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## Acquisition of shares: Abuse of dominance in market

### INTRODUCTION

Since ancient times, the various political systems have disregarded the concentration of economic power. Legislations to curb this phenomenon have been put in practice by different governments in the garb of competition laws. Most competition laws cover three areas namely, anti-competitive agreements, abuse of dominant position and M&A activity. Abuse of dominance under the Indian competition law is covered under 3 principal statutes: (i) Section 4 of the Competition Act, 2002; (ii) Section 2(d) of the Monopolies and Restrictive Trade Practices Act, 1969 (“**MRTP Act**”) which defines a *dominant undertaking*; and (iii) Sections 108A to 108I of the Companies Act, 1956 (“**Act**”) impose certain restrictions on the acquisition and transfer of shares by or in favour of a dominant undertaking.

A word of caution at the outset: the Competition Act has not come into full force yet. Only some provisions including definitions clause, formation of the Competition Commission of India (“**CCI**”) and procedural aspects are implemented. The CCI has still not been fully constituted. The Indian Parliament approved the Competition (Amendment) Bill, 2007 as of September 11, 2007. Given the litigious history on the constitution of the CCI there is apprehension that this Bill may lead to another round of litigation which may stall the eventual implementation. Till the Competition Act comes into full force, the MRTP Act will remain operative along with relevant provisions of the Act.

The prime focus of this newsletter is to examine the concept of abuse of dominant position in the Indian context and methods to curb it. It also analyzes the restrictions imposed on acquisition of shares of/by dominant undertakings and how these restrictions help in curbing abuse of dominance.

#### 1. What is a dominant undertaking?

Defined in the MRTP Act<sup>1</sup>, “*dominant undertaking*” is an undertaking which (1) by itself or along with inter-connected undertakings produces, supplies, distributes or otherwise controls at least one-fourth of the total goods that are produced, supplied or distributed in India or any substantial part thereof; or (2) provides or otherwise controls at least one-fourth of any services that are rendered in India or any substantial part thereof. The emphasis of the antitrust laws in India is mainly on the prohibition of restrictive and unfair trade practices and the law is designed to guard against different aspects of market imperfections leading to creation of monopolies. Thus, where a transaction has the effect of creating a dominant undertaking in India post-acquisition i.e. with 25% of the market share, prior approval from the Central Government would be required. The important factor is that only the Indian operations and not global activities are to be considered to judge as to whether a company falls under the definition of a “*dominant undertaking*” or not.

This definition should be read in conjunction with section 4 of the Competition Act which defines dominant position as a position of strength, enjoyed by an enterprise in the relevant market<sup>2</sup> in India which enables it to operate independently of the competitive forces in the relevant market or to affect its competitors or consumers or the relevant market in its favour.<sup>3</sup> Under the Competition Act, the CCI will determine the relevant market taking into account

<sup>1</sup> Section 2(d) of MRTP Act.

<sup>2</sup> Under Section 2(r) of the Competition Act, “relevant market” means the market which may be determined by the Commission with reference to the relevant product market or the relevant geographic market or with reference to both.

<sup>3</sup> Explanation (a) to section 4 of Competition Act.

a host of factors like regulatory trade barriers, national procurement policies, physical characteristics or end-use of goods, price of goods, consumer preferences, classification of industrial products etc. This is in consonance with the competition laws of many developed countries which seek to define a dominant undertaking more subjectively.

The definition renders it difficult to determine whether an undertaking is dominant or not. Certain determinative factors include the average annual supply, distribution or production of goods in the undertaking during the period of three years immediately preceding the year in which the position has to be determined.<sup>4</sup> Market share of an undertaking has a direct influence on its position of strength. However, in a dynamic changing economic environment, it is very difficult to define dominance. There is no single objective market share criteria that can be blindly used as a test of dominance.

## 2. Abuse of dominance vis-à-vis acquisition of shares

### 2.1 Abuse of dominance in Competition Act

With the object of promoting fair competition and protecting consumer interests the Competition Act has stated that an enterprise should not abuse its dominant position. The factors<sup>5</sup> which constitute abuse by a dominant undertaking are:

(i) Charging prices or imposing terms and conditions which are unjustifiably burdensome or which impede market access by other competitors or induce them to abandon their operations. Offering discounts at an exceedingly high rate or refusal to supply by imposing discriminatory conditions on purchase or sale of goods or services may be considered abuse. An example is where a dominant undertaking applies prices below those normally needed to cover costs and provide a profit and where the aim is to eliminate competitors or make market entry more difficult. However, adopting certain conditions or prices to meet the competition would not be an act of abuse.

(ii) Limiting or restricting the production of goods or provision of services or otherwise influencing the market including the technical or scientific development relating to the goods and services to the prejudice of the consumers would constitute an abuse of power. Exclusive dealing agreements and similar practices that tie up suppliers and distribution networks can be termed as one such practice which restricts production and the market.

(iii) Engaging in practices which may lead to denial of market access to capable undertakings will be an abuse of position to the detriment of the society at large.

(iv) Execution of contracts that are subject to acceptance of supplementary obligations by other parties which have no connection with the subject of the contract. For example, a tie-in clause may be included to compel a purchaser to purchase an additional product which does not have a natural or reasonable connection with the first product.

(v) Using a dominant position in one relevant market to enter into, or protect other relevant market also constitutes abuse.

Where a dominant undertaking abuses its dominance then the CCI, suo moto or on any complaint or reference, may pass an order to discontinue such a practice. The CCI also has the power to impose a penalty of up to 10% of the average turnover for the three preceding financial years.<sup>6</sup>

### 2.2 Restriction on acquisition of shares

Companies frequently acquire shares or assets of other undertakings operating in the same field to increase their market share. An unregulated practice in this regard can lead to abuse. Therefore, the Act has provided certain safeguards that are discussed below. Sections 108A to 108F apply to dominant undertakings, their owners or undertakings/individuals capable of becoming a dominant undertaking by virtue of an acquisition of shares.<sup>7</sup> Under these provisions, for some particular

<sup>4</sup> Explanation V and VI to section 2(d) of MRTP Act.

<sup>5</sup> Section 4(2) of Competition Act.

<sup>6</sup> Section 27 of the Competition Act.

<sup>7</sup> Section 108G of the Act.

acquisitions prior approval of the Central Government is required.

If the acquirer of shares of a public company is a dominant undertaking or an owner thereof or by virtue of such acquisition becomes one, there would be concentration of economic power which may eventually lead to abuse. The Central Government scrutinizes acquisition of shares of a public company or a private company which is a subsidiary of a public company. If through such an acquisition, the acquirer intends to hold more than 25% of the equity share capital of the target company, prior approval of the Central Government is essential.<sup>8</sup>

No specific parameters have been laid down on which the Government must base its decision which is generally granted in 60 days after the application is submitted. Therefore, the Government is free to exercise discretion while examining the following factors:

- (1) Nature of the undertaking: The main aspect to be considered is whether the acquirer is a dominant undertaking or whether the acquirer, by virtue of the acquisition, becomes a dominant undertaking.
- (2) Purpose of acquisition: The intention of the acquirers is critical to determine whether the interests of the target company is taken into account or not.
- (3) Impact of the acquisition: The acquisition should not adversely effect competition and should not be prejudicial to the interest of the target company or the public.

### 2.3 *Restriction on transfer of equity shares*

If a body corporate holds more than 10% of the nominal value of the subscribed equity share capital of another company (includes a foreign company having an established place of business in India<sup>9</sup>) and intends to transfer its shares, it has to notify the Central Government.<sup>10</sup> Such a notification is necessary only when the transfer involves a dominant undertaking. The Government will examine the details of transfer and if the transfer impacts the

constitution of the Board prejudicially, the Government will issue appropriate directions accordingly.

### 2.4 *Restriction on voting power*

Sometimes, transfer of shares of a company leads to change in its controlling interest. In common parlance, this is understood as control of voting power above 50% or the ownership of more than 50% of the equity share capital. Preference shares of a company with limited voting rights may also be taken into account while determining the “controlling interest.” As an endeavor to curb abuse of dominance, such transfers are prohibited under the Act. However, if such a transfer has already been registered in the company, the Central Government can suo moto or on receipt of any complaint from affected persons (e.g. shareholders) direct the company to freeze the voting rights of the transferee, its nominees or proxies.<sup>11</sup>

The aim of these provisions is to curb the concentration of economic power and abuse of dominance. In *Karamsad Investments Ltd, GMM Pfandler Limited, Karamsad Securities (P) Ltd. V Nile Ltd & Ors.*<sup>12</sup> the Court observed that “the need to control acquisition or transfers by the owners of dominant undertakings arose as those undertakings could seriously affect the supply of materials to the society and also perhaps to see that the control of industrial undertakings does not go into the hands of inexperienced and inefficient lot as the same might seriously affect the availability of goods or services to the society.”

Size is itself an earmark of monopoly power because size carries with it an opportunity for abuse.<sup>13</sup> The increase of dominance consequent upon acquisition of shares is, thus, regulated by the provisions discussed in sections 2.2, 2.3 and this section.

<sup>8</sup> Section 108A of the Act.

<sup>9</sup> Section 108C of the Act.

<sup>10</sup> Section 108B (1) of the Act.

<sup>11</sup> Section 108D of the Act.

<sup>12</sup> [2002] 108 CompCas 58 (AP).

<sup>13</sup> Colgate Palmolive India (P) Ltd. Vs. Union of India and Ors.

### 3. Penal provisions on contravention

A finding of an abuse of dominance can lead to a number of consequences ranging from the imposition of fines to imprisonment for officers<sup>14</sup> of the company. Transfers in contravention of the statutory provisions will attract a monetary fine of Rs. 50,000 (equivalent to \$1250) or imprisonment extending to 3-5 years.

Under the Competition Act, the CCI will have the power to regulate any contravention if a consumer or an aggrieved party approaches it or when the Central Government makes any reference to it. The power of the CCI, however, is dependent on the successful implementation of the Competition (Amendment) Bill, 2007. Till then recourse will be under the Act.

### CONCLUSION

Fair play among the market forces is very important to establish a sustainable and healthy economy. The Act attempts to keep unfair practices at bay by curtailing the liberty on acquisition of shares. The Central Government has been empowered accordingly. However, determination of dominance is difficult and these provisions are triggered on rare occasions. While exercising its power the Government keeps in mind that dominance should be judiciously exercised to facilitate healthy competition which do not adversely affect the public at large. (*Mondakini Mahanta*)

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<sup>14</sup> Under Section 2(30) “officer” includes any director, manager or the secretary of a company.



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