of each ceases to exist."

⁷ Kuwaiti Ministry of Commerce and Industry, <http://www.moci.gov.kw/>.

Horizontal merger is presumed to reduce competition and ensure industrial concentration and stability. However, it may result in monopoly and price control. The state should intervene if it believes that horizontal merger is premised on monopoly or weakens competition in the market.

2.1.3.2. Vertical Merger

A vertical merger occurs when the objectives of merging companies are complementary (i.e. each company complements the other). For example, a company produces a commodity or delivers a service that is complementary to that produced or delivered by the other. A food processing company can merge with another that manufactures food cans, a food marketing company, or both. Also, a car maker can merge with a company that produces wheel tyres.

Vertical merger takes place between two or more companies that operate interconnected stages of the production process. It aims to consolidate financial liabilities and provide an integrated service to customers. This activity requires a significant economic base, which can be maintained by vertical merger (Al-Fayyumi, 2009; Sayyed Ahmed, 2013).

2.1.3.3. Mixed (Conglomerate) Merger

In mixed (conglomerate) merger, the objectives of merging companies are different; i.e. each company does a different business. Forms of mixed (conglomerate) merger are few.

2.1.4. Merger according to Management Intervention

Merger as per management intervention can be either amicable (voluntary) or compulsory (involuntary).

2.1.4.1. Amicable (Voluntary) Merger

This is the principal form of merger. It is based on an agreement concluded between merging companies without coercion, pressure, or intervention by any party.

2.1.4.2. Compulsory (Involuntary) Merger

Compulsory (involuntary) merger takes place when a particular management merges companies involuntarily in order to adjust the position of companies in default or those on the brink of bankruptcy or liquidation. More precisely, this activity is closer to absorption than to merger.

2.2 The Scope of Application of Merger

This subsection elaborates on the form, nationality, and objectives of companies participating in merger.

2.2.1. Form of the Company Participating in Merger

The 2016 Palestinian Draft Company Law and Emirati Company No. 2 of 2015 do not place any restrictions on the forms of the companies wishing to merge. According to one opinion, all types of companies provided under the 2016 Draft Company Law may merge, regardless of whether they are of an identical form or not. This is considered as a modification of the company's memorandum of association and articles of association (Abu Zeinah, 2012). Article 255 of the Kuwaiti Company Law No. 1 of 2016 explicitly provides that a company may merge with another of the same or a different corporate form (Fayyad, 2017).

However, Article 187 of the 2016 Draft Company Law provides: "If two more companies of the same type merge into an existing company or to form a new company, the merging company or new company, which results from the merger, is of such type. However, the limited liability company or private joint stock company may merge into an existing public joint stock company or incorporate a new public joint stock company." As a rule, the 2016 Draft Company Law restricts merger to companies of a single type. This means that merger can involve two partnerships (a joint liability

company with another to form a new joint liability company), or two joint stock companies (a private joint stock company with another, or limited liability company with another, to form a company of the same type). Accordingly, two companies of different forms may not merge; e.g. a partnership (general partnership)⁸ with a joint stock company.⁹ The difference between both is substantial and affects the rights of partners or stockholders. On the other hand, the law endorses the merger of joint stock companies with others. In this context, a limited liability or private joint stock company can merge into a public joint stock company. Both companies can also merge to form a new public joint stock company.¹⁰

2.2.2. Nationality of the Company Participating in Merger

Article 130 of the Egyptian Company Law allows a foreign company, operating in Egypt, to merge with an Egyptian public joint stock company or form a new Egyptian company.

By contrast, the 2016 Palestinian Draft Company Law does not provide explicitly for the nationality of the company participating in merger. Overall, it is perceived the Draft Law allows and regulates the merger of national companies only. There can thus be no question of a Palestinian company merging with a foreign company, whether operating in Palestine or elsewhere.

As an exception, Article 186(3) of the 2016 Draft Company Law provides: “Through the merger of the branches and agencies of foreign companies operating in Palestine with an existing or new Palestinian company incorporated for such purpose, the branches and agencies shall expire and the corporate personality of each of them no longer exists.”¹¹ On the other hand, Article 204(a)(3) of the 2010 Draft Law prescribes: “Through the merger of a branch or branches of foreign companies operating in Palestine in line with either of the two methods mentioned above, on condition that the parent company of the branch or branches approves the merger process”.

Accordingly, a national company may not merge with a foreign company. If a national company wishes to merge into or with a foreign one, it can do so after it is dissolved, liquidated, and its net assets are transferred to the merging or new company.

2.2.3. Purposes of the Merging Company

The goal or purpose of the merging company is to conduct the business (Fayyad, 2012), for which it has been incorporated to exercise and deliver. This is stated on the company’s memorandum of association and articles of association. As a general rule, the company may not conduct a business that does not fall within its objectives. The latter identify the company’s corporate entity.

To this avail, Article 186 of the 2016 Draft Company Law stipulates that “[t]he objectives of any of the companies wishing to merge must be identical or complementary”.¹² Accordingly, merger can only take place between companies with identical or complementary objectives. In this case, merger reflects a modification of the objective of the merged company. If a company wishes to merge with another of a different objective, it must, *ab initio*, modify its memorandum of association and

⁸ Article 9 of the 1964 Jordanian Company Law defines a general partnership as the “company in which all partners are personally and jointly liable for the company’s debts as well as all of its contracts and obligations.”

⁹ Article 39(2) of the 1964 Jordanian Company Law defines a public joint stock company as the “company which is void of an address. Its capital consists of tradable shares that are offered for public subscription. The stockholders’ liability is limited to the contribution of each to the company’s capital.”

¹⁰ The 2016 Draft Company Law quotes this provision from Article 223 of the Jordanian Company Law No. 22 of 1997. On the other hand, Article 130 of the Egyptian Company Law No. 159 of 1981, Amended by Law No. 3 of 1998, and Article 228 of the respective Bylaw, allow joint stock companies to merge with both types of partnerships in shares, limited liability companies, and joint liability companies... and to form a new Egyptian joint stock company. Also, Article 133 of the Bylaw of the Kuwaiti Company Law No. 1 of 2016 unrestrictedly allows merger between two or more companies of any type.

¹¹ Quoted from Article 222 of the Jordanian Company Law.

¹² Article 204(a) of the 2010 Palestinian Draft Company Law also prescribes that “[t]he objectives of any of the companies wishing to merge must be similar, identical or complementary”. This provision is quoted from Article 222 of the Jordanian Company Law.

articles of association based on a decision from the extraordinary general assembly for reasons to be approved by the competent management body.

However, the objectives of companies wishing to merge may not necessarily be completely identical. It suffices that company objectives be similar or complementary (Fayyad, 2012). This means that merger can occur between commercial and civil companies if the objectives of both are complementary. For instance, a civil company with the objective of livestock breeding and sale of livestock products can merge with a dairy products company, or a civil agricultural company with a commercial agribusiness company.

In the case of absorption, the merging company must add a new objective, stating the merged company's activity. In the case of consolidation, the new company's objective is dual, combining the operations of both merged companies.

By contrast, the Emirati Company Law No. 2 of 2015 and Kuwait Company No. 1 of 2016 do not require that the objective of companies wishing to merge be identical or complementary.

3. The Impact of Merger on Partners and Shareholders

Merger has a bearing on partners and shareholders of the companies participating in merger. The impact of merger is addressed in four subsections below.

3.1. The Rights of Partner or Shareholder in Relation to Merger

Merger results in the termination and cessation of the corporate personality of merged companies.¹³ However, termination does not cause extinction of the projects, for which the company has been incorporated. These projects continue to exist and operate, but are transferred to the merging or new company as a contribution in kind. According to the conditions of the merger contract, partners or shareholders of the merged company(s) obtain a number of shares or interests in the merging or new company in place of their rights in the dissolved company.

Shares and interests in the new or merging company are offered to partners in their individual capacity, rather than to the merged company. In other words, the offering is made directly to partners of the merged company in their capacity as successors of that company (Chadefux, 1999).

In merger through absorption, the merging company issues new interests or shares that match the net assets of the merged company(s). These are proportionally distributed to partners or shareholders of the company(s) relative to the rights each partner had in the merged companies (Fayyad, 2014). Accordingly, each one becomes a partner or shareholder of the merging company. In merger through consolidation, the new company resulting from the merger distributes the interests or shares issued by the company for the first time to the partners or shareholders of the merged companies, whereby they become partners or shareholders of that company. They may not be compensated for their interests or shares in any other way, such as bonds, shares of a company other than the merging or new one, or a sum that is distributed to partners or shareholders of the dissolved company. This would be considered as a sale, rather than a merger (Taha, 2000; Mihrez, 2004; Sarkhuh, 1993; Abu Zeinah, 2012).

Each partner must obtain the same number of interests or shares, which they owned in the merged company, unless valuation of the merged company's assets and properties reduces this number and unless otherwise agreed (Al-Shimmari, 1991).

¹³ The Jordanian Court of Cassation has consistently resolved that by merger, merged companies are terminated and their corporate personality ceases to exist. Their financial liability is transferred to the merging or new company. *Journal of the Jordanian Bar Association*, (1995). 3-4, Year 43. In many judgements, the Egyptian Court of Cassation has also ruled that merger terminates and removes the corporate personality of the merged company, The merging company generally succeeds the merged company in terms of rights and obligations. Egyptian Court of Cassation. Objection 250, Judicial Year 46, Session of 24 March 1980, quoted in (Al-Qalyoubi, 1993).. Also see Egyptian Court of Cassation. Objection 27, Judicial Year 51, Session of 26 December 1981, quoted in (Saleem, 2000).

If shares of the merged company are of a single type and have the same value, the merging or new company issues one type of shares. These are proportionally distributed to shareholders of the merged company relative to their rights in the merged company.

If the Company Law allows to issue preferred shares,¹⁴ and the merged company's shares are split into several types on the basis of rights and privileges or split into several categories on the basis of value, shareholders of that company must receive a number of shares, which vest them with the same rights endowed by their shares in the merged company. If shareholder rights in the merged company prefer shareholder rights in the merging company to its assets, the first category of shareholders must enjoy the right to preference over the shares acquired by the other category of shareholders (Al-Masri, 1986). If the merging company's memorandum of association and articles of association do not allow to issue preferred shares, the company may modify and submit its articles of association to the extraordinary general assembly to issue and distribute preferred shares to shareholders of the merged company, giving them the same privileges they were entitled to before the merger took place (Mihrez, 2000).¹⁵

Shareholders of the merged company(s) retain their capacity in the merging or new company. Consequently, they enjoy all partner rights, showing no difference from old partners or shareholders of the merging company (Al-Saghir, 2016). Jointly with the old shareholders, they are entitled to share a portion of the profits made by the merging or new company, participate in ordinary and extraordinary general assembly meetings, vote for decisions, elect board of directors, challenge the decisions made in violation of the law, receive a portion of assets at the time of liquidation., etc.

A question that arises in this context is: How are partners' interests and shareholders' shares in the merged companies assessed?

According to the provisions of comparative laws, the merged companies' assets and liabilities which are transferred to the merging or new company are considered as contributions in kind. Hence, the value of the merged company's shares is assessed in line with the rules of valuating contributions in kind.

Merged companies' assets and properties are assessed at three stages:

1. Initial valuation of assets and liabilities

This valuation is provided and stated by the merged companies on the application for merger. To this end, these companies can consult with experienced accountants, technicians, etc. According to Article 225(e) of the Jordanian Company Law and Article 189(e) of the Palestinian Draft Company Law, companies wishing to merge are entitled to assess their assets and liabilities at actual or market value. They can choose between the two values to maintain their interest. Companies can choose the higher market value of, for example, real estate, patents or trademarks.¹⁶

2. Final valuation

At this stage, valuation is provided by an ad hoc committee, which is established for this purpose, to ensure an accurate assessment. While, the Egyptian Company Law provides that it is formed by the Capital Market Authority (Article 290 of the respective Bylaw), the Jordanian Company Law assigns the Company Controller to establish the committee (Article 228). By contrast, the 2016 Palestinian Draft Company Law authorises the minister to form the valuation committee (Article 192).

¹⁴ Preferred shares give their holders the privilege to receive a certain portion of profits while the company exists. Holders of preferred shares are also prioritised when the company assets are divided at the time of liquidation (Al-Saghir, 2016). Along this vein, Article 35(2) of the Egyptian Company Law No. 159 of 1981 asserts that the "regulation may provide for setting certain privileges for particular categories of shares in voting, profits, the outcome of liquidation..." This is the same provision under relevant French legislation (Al-Saghir, 2016).

¹⁵ While the 1964 Company Law does not allow to issue preferred shares, Article 96 of the 2016 Draft Company Law does.

¹⁶ Al-Saghir, Husam al-Din (2016). *The Legal Framework Company Merger*. Alexandria: Dar al Fikr al Arabi, 537; Al-Akkili, Aziz. (2010). *The Intermediate in Trading Companies*. 1st ed. Amman: Dar Al-Thaqafa for Publishing and Distribution, 534.

According to Article 192 of the Palestinian Draft Company Law, membership on the valuation committee includes the Controller or his representative, the auditors of the companies wishing to merge, a representative of each company, and a suitable number of experts and specialists. The committee evaluates all the assets of the companies wishing to merge along with their liabilities, in order to substantiate the net equity of shareholders or partners, as the case may be, at the date designated for the merger. The committee submits its report to the minister along with the opening balance sheet for the company resulting from the merger, within a period not exceeding 90 days from the date of referring the matter thereto. The minister may extend this period for another similar period should it be necessary. The wages and remuneration of the committee are determined by a decision from the minister, and they are equally borne by the companies wishing to merge.

3. Voting for the final valuation

After the valuation committee's report is submitted, the shareholders' extraordinary general assembly or creditors of each merged company are invited to approve the valuation. In the presence of the Controller or competent employee, the decision is made by a majority of 75 percent of the shares represented for each company.¹⁷

The French legislator does not set particular rules for valuing or assessing the values of companies, leaving the matter to professionals. This process is complicated and is not conducted in line with strict, consolidated, or practically difficult rules (Faut, 1995; Pirolli, 1979). Multiple valuation techniques are used, including those applicable to liquidation, profit account, and stock exchange rate.

Companies adopt the account approved in the last fiscal year by the general assembly. This is the objective criterion, which takes into consideration common personal factors among companies, such as hiring new managers, active management, and easy access to the stock exchange.

The researcher is of the view that more than one criterion of needs to be adopted in the valuation process. The exchange rate should not be restricted nor assessed by shareholders. The share price will eventually be a compromise between negotiating companies.

The net value of the company's assets is divided by the constituent shares or interests. If the actual value of the merging company's shares is higher than their nominal value, the difference between both, as well as the amount of capital increase which was effected by the merging company, must be maintained off the balance sheet as part of the merger price. It is considered as a debt owed by the company to the new partners.

3.2. Shareholders' Right to Manage the Merging or New Company

In addition to the rights mentioned above, partners or shareholders in the merged company(s) enjoy the right to participate in managing the merging or new company.

A problem does not arise for the company management if the merging or new company is a general partnership (joint liability company) or a limited partnership (limited partnership in shares). The company management either convenes by all joint partners if a manager is not appointed. Otherwise, it convenes by the manager(s) appointed under the memorandum of association of the merging or merged company or under a separate memorandum of association. In this context, the rules which regulate partners' rights in this type of companies are applicable (Al-Takruri and Sinnawi, 2011).

In joint stock companies, based on the conditions set by the merger contract, shareholders in the merged company(s) become members of the general assembly of the merging or new company. Similarly, a difficulty does not arise if the law (e.g. 1981 Egyptian Company Law) does not set a maximum limit of the number of members of the board of directors. The merging or new company's board of directors may consist of any number, provided that it is not less than three. In this case, the

¹⁷Article 194(a)(2) of the 2016 Draft Company Law

company's board of directors can accommodate all members of the board(s) of directors of the merged company(s). This implies a negative dimension, however. The board's activity and efficiency might be disrupted if members are too many, impeding the decision making process (Al-Masri, 1986).

On the other hand, management provided by the board of directors of the merging or new company is made difficult if the law sets a maximum number of the board members. The maximum number of members of the board of directors is 11 under the 1964 Company Law, 12 under the French Company Law, and 13 by both the 1997 Jordanian Company Law and Palestinian Draft Company Law. The limits provided by law may not be exceeded even if the company results from the merger of two or more companies (Mousa, 1997).

To overcome this difficulty, the French Company Law allows to extend this maximum limit to include all members of the merged companies' boards of directors for a period of not less than six months prior to the merger. However, the number varies according to whether the merged companies are listed on the stock exchange. If neither company is listed, it is a condition precedent that members of the merging company's board of directors are not more than 24. By contrast, if the company is listed on the stock exchange, the number may be raised to 21 members. If both companies are listed, the number may be as high as 30. This increase is limited to three years, starting from the date of merger. The French jurisprudence calls this *condition de mariage* (Abu Zeinah, 2012).

Against this background, the merging or new company's board of directors may include members of company board(s) up to the maximum allowed. If it exceeds the maximum (e.g. if merger takes place between three companies with 12 board members each), some members of the merged company's board of directors need to abandon their positions. Often times, this issue is negotiated between initiators of the merger with a view to identifying members of the merging or new company's board of directors following the merger. Otherwise, at least the number of members is determined (Al-Saghir, 2016).

On the other hand, the Jordanian Company Law and Palestinian Draft Company Law provide for an interval between approval and completion of merger. Boards of directors of companies wishing to merge continue to exist and operate until merger procedures are finalised and the merging or new company is registered.¹⁸

After merger procedures are finalised and the company is registered, the company is managed by the executive committee, which is established by the minister, for a period of 30 days. The committee comprises a number of chairs and members of the boards of directors of the companies wishing to the merge, as well as the auditors of these companies. It invites the general assembly of the merging or new company to elect a new board of directors after the shares resulting from the merger are distributed. The general assembly ensures that shareholders who wish to run for membership of the board of directors fulfil relevant conditions. Accordingly, the elected board will be representative of all the merged companies. The company auditors will also be elected.

It can be concluded that the Egyptian legislator does not restrict the number of members of the merging or new company's board of directors.¹⁹ However, expanded board membership might obstruct the company's operations and cause disagreement among members due to different objectives, priorities, and management methods.

Providing a more balanced approach, the French legislator allows extending board membership up to a maximum limit. Nevertheless, board members of merged companies, particularly influential individuals who would lose their positions, may disrupt the merger process.

Therefore, the Jordanian and Palestinian legislators have rightly chosen to provide that each company wishing to merge maintain its board of director during the interval between approval and completion of the merger process. The executive committee is then in charge of the company management for a period of 30 days, during which a new board is elected.

¹⁸ Article 232 of the 1997 Jordanian Company Law and Article 196 of the 2016 Palestinian Draft Company Law.

¹⁹ The number of members of the new board of directors is raised to cope with the increasing tasks and expanding economic enterprise of the merging company (Romanicianu, 1991).

3.3. Partners' Right of Objection to Merger and Withdrawal from the Company

Comparative legislation provides two approaches to addressing partners' objection to the decision on merger, either at the merging or merged company, potential withdrawal from the company, and refunding of the value of shares.

Firstly, partners' withdrawal is regulated by clear, explicit provisions, which protect the rights of shareholders, who object to the merger. This approach is embraced by, *inter alia*, the Egyptian, Emirati, Kuwait, and Palestinian legislators.

1. Egyptian Law

Article 135 of the 1981 Egyptian Company Law and Article 295 of the respective Bylaw set the conditions for the right of objection to merger and withdrawal from the company.

Accordingly, the shareholder or partner, who objects to the decision on merger at the general assembly, which is invited to approve the merger, or does not attend the meeting on grounds of an admissible excuse, may submit a request to withdraw from the company and recover the value of his shares. He submits a written request to the company, either in person or via registered mail, within 30 days from the date of announcing the merger; i.e. the minister's decision on merger is included on the commercial register. In the request, the shareholder or partner expresses his willingness to withdraw from the company, making clear the shares or interests he possesses.

The board of directors or managers must notify the objecting partner or shareholder, by a letter with the acknowledgement of receipt and within 15 days from the date his letter is received, of whether his excuse is admissible according to the rules the company sets and includes on the invitation to the general assembly, which is invited to consider the merger. If a dispute arises between both parties, the concerned party files the matter to court to adjudicate how valid the admissible excuse is.²⁰

It is noted that the objector is not required to state the reasons for his objection as he is not obliged to stay in a company other than that he is a partner or shareholder of. On the other hand, if it does not admit the excuse, the board of directors must state the reasons of rejection so that the objector can challenge the decision.²¹

The value of interests or shares is assessed by mutual agreement or at court, taking account of the current value of all company assets. The board of directors or managers inform the shareholder or partner, who opts for withdrawal, of the value of his shares or interests, which the company assesses, on the basis of the current value of its assets. He is also notified of the date, on which the amount is placed at his disposal. If he is not satisfied with the value, the shareholder or partner can submit the matter to court to assess the value of his shares or interests. The court renders a judgement, stating compensations for the concerned parties, if relevant. The amounts awarded in compensation have a lien on all assets of the merged company. The undisputed value of relinquished shares or interests must be paid to the entitled parties before the merger process is completed.²²

2. Emirati Law

In relation to the right of objection to merger, the Emirati Company Law No. 2 of 2015 draws a distinction between shareholding and other companies.

In regard of companies entering the merger, Article 285(2)(b) of the Law stipulates that, in the invitation of the general assembly to examine the merger, the "contract shall clearly state the right of any one or more shareholders holding at least 20 percent of the capital of the company, who objected to the merger, to appeal the merger before the competent court within 30 (thirty) days from the date of approval of the merger contract by the General Assembly or any other similar body."

²⁰ Article 235 of the Bylaw of the 1981 Company Law.

²¹ Article 76 of the 1981 Company Law.

²² Article 135(4) of the 1981 Company Law.

With reference to refunding the value of shares, Article 287 provides:

1. Except for joint stock companies, the partners who object to the merger decision may demand to withdraw from the company and to recover the value of their shares, by providing a written request to the company within 15 (fifteen) working days from the date of the merger decision.
2. The value of the shares, the subject matter of withdrawal, shall be assessed by mutual agreement. In the event of disagreement on such assessment, the matter shall be referred to a committee formed by the competent authority for this purpose in respect of all companies prior to resorting to the court.
3. The undisputed value of the shares, the subject matter of the withdrawal, shall be paid to their holders prior to completing the merger procedures and prior to resorting to the committee as set forth in the preceding clause in connection with the disputed value.

3. Kuwaiti Law

Article 261 of the 2016 Kuwaiti Company Law provides that “[i]n case the merger will cause an increase of the financial burdens of partners or shareholders, or prejudice their rights in any of the companies participating in the merger, all partners or shareholders of the company shall approve the merger.”

If a partner or shareholder objects to the merger, the provisions of Article 251 of this law shall apply.

According to Article 251 of the Law, “[a] partner who objects to the merger decision may withdraw from the company and recover the value of his interests or shares through a request submitted to the company within sixty days from the date of registration. Payment of the value of interests or shares shall be made according to their actual value as indicated in the valuation report,” which is compiled by an auditing firm approved by the Authority according to Article 11 of the Law. The report shall only be final after it is approved by the general assembly.

4. Palestinian Draft Law

Article 198 of the 2016 Palestinian Draft Company Law allows any interested shareholders or partners to file an objection to the minister within thirty days from the date of announcing the final merger in local newspapers according to the provisions of Article 195. The objector states the subject matter of his objection, the reasons on which it is based, and the specific damage he claims that the merger caused to him.

The minister refers the objections to the Controller to settle them. If the Controller fails to do so for whatever reason within 30 days from the date on which the objections were referred to him, the objecting party has the right to resort to the court.

Article 204 entitles shareholders to oblige the company to purchase their shares when the conditions below are met:

- a. The shareholder has the right to vote for the merger proposal.
- b. Shareholders decide to approve the merger proposal.
- c. The shareholder casts all the votes associated with the shares owned by and registered in his name on the Shareholders’ Register against the merger proposal, or the shareholder does not sign the decision on approval of the merger proposal when the decision is made in pursuance of the provisions of this Law.

Article 205 of the Draft Law provides:

- a. The shareholder, who has the right to oblige the company to purchase his shares according to the article above, may send a written notice to the joint stock company (Fayyad, 2012), stating his wish to do so, within fifteen days from the date of making the decision at the general assembly meeting.

- b. The board of directors, within a period of thirty days from receiving the notice mentioned under the previous paragraph, is bound to make one of the following decisions:
 1. Approve that the joint stock company purchase the shares.
 2. Devise a particular arrangement to ensure that another person agree to purchase the shares
 3. Submitting an application to the Control Department for a decision on exemption.²³
 4. Work – before the procedures in question is taken – towards cancelling the general assembly’s decision or issuing a proper decision to not take the procedure in question, as the occasion may be.
 5. In all cases, the board of directors is bound to send a written notice to the shareholder, including the decision it makes in accordance with this paragraph.

Article 206 obliges that the damage caused to shareholders of the merged company be reversed:

- a. If the merger causes damage to a shareholder of the merged company... the Controller may – based on an application submitted to him by such person before the merger takes place – issue the decision he deems fit regarding the merger proposal. This includes issuing a decision:
 1. Considering the merger ineffective.
 2. Modifying the merger proposal in the manner he deems fit.
 3. Obliging the company or its board of directors to reconsider the merger proposal, wholly or partly.
- b. The Controller may issue the decision under the previous paragraph when the conditions he deems fit are met.
- c. The Controller’s decision under paragraph (b) above may be appealed before the competent court.

Secondly, the withdrawal of objecting partners or shareholders is not regulated by, *inter alia*, the French and Jordanian legislators. However, the fact that this issue is not addressed does not mean that partners are bound to continue their partnership in spite of their objection to, and dissatisfaction with, the decision on merger. It leaves the door open to withdraw from the company. They may not be forced to be partners in a merging or new company, other than that they started their investments in (Ismail, 1986).

1. French Law

The French Law does not recognise the right of partners or shareholders to withdraw from the company and recover the value of their shares in the case of merger. The French legislator does not oblige the company to purchase the interests or shares of persons opting for withdrawal, nor does it force the company to assess their value relative to its actual assets. If partners or shareholders insist on

²³Article 382 of the 2005 Draft Law provides: “(a) The notified joint stock company may submit an application to the Control Department for a decision, exempting it from the obligation to purchase the shares in the following cases: (1) If the purchase will cause severe damage to the joint stock company; (2) if the joint stock company is incapable of funding the purchase; and (3) if obliging the joint stock company to purchase the shares is inconsistent with the rules of equity. (b) Based on the application submitted according to this article, the Control Department may make a decision, exempting the joint stock company from the obligation to purchase the shares, or it makes any other decision it deems fit, including (1) invalidating the general assembly’s decision; (2) obliging the joint stock company to take, or not to take, any measure it states on the decision; (3) obliging the joint stock company to pay compensation to affected shareholders; (4) placing the joint stock company in the liquidation process; and (5) postponing implementation of the obligation to purchase the shares by the joint stock company. (c) The Control Department may not issue its decision under the paragraph above on the basis of any of the two reasons stated under clauses (1) and (2) of paragraph (a) of this article, unless it is convinced that the joint stock company has made a reasonable effort to find another person to purchase the shares.

withdrawal, their rights are valued by the prices of shares at the stock exchange at the time of the offer for sale. Issued by the majority vote prescribed by law or the memorandum of association or articles of association of each company entering the merger, the decision on merger is binding on all shareholders, both proponents and opponents. The minority should comply with the majority's decision (Al-Saghir, 2016; Al-Masri, 1986; Mihrez, 2004). Thus, the objector is left with one of two options. He can comply with the majority's decision on merger and stay in the merging or new company. Otherwise, he can withdraw from the company by selling their shares at the stock exchange at the current sale price as long as the law or memorandum of association does not place restrictions on the trading of shares. The objector may sell his shares at the time he deems fit. A new shareholder can join the company without compromising the capital (Abu Zeinah, 2012).

2. Jordanian Law

The 1997 Jordanian Company does not oblige the merging or new company to purchase the shares or interests of those who refuse the decision on merger at the market price. It suffices with allowing the objectors to challenge invalidity of the decision on merger. If this outcome is not achieved, the objector to merger can sell his shares or interests by the legally prescribed methods.

The Law allows the partner to object to the merger. The objection is submitted to the minister. The objector must state the reasons of objection and describe the damage he claims was caused to him as a result of the decision on merger. An objection without a statement of reasons is not admitted (Basbous, 2010). The minister refers the objection to the Controller to settle or refer it to court. If the Controller cannot settle the dispute, the objector has the right to resort to court to adjudicate the objection.

The Jordanian legislator's approach is criticised, however. Some scholars believe that the court must have the jurisdiction to examine and dispose the objection (Ismail, 1986).

3.4 Appeal against the Decision on Merger

The decision on merger is supposed to be legally valid; i.e. issued by the extraordinary general assembly or partners – as the occasion may be – in a valid session, within the limits of its powers, and following the procedures provided by the company's articles of association. The decision may not violate public order, nor may it involve fraud or forgery of papers or documents, on the basis of which the general assembly issues it. Additionally, the decision may not be issued under the threat of, for example, declaring the company bankrupt.

Thus, if the decision on merger is made in violation of the law, any partner or shareholder may institute a case before the competent court, requesting that the merger be invalidated.

3.4.1 Egyptian Law

Article 76 of the 1981 Egyptian Company Law provides that “[w]ithout prejudice to the rights of *bona fide* third parties, any decision issued by the general assembly in violation of the provisions of the law or the company's bylaws shall be void. Likewise, any decision issued in favour of, or causes damage to, a certain category of shareholders, or brings particular benefit to members of the board of directors or others, in disregard of the company's interests, shall be void. In this case, invalidation may only be requested by the shareholders who object to the decision on the meeting minutes, or those who were absent by an admissible reason. The relevant management body may represent them in the application for invalidation if they present serious reasons.

The ruling on invalidation shall render the decision ineffective for all shareholders. The board of directors must publish a summary of the ruling in a local newspaper as well as in the company register.

The invalidation case shall lapse one year from the date of issuing the decision. Institution of the case shall not result in the stay of execution of the decision unless the court thus orders. Hence, the appeal shall not be used by the minority as a tool to impede the company's activity.”

3.4.2 Jordanian Law and Palestinian Draft Law

Article 235 of the 1997 Jordanian Company Law and Article 199 of the 2016 Palestinian Draft Company Law state the duration and causes of the appeal against merger, which contravenes the law and bylaws: “If the merger does not observe any of the provisions of this Law, or should the merger contradict public order, any interested party may file a case before the court, contesting the merger, provided that this takes place within sixty days from the date of announcing the final merger, and provided that the plaintiff indicates the reasons on which he based his case, particularly the following:

- a. Should it become evident that there are deficiencies which invalidate the merger agreement or should there be a substantial and clear discrepancy in the valuation of shareholder rights.
- b. Should the merger involve an abuse of rights, or should it aim to achieve a direct personal interest to the board of directors of any of the merging companies, or to the majority of shareholders in one of the companies at the expense of the rights of the minority.
- c. Should the merger involve deceit or fraud, or should the merger cause damage to the creditors.
- d. Should the merger lead to a monopoly, or is preceded by a monopoly, and it becomes evident that it causes damage to the public economic interest.

These are the same reasons, based on which an objection may be filed to the minister. However, the objector is not required to use an administrative objection before he resorts to the court. The 60-day period reflects a statute of limitations; it is neither ceased nor interrupted (Abu Zeinah, 2012).²⁴

Article 236 the 1997 Jordanian Company Law also provides that the “appeal against validity of the merger shall not suspend its implementation until a court decision is rendered, ruling for invalidation. The court may, when it considers the case on invalidity, determine, *sua sponte*, a respite to adjust the causes that led to the appeal against invalidity. It shall also be entitled to dismiss the request for invalidation if the concerned party adjusts the positions before the ruling is pronounced”.

Albeit with a different drafting style, Article 200 of the Palestinian 2016 Draft Company Law quotes the same provisions above: “a definitive court decision on invalidation shall be rendered... a period is set for taking certain procedures to adjust the causes”.²⁵

3.4.3. Kuwaiti Law

Article 220 of the Kuwait Company Law provides that “[e]ach shareholder may institute a case on the invalidity of any decision of the board of directors or the ordinary or extraordinary general assembly, which is in violation of the law or the company’s memorandum of association, or if it is intended to causing damage to the interests of the company. Compensation may be claimed if necessary. The case on invalidity shall be dismissed two months from the date, on which the decision of the general assembly is made or the shareholder is aware of the board of directors’ decision.

Decisions of the ordinary and extraordinary general assemblies, which prejudice the minority rights, may be appealed. The appeal shall be filed by a number of the company shareholders, who own fifteen percent of the issued capital of the company and who have not agreed to such decisions. The case shall be dismissed two months from the date of the general assembly’ decision. In such case, the court may uphold, modify or annul the decisions, or postpone their implementation until an appropriate settlement is made to purchase the shares of the objecting parties, provided that such shares are not purchased from the company's capital.”

²⁴ This corresponds to Articles 212 and 213 of the 2010 Draft Company Law.

²⁵ Article 214 of the 2010 Draft Law includes the same provisions.

3.4.4. Emirati Law

According to Article 170 of the Emirati Company Law No. 2 of 2015:

1. Without prejudice to the rights of a *bona fide* third party, any decision passed in contravention of the provisions of this Law, the memorandum of association or articles of association of the company or for or against a certain category of shareholders or to bring a special benefit to the related parties or others without consideration of the interest of the company shall be invalid.
2. Ruling such invalidation shall make the decision void *ab initio* in respect of all the shareholders.
3. The board of directors shall publish the invalidation judgment in two daily local newspapers, one of them issued in Arabic.
4. The invalidation lawsuit shall be time barred after 60 (sixty) days from the date of issuance of the contested decision. Filing the case shall not prevent the execution of the decision, unless the competent court orders otherwise.

Article 191 of the Law regulates suspension of the general assembly's decision:

1. At the request of the shareholders who hold a percentage of at least 5 percent of the shares of the company, the Authority may issue a decision to suspend the execution of the decisions passed by the general assembly of the company to the detriment of the shareholders or in favour of a certain category of the shareholders or to bring a special benefit to the members of the board or others whenever the grounds of the request are serious.
2. A request to suspend the execution of the decisions of the general assembly shall not be acceptable upon the expiry of 3 (three) working days from the date of such decisions.
3. The concerned parties shall institute the case to annul such decisions before the competent court and notify the Authority with a copy thereof within 5 (five) days from the date of the decision suspending the execution of the decisions of the general assembly, otherwise the suspension shall be void *ab initio*.
4. The court shall consider the case to annul the decisions of the general assembly, and may order, as a matter of urgency, to suspend the execution of the decision by the Authority at the request of the adversary party until the conclusion of the merits of the case.

4. Conclusion

To cope with fierce competition between companies, merger is a legal tool that has been widely used over the past two decades in the context of economic globalisation.

This paper observes the following about the impact of merger on partners:

1. Company merger is a tool of economic concentration and conversion of SMEs into large-scale corporations. Merged companies wish to collaborate and achieve integration by consolidating production tools to support competitiveness, increase productivity, introduce new products, improve the quality of goods, and reduce production cost and prices. Mergers also contribute to enhancing standards of living, boost national economy, and yield greater profitability for shareholders. By contrast, companies desire to control and exercise monopoly, negatively reflecting on the quality, prices, and availability of goods. It also disrupts SME emergence and continuity, whereby it is an unfavourable practice.
2. In Palestine, the Company Law No. 12 of 1964 in force in the West Bank, as well as the Company Laws of 1929 and 1930 operative in the Gaza Strip, do not provide a detailed account of merger. As these laws are outdated, companies wishing to merge apply the process prescribed by the Jordanian Company Law No. 22 of 1997.

3. According to its definition and relevant regulations, merger is of two main types: merger through absorption, and merger through consolidation.
4. Merger as per management intervention can be either amicable (voluntary) or compulsory (involuntary).
5. As a rule, the 2016 Draft Company Law restricts merger to companies of a single type. This means that merger can involve two partnerships or joint stock companies. Accordingly, two companies of different forms may not merge; e.g. a partnership (general partnership) with a joint stock company. The difference between both is substantial and affects the rights of partners or stockholders.
6. The 2016 Draft Company Law stipulates that “[t]he objectives of any of the companies wishing to merge must be identical or complementary”. Accordingly, merger can only take place between companies with identical or complementary objectives. In this case, merger reflects a modification of the objective of the merged company. If a company wishes to merge with another of a different objective, it must, ab initio, modify its memorandum of association and articles of association based on a decision from the extraordinary general assembly for reasons to be approved by the competent management body. By contrast, the Emirati Company Law No. 2 of 2015 and Kuwait Company No. 1 of 2016 do not require that the objective of companies wishing to merge be identical or complementary.
7. According to the provisions of comparative laws, the merged companies’ assets and liabilities which are transferred to the merging or new company are considered as contributions in kind. Hence, the value of the merged company’s shares is assessed in line with the rules of valuating contributions in kind.
8. Comparative legislation provides two approaches to addressing partners’ objection to the decision on merger, either at the merging or merged company, potential withdrawal from the company, and refunding of the value of shares. Firstly, partners’ withdrawal is regulated by clear, explicit provisions, which protect the rights of shareholders, who object to the merger. This approach is embraced by, inter alia, the Egyptian, Emirati, Kuwait, and Palestinian legislators. **Secondly**, the withdrawal of objecting partners or shareholders is not regulated by, *inter alia*, the French and Jordanian legislators.

Based on these main findings, the paper recommends the following:

1. Competent Palestinian authorities are advised to enact modern and detailed laws and regulations, particularly on merger, which is briefly governed by outdated commercial laws in force in the West Bank and Gaza Strip. Rules and provisions of merger need to be concisely and clearly regulated, furnishing an opportunity to interested companies to proceed with merger. This holds significant positive value for the national economy.
2. Between 2005 and 2016, a set of regulations were developed to govern companies in general, and merger in particular. However, these were neither approved nor enforced in line with applicable Palestinian norms. Essentially, regulations should be approved and put into effect as practically as possible. Otherwise, the effective Company Law should be amended. This plays a crucial role in facilitating merger for interested companies.
3. In relation to valuating shares of the partners or shareholders of companies participating in merger, the researcher is of the view that more than one criterion of needs to be adopted in the valuation process. The exchange rate should not be restricted nor assessed by shareholders. The share price will eventually be a compromise between negotiating companies.

4. In the case of merger, based on general rules, the legislator will ensure protection of the rights of the weaker shareholders to avoid domination of powerful parties.
5. Apart from general rules, third parties' rights which might be affected by the merger process will be identified. Merged companies will personally address all clients, assuring that acquired rights will be maintained and recognised.

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