COMPETITION COMMISSION TAKES HOLD OF M&A ACTIVITY

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BACKGROUND

The Competition Commission of India ("CCI") stepped into a new regulatory role with the release of the CCI (Procedure in regard to transaction of business relating to combination) Regulations, 2011 ("Combination Regulations") on May 11, 2011. This was a sequential step to the notification of combination provisions (sections 5 and 6) of the Competition Act, 2002 ("Act") issued on March 4, 2011. As a result, the CCI is now equipped with a complete set of substantive and procedural rules to scrutinize mergers and acquisitions which cross the prescribed assets or turnover based thresholds. Effective June 1, 2011, no transaction that is likely to have an "appreciable adverse effect on competition in relevant market in India" can be consummated without a prior approval from the CCI. After implementing the Combination Regulations for almost nine months, CCI has brought some significant changes through the CCI (Procedure in regard to transaction of business relating to combination) Amendment Regulations, 2012 ("Combination Amendment Regulations") on February 23, 2012.

This article analyses this new regulatory framework, highlighting the potential impact of the Combination Regulations as well as the Combination Amendment Regulations on mergers and acquisitions in India.

TRANSACTIONS COVERED UNDER THE COMPETITION ACT

Section 5 of the Act has been very broadly cast and defines "combination" to include an acquisition of shares, voting rights, assets, or control of an enterprise or merger or amalgamations of enterprises. Essentially, all transactions crossing the following prescribed monetary threshold would require a prior notification to the CCI. All figures are approximations.

Threshold referencing India:

- Acquirer and target having assets worth $330 million or turnover of $1 billion.
- Acquiring "group" and target having assets worth $1.33 billion or turnover of $4 billion.

Threshold with world-wide reference:

- Acquirer and target having assets worth $0.75 billion (out of which at least $167 million in India) or turnover of $2.25 billion (out of which at least $500 million in India).
- Acquiring "group" and target having assets worth $3 billion (out of which at least $167 million in India) or turnover of $9 billion (out of which at least $500 million in India).

Interestingly, on March 4, 2011 (the same date on which the combination provisions under the Act were notified) the government also issued an array of investor friendly notifications, including: (i) an increase of 50% in asset/turnover based monetary thresholds to reach the present levels mentioned above; (ii) amendment to the definition of "group" whereby groups exercising less than 50% of voting rights in the other enterprise are exempt from the purview of the Act and Combination Regulations for a period of five years starting June 1, 2011; and (iii) a similar exemption of five years to enterprises having assets below $56 million or a turnover of not more than $167 million.

In our view, the monetary criterion alone is not appropriate to define the contours of a combination in

every case. But, if financial triggers are attracted, that would compel parties to notify even small combinations having no appreciable adverse effect on competition, just on account of their size. On the other hand, dilution of the definition of "group" is a welcome move as it would ensure safe harbor for many more transactions involving group companies, than would have been the case with the earlier threshold of 26%.

PROCESS OF FILING NOTICE WITH CCI

Trigger Point: 30 days!

The Act mandates that a notice is to be filed with CCI within 30 days of an approval by the board of directors in case of intended mergers or amalgamations or execution of any agreement or "other document" in case of acquisitions. According to the definition inserted now in the Combination Regulations, "other document" will mean any "binding document" conveying or exhibiting the intention to acquire. In the context of "hostile takeovers," mere execution of such a document by the acquirer itself would trigger the deadline of 30 days. The CCI will not interfere with transitory transactions where the relevant trigger event has occurred before June 1, 2011.

Form and fee

The CCI is to be normally notified in Form I (a short form prescribing entries with respect to products/services, market share, etc.) with a stipulated fee of approximately $20,000. This amount is a result of the Combination Amendment Regulations, whereby the fees has been increased almost 20 times. Regulation 5(2) provided an inclusive list of transactions, where in most cases only Form I (Part I) was required to be filed. The recent amendment deleted the reference to transactions for which Form I (Part I) had to be filed. This implies that it is now mandatory to file the complete Form I (Part I and Part II) in every instance.

Parties to the transaction also have an option to file Form II with a prescribed fee of approximately $80,000. The amended regulations also provide for some instance where filing of Form II is recommended. These recommendations include combinations involving horizontally or vertically aligned entities with combined market share of more than 15% or 25% in each case. Form II is longer and contains detailed requests for information regarding (among other things) relevant market structure, demand and supply in the market, entry and exit conditions. It is apparent that the type of detailed information required by the CCI would necessitate filing certain confidential information that could, eventually, be leaked out to the market and competitors and may not be in the best interest of the transacting parties. In order to claim confidentiality, parties are required to formally request and specify cogent reasons, including the implications on the business for protecting confidentiality regarding any information supplied to the CCI. Complete discretion rests with the CCI in granting any such request for confidentiality. Unless addressed properly, this could become a thorny issue as there will be inevitable reluctance to share confidential information without adequate security that it shall be preserved.

Any acquisition by a public financial institution, foreign institutional investor, bank or venture capital fund, pursuant to a covenant under a loan or investment agreement does not require a prior approval from the CCI. Such bodies are just required to notify the CCI in a simplified Form III along with a certified copy of the executed loan or investment agreement, without any fee, in seven days post such acquisition. The Combination Amendment Regulations have inserted a new sub regulation whereby CCI may permit filing of Form III even beyond the seven day period. This is inconsistent with section 6(5) of the Act, which specifically limits the filing period to seven days.




Onus of filing notice

In the acquisition of shares, voting rights, or control in an enterprise, the acquirer is under an obligation to file the relevant form with the CCI. In case of a merger or amalgamation, the transacting parties are required to jointly file the appropriate form with the CCI. The recent amendment has also authorized the company secretary of the company, duly authorized by its board, to do filing with the CCI in the aforementioned cases. In a scenario, where the intended objective of a business transaction is achieved through a series of individual transactions (inter–connected or inter–dependant), one or more of which may amount to a combination, the Combination Regulations provide that a single notice can be filed with the CCI. For example, in the recently proposed acquisition of UTV Software Communications by Walt Disney Company , the complete transaction as proposed by the parties involved two steps: firstly, acquisition of shares held by public shareholders through a delisting offer under the Delisting Regulations, 2009 and, secondly, a subsequent acquisition from promoters. The acquirer filed a single notice in Form I and CCI approved the entire transaction through an order dated August 25, 2011.

Failure to file any of the prescribed forms can result in a penalty of up to 1% of the combined assets or turnover of the combined entity, whichever is higher, on the enterprise(s) that is under the obligation to file the relevant form in a particular case.

EVALUATION OF PROPOSALS BY THE CCI

Prima facie opinion: the CCI is obligated to make a prima facie opinion regarding whether there will be an appreciable adverse effect of the proposed transaction on the Indian market within 30 days of filing the notice. There were apprehensions in the industry on the competence of the CCI to approve proposed combinations within the short span of 30 days. However, on July 26, 2011, the CCI came out with its first order approving an acquisition by Reliance Industries Limited and Reliance Industrial Infrastructure Limited of a 74% stake held by the Bharti Group in each of two joint venture insurance companies, namely Bharti AXA Life Insurance and Bharti AXA General Insurance. The order approving the transaction was passed in a record time of just 18 days. Further, the competition regulator has already given its nod to twenty seven more proposed transactions, and most of them well within the timeframe of 30 days. Certainly, the CCI has started out well and it remains to be seen if such time frames shall be maintained going forward.

Detailed Investigations: If unsatisfied at the preliminary stage, the CCI could go for a detailed investigation, and, in such a case, would endeavor to pass an order within 180 days as opposed to 210 days. It is noteworthy that despite the global concern there is no commitment to approve within the reduced period of 180 days. The obligation of the CCI is merely confined to best efforts. There is also a provision for deemed approval in case the CCI does not pass an order within 210 days.

It remains unclear when the clock will start and the 210-day period will commence because chances are that the CCI will seek additional clarifications/information and that process could prove to be time consuming. Only time will tell whether the 210-day period will be extended or curtailed and respected. So far, the prognosis appears to be encouraging.

Another conundrum remains in case of takeovers or the substantial acquisition of shares of listed entities. In case parties execute an agreement to acquire more than 25% of voting rights in a listed company, this would trigger the "open offer" obligation under the Takeover Regulations. At the same time, notice would also need to be filed with the CCI under the Combination Regulations. This may lead the

transacting parties embroiled between the competition and securities law, as they might not be able to complete the open offer within the time stipulated under the Takeover Regulations for want of clearance from the CCI which can, in turn, lead to payment of interest on the offer price to tendering shareholders at a rate decided by the Securities and Exchange Board of India ("SEBI").

TRANSACTIONS THAT ARE NOT REQUIRED TO BE NOTIFIED

The Regulations under Schedule I enumerate a list of transactions that are unlikely to cause any appreciable adverse effect on competition in India. The list includes:

- An acquisition of shares or voting rights of an enterprise solely for the purpose of investment or in the ordinary course of business. In this case, the total share holding or voting rights of the acquirer should not exceed 25% and should not lead to the acquisition of control over the enterprise. The limit has been recently increased from 15% to 25% through the Combination Amendment Regulations. This amendment ensures that the threshold of 25% is in consonance with the new Takeover Regulations announced on October 22, 2011.

- Any consolidation of holding where the acquirer already has more than 50% of share holding or voting rights in the target except when such acquisition leads to sole control from joint control. The Combination Regulations are silent upon any acquisition or consolidation of shareholding between 25–50%. This is in contrast to the new Takeover Regulations, which allow the consolidation of shareholding in a listed entity through the "creeping acquisition" of 5% in a financial year without getting indented by open offer requirements, in case the acquirer holds 25% or more in the target and until he transgresses the maximum permissible non-public shareholding limit of 75%. The Combination Regulations, on the other hand, do not provide for such leverage. A clarification on this particular point is very much required, as an acquisition of 5% of voting rights in a financial year in cases where it does result in change of "control" in an enterprise, would not cause any significant appreciable adverse effect on competition in the relevant market and should be exempted.

- An acquisition of stock-in-trade, raw material, stores, etc. in ordinary course of business.

- An acquisition of bonus or right shares not leading to control. The recent amendment has extended this exemption to buy back of shares as well.

- Intra-group acquisitions are exempted. The Combination Amendment Regulations have now specifically exempted intra-group mergers or amalgamation between (i) wholly owned subsidiaries of the parent company inter-se or (ii) wholly owned subsidiary with the parent company. This change will facilitate consolidation of group companies with lesser statutory compliance. Further, the erstwhile regulations provided for a definition of "group" while determining any intra-group acquisition. The amendment has curiously deleted this definition leaving stakeholders with little guidance on interpretation of the term "group."

- A combination taking place entirely outside India with "insignificant local nexus" and effects on relevant market in India. Regrettably,

no objectives or parameters are provided to determine "insignificant local nexus."

The Combination Regulations state that these transactions are "ordinarily not likely" to cause an appreciable adverse effect in the relevant market, leaving it on the parties to assess the implication of their proposed combination and make a decision on notifying the CCI.

PRE -MERGER CONSULTATION

The Combination Regulations failed to provide any pre–notification consultation. But, in conformity with international practices and paying regard to the demands from industry, the CCI has recently started a separate mechanism, offering an informal and verbal consultation with the CCI staff by appointment. It is unclear at this stage what assistance the staff would provide, but in essence it could be confined to clarifications or guidance for the completion of forms. The CCI has also upfront clarified that such consultation should not be construed as its opinion and would not have any binding effect on it. At the very least, the CCI staff should review the relevant form and intimate parties of changes, if any, or any additional information/documents that ought to be supplied to avert delays at a later stage.

COMMENT

The combination provisions under the Act have finally gathered full force after being in abeyance for almost a decade. There is some jurisprudence that exists with regard to anti-competitive agreements and abuse of dominant position in India, and now specific merger control regulations are a step in the right direction for healthier competition in the market. The industry anticipates a slowdown in the mergers and acquisitions due to the time the CCI will take in issuing its approval. The CCI is required to make sure that it strengthens the pre-merger consultation mechanism and regularly comes out with clarifications and amendments, as the recent one, to remove ambiguities. Nonetheless, the CCI has gathered the right momentum by approving most of the initial combination proposals within the stipulated 30 days, and this could be the harbinger of favourable and efficient regulatory action in days to come.

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