INDIAN MERGER CONTROL – ONE STEP FORWARD, TWO STEPS BACK

By Naval Satarawala Chopra & Aparna Mehra [1]

I. INTRODUCTION

The merger control regime in India has been in place for the last five years. When the regime was introduced, practitioners and academics feared that the approval process adopted by the Competition Commission of India ("CCI"), which allowed a 210 day review process, would delay transactions and be costly. However, the CCI has, to a large extent, allayed such fears by clearing close to 350 merger notifications within a much shorter time-frame[2] than expected. That's the good news!

From the initial pragmatic "light touch" approach, the CCI is perceived now to be taking a more aggressive approach, especially in interpreting exemptions issued by both the Government of India and the CCI itself. Not only does this approach defeat the purpose of these exemptions, but given the personnel shortage at the CCI, it has resulted in delays. Further, while the CCI has amended its regulations to simplify the notification process, there remains procedural drawbacks that require legislative intervention.

In this paper, we discuss the trends and challenges of the merger control regime in India.

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[1] The authors are Partners in Shardul Amarchand Mangaldas & Co.'s Competition Law Practice. The authors are grateful to Supritha Prodaturi for her assistance in preparing this paper.

[2] On an average, 18-25 calendar days (Source: Annual Report of CCI, 2014-15).

II. KEY ISSUES AND DEVELOPMENTS

A. *Erroneous Interpretation of the Target Exemption*

In order to adopt a "light touch" and to ensure that insignificant transactions are not require notification to the CCI, the Ministry of Corporate Affairs, Government of India, issued and subsequently renewed the *de minimis* target based exemption, pursuant to which, for a period of 5 years until March 3, 2023 (as renewed), transactions where the target has either assets in India less than INR 350 crores (approx. USD $50 million), or turnover in India less than INR 1000 crores (approx. USD $150 million), do not need to be notified to the CCI ("Target Exemption").

Unfortunately, the CCI has interpreted this exemption extremely narrowly. The CCI's position is that, due to the wording of the Target Exemption, it is available only for transactions, acquisitions of shares or assets but not mergers or amalgamations. This artificial distinction makes no sense and it was hoped that the CCI would apply a purposive interpretation of the Target Exemption.

More concerning however is the fact that the CCI considers the "target" (for purposes of determining assets/turnover thresholds) to be limited to an incorporated entity as opposed to a business or division. Therefore, in case of the sale of a business or division, the assets and turnover of the seller as opposed to what is being sold has to be considered. Naturally, this has resulted in some corporations failing to notify transactions and recently the CCI fined Eli Lilly INR 1 crore (approx. USD $150,000), for failing to notify the acquisition of the global veterinary pharmaceutical business of Novartis.[3] There are other cases of such non-compliance which the CCI is currently considering.

This practice is also not in line with international best practices issued by the International Competition Network, which the CCI is a part of. Ironically, if these assets/divisions were housed in a separate legal entity, the transaction would have the benefit of the Target Exemption. Such a form over substance approach is antithetical to the ease of doing business in India and defeats the purpose for which the Target Exemption was introduced in the first place.

The CCI's rationale for this interpretation is that the term "enterprise" used in the Target Exemption and defined in the Competition Act of 2002 (the "Competition Act"), does not include a business or division. This approach would imply that acquisitions of businesses or divisions would not fall within the ambit of the merger control regime, as the requirement to notify is triggered only in case of the "acquisition of one or more enterprises." This would be an equally absurd position but would follow from the CCI's interpretation.

[3] *Eli Lilly/Novartis* (C-2015/07/289)

B. Control

The interpretation of "control" is critical from the perspective of examining whether a transaction may avail the benefit of exemptions. The definition of "control" has always been a sticking point in India and the merger control regime has not been immune to this phenomenon. As a starting point, "control" is defined (rather circuitously) under Section 5 of the Competition Act to include "controlling the affairs or management by (i) one or more enterprises, either jointly or singly, over another enterprise or group; (ii) one or more groups, either jointly or singly, over another group or enterprise."

The CCI, in its limited decisional practice, has interpreted control to mean "the ability to exercise decisive influence over the management or affairs and strategic commercial decisions"[4] of a target enterprise, whether such decisive influence is being exercised by way of a majority shareholding, veto rights (attached to a minority shareholding) or contractual covenants. In its decisions, the CCI has considered the ability to veto (or cause a deadlock in respect of) strategic commercial decisions (such as the annual business plan, budget, recruitment and remuneration of senior management, and opening of new lines of businesses) as sufficient to confer at least joint control.[5]

Accordingly, the guidance from the CCI on the interpretation of "control" under the Competition Act is unhelpful. One of the biggest challenges for parties to transactions in relation to the interpretation of control continues to be the question of how to differentiate mere investor protection rights from those rights which result in a situation of control/joint control.[6] The CCI's general observation is that a case-by-case approach needs to be adopted while assessing "control," which is of limited assistance to parties. In this climate of uncertainty, parties are often required to make a call on whether their acquisition will, or will not, be viewed by the CCI as an acquisition of control.

C. Investment only Exemption

Schedule I of the Competition Commission of India (Procedure in regard to the transaction of Business relating to Combinations) Regulations of 2011 ("Combination Regulations") was introduced to effectively exempt certain types of transactions from the filing requirement, as they are ordinarily unlikely to cause an appreciable adverse effect on competition ("AAEC"). Under the Combination Regulations, transactions falling within the categories listed in Schedule I do not normally require notification to (and prior approval of) the CCI. However, in practice, the CCI has interpreted these very restrictively and have watered down their scope to a large extent.

One of the key exemptions of Schedule I, Item 1, ordinarily "exempts" transactions that involve the acquisition of less than 25 percent shareholding, "solely as an investment" or in the "ordinary course of business," provided it does not result in an acquisition of control. The CCI's interpretation of these terms is again very narrow – the CCI views the acquisition of

[4] See *Independent Media Trust/Network 18* (C-2012/03/47).
[5] See *SPE Holdings/MSM/Grand way and Atlas* (C-2012/06/63).
[6] See *SAAB/Pipavav* (C-2012/11/95).

shares in more than one company, in the same sector, as strategic even if such acquisitions do not involve acquisition of control or are by investment funds. For example, the acquisition by a private equity fund of minority non-controlling shares in more than one company in a particular sector would not benefit from this exemption. In January 2016, the CCI amended Item 1 of Schedule I to include an explanation which clarifies that acquisition of less than 10 percent shares or voting rights would be treated solely as an investment, provided the acquirer (a) has the ability to exercise only ordinary shareholder rights commensurate with their shareholding; (b) is not a member of the board of directors of the target nor has a right or intention to nominate a director in the future; and (c) does not intend to participate in the affairs or management of the target.

The explanation therefore benefits investment companies acquiring an up to 10 percent shareholding in an enterprise even where it already has shareholdings in other enterprises competing with the target. In such a case, the acquisition can be treated "solely as an investment" and made "in the ordinary course of business" and will be exempt from the notification requirement. However, it is not clear whether the CCI would adopt the same position where such an investment company has a pre-existing controlling investment in a target in the same sector.

D. Strict Timeline and Failure to File

The Competition Act has a strict deadline to make a filing with the CCI. If the parties fail to notify a merger within 30 days from the trigger event, or at all, the CCI has the power to impose a penalty of up to one percent of the total worldwide turnover or value of assets, whichever is higher, of the proposed merger. The CCI has used these powers regularly in cases where late filings have been made.

The CCI accepted all late filings made in the first year of operation of the merger control provisions and did not impose any penalties. Penalties have, however, been imposed since then. The CCI imposed a "relatively nominal" penalty of INR 5 lakhs (approx. USD $7,500) for a late filing in *Dewan Housing Finance Corporation Limited/First Blue* (C-2012/11/92), where the parties argued that the reason for the delay in filing was incorrect legal advice.

Last year saw CCI proactively issuing show-cause notices to parties who have, (a) failed to notify a transaction; and (b) consummated the transaction before obtaining an approval from the CCI. The quantum of penalties levied by the CCI for a delayed or no filing has significantly increased in the past year with the CCI levying fines up to a maximum of INR 5 crores (approx. USD $750,000).[7]

While the fines levied by the CCI are a fraction of the amount that they have the power to levy, given the continuing ambiguity in the Indian merger control regime (for example, definition of "control," ability to carve out the Indian leg of a global transaction, availability (or lack) of exemptions), it is hoped that the CCI will be more receptive to accepting mitigating factors and have a consistent approach while levying a penalty.

[7] *GE/Alstom* (C-2015/01/241) and *Piramal/Shriram* (C-2015/02/249).

E. Phase I and Phase II

On receipt of a notification, the CCI is required to form a *prima facie* opinion on whether a merger causes or is likely to cause an AAEC within the relevant market in India within a period of 30 working days. However, if the CCI requires the parties to remove defects in the notification or to provide additional information, it "stops the clock" until the additional information is provided.[8]

Even in relation to non-problematic cases, a detailed scrutiny is adopted by the CCI. The CCI is increasingly contacting customers and competitors as well as third party agencies for information or opinions even during Phase 1 reviews. The increasingly rigorous approach by the CCI means that transaction review timelines have also increased. This results in transactions taking 75-90 days to be approved, even though they ought to be cleared within 30 working days (i.e. approx. 45 calendar days).

In cases where CCI forms a prima facie opinion that a merger is likely to cause, or has caused, an AAEC within the relevant market in India, it is required to issue a show-cause notice to the parties asking for an explanation as to why an investigation in to the merger should not be conducted. Depending on the response received from the parties, the CCI may either direct the Director General to conduct an investigation or perform a detailed investigation, including public scrutiny, on its own.

To date, all cases have been approved in Phase I with the exception of *Sun/Ranbaxy* (C-2014/05/170), *Holcim/Lafarge* (C-2014/07/190) and *PVR/DT* (C-2015/07/288).

There has been an increased use by the CCI of its powers to require remedies to address competition concerns before clearance. The CCI has cleared a number of mergers where parties have voluntarily offered modifications of a behavioral nature, which include reductions in the period of non-compete obligations, giving access to infrastructure or undertaking to comply with competition and other laws.

In all three cases which went to Phase II, the CCI had tailored the remedies to the specific circumstances in each of these cases. Accordingly, it has not followed a "one size fits all" approach. One of the most contentious decision of the CCI was *PVR/DT*, where by a majority of 4-3, the CCI approved a hybrid remedy of divestitures and expansion freezes and rejected a purely behavioral remedy involving price caps and expansions freezes. This demonstrates that the CCI is pushing the envelope on remedies. However, there remain concerns on the use of economics and common antitrust tools in both recognizing and addressing anti-competitive concerns.

F. Invalidation of Notices

Another recent trend is for the CCI to reject notifications after being accepted, for being

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[8] If the CCI reaches out to third parties during Phase I, this time period is extended by 15 working days. Further, where modifications are offered in Phase I, the time period is further extended by 15 days. This is Phase I of the review period.

defective, incomplete or filing the incorrect notification form.[9] Based on publically available information, the CCI rejected a notification filed by *TPG / Manipal Health* (C-2014/12/234), nearly at the end of Phase I, for failure to notify an interconnected (albeit exempt) step, as a result of which the basis for the competitive assessment was found to be incomplete. It is likely that the CCI is taking this approach in other cases too where it finds the information provided by the parties in the notification form to be insufficient or incomplete for undertaking the competitive assessment.

It appears that the CCI has adopted this approach because, unlike other jurisdictions, the statutory review period commences on the day when the notice is filed by the parties and there is no formal pre-acceptance period in which the CCI can assess the level of information being provided by the parties to conduct a meaningful review. Further, in case parties provide additional information which impacts the competitive assessment or if new overlaps are discovered mid-way through the review, the CCI does not want to be disadvantaged by the statutory time limit in conducting a thorough review. In such cases, the CCI requires the parties to re-file a complete notification, without requiring the fee to be paid again.

In practical terms, this has the effect of re-setting the review clock and re-commencing the 210 day statutory review period and this possibility will have to be borne in mind by parties when filing the notification form.

G. Filing Formalities

The officials at the CCI have proved to be rigid in terms of filing formalities and each filing is checked extensively before being accepted. The filing process has proved to be a cumbersome one and parties need to prepare filings with the utmost care. In an extremely welcome step in 2015, the CCI now permits (i) any person authorized by the company to sign the notification without a specific board resolution; and (ii) a declaration to be made on behalf of the notifying party (which does not require notarization and legalization). Additionally, the declaration makes a specific mention of Sections 44 and 45 of the Competition Act which lay down the penalties applicable for submitting false information or omitting to submit material information.

The CCI has recently announced the introduction of an online portal for filing notification forms. However, this system is yet to take off.

III. CONCLUSION

There is an urgent need to amend the Competition Act and the Combination Regulations to remove the ambiguities and issues highlighted above. This is especially important given the Government of India's desire to make India an attractive investment destination.

With its limited staff, the CCI must be commended for its efforts in implementing the merger control regime. However, it is hoped that the CCI will consider the concerns raised by

[9] *GE/Alstom* (C-2015/01/241), *CommScope Inc.* (C-2015/5/275). In case an incorrect form is filed by the parties, the CCI has directed the parties to file Form II within a period of 30 days of the said direction.

various stakeholders and mature into an authority which is focused on analyzing and reviewing transactions which cause AAEC and adopt a more pragmatic approach to transactions where such concerns do not exist. The CCI itself will benefit from such a focused approach with a reduced strain on its resources.