Composite Transactions and market purchases: Supreme Court upholds penalty for gun jumping in Thomas Cook and SCM Soilfert cases

By Ajay Goel & Subodh Prasad Deo (Saikrishna & Associates)[1]

The Supreme Court of India, via two separate judgements passed on 17.08.2018[2], upheld the order of the Competition Commission of India ("CCI") imposing a penalty of INRTen million in the Thomas Cook Case and INRTwenty million in the SCM Soilfert case upon the respective acquirers.

The appeal before the Supreme Court ("S.C.") in the Thomas Cook case was preferred by the CCI against the order the Competition Appellate Tribunal ("COMPAT"), which had struck down the CCI's penalty. Pertinently, the CCI had imposed said penalty due to non-compliance with the provisions of section 6 (2) of the Competition Act, 2002 ("Act") as market purchases transaction, which constituted one part of interconnected and interdependent transactions and was already consummated at the time of notification to the CCI. In the SCM Soilfert case, the acquirers had preferred the appeal before the S.C., as they were aggrieved with the order of COMPAT affirming the penalty order by the CCI on the acquirers due to non-compliance with the provisions of section 6(2) of the Act.

In both cases, the Supreme Court has ruled that the imposition of penalties under section 43A of the Act is on account of a civil obligation and there is no requirement of *mala fide* or intentional breach, as the proceedings are neither criminal nor quasi criminal.

Thomas Cook case[3]:

To give a brief background, pre-merger notification in this case was filed on 14.02.2014 by Thomas Cook (India) Limited ("TCIL"), Thomas Cook Insurance Services (India) Limited ("TCISIL") and Sterling Holiday Resorts (India) Limited ("SHRIL") regarding a composite scheme of arrangement and amalgamation ("Scheme") whereby the resorts and time share business of SHRIL would be transferred by way of a separation from SHRIL to TCISIL (a subsidiary of TCIL) while SHRIL with its residual business would be absorbed into TCIL. Additionally, the details of certain acquisitions were also disclosed in the notification, which were claimed to be exempt pursuant to the Government of India ("GoI") Notification dated 04.03. 2011 (regarding *de minimis* target exemption), namely (i) subscription of 22.86 % of the equity shares of SHRIL by TCISIL, pursuant to a Subscription Agreement (SA) dt.07.02. 2014 (ii) purchasing of 19.94 % equity shares of SHRIL by TCISIL pursuant to a Share Purchase Agreement ("SPA") dated 07.02.2014 (post preferential allotment/subscription) (iii) open offer for shares of SHRIL pursuant to the SA and SPA under the relevant provision of the Takeover Regulations, 2011 for which TCISIL along with TCIL, as a person acting in concert, had made public announcement to purchase up to 26 % of the equity share capital of SHRIL from the public shareholders pursuant to the respective resolutions of TCISIL and TCIL on 07.02. 2014 and (iv) 'market purchases' during the period between the 10th and 12th of February, 2014 by TCISIL of equity shares representing 9.93 % of the equity share capital of SHRIL.

In the course of its assessment, having considered the Scheme and the aforesaid acquisitions as parts of one single composite combination, the CCI noticed that 'market purchases', constituting a part of said composite combination, had already been consummated prior to filing of the notification

and accordingly imposed the penalty on the grounds of non-compliance with the provisions of section 6(2) of the Act.

Statutory context:

As per the extant provisions of section 6(2) as applicable at the relevant point of time, any person or enterprise proposing to enter into a merger operation was required to give notice to the CCI within 30 days from the date of approval by the boards of each company in regards to the merger or amalgamation, referred to in section 5 (c), or executing an agreement or 'other document' for the acquisition or acquiring of control referred under section 5 (a) or 5 (b). Thus, if any person or enterprise failed to give notice under section 6 (2), the CCI could impose on such person or enterprise a penalty of up to one percent of the total turnover or assets, whichever is higher, of such a combination, by the terms of section 43A since the Act provides for a mandatory and suspensory merger regime.

It may be relevant to state herein that the GoI, via Notification dated 29.06.2017, has done away with the requirement of pre-merger notification within the 30-days deadline. Further, via GoI Notification dated 04.03.2011, the parties were exempt from the filing requirement in cases where the enterprise being acquired had either assets with a value of not more than INR 250 crore (1 crore =10 million) in India or turnover of not more than INR 750 crore in India. However, such an exemption was applicable only to cases of acquisitions but not to mergers or amalgamations. Pertinently, via GoI Notification dated 04.03.2016, *de minimis* target exemption has been enhanced to INR 350 crore for the value of assets and to INR 1000 crore for the turnover. Further, via GoI Notification dated 27.03.2017, the same has also been extended to mergers and amalgamations, thereby exempting small value mergers from the requirement of notification to the CCI.

In this context, it is also relevant to state that Regulation 9 (4) of the Competition Commission of India (regarding the transactions of businesses relating to combinations) Regulations ("Combination Regulations"), notified on 11.05.2011, provided that where the ultimate intended effect of a business transaction is achieved by way of a series of steps or smaller individual transactions which are inter-connected or inter-dependent on each other[4], one or more of which may amount to a merger, a single notice covering all these transactions may be filed[5] by the parties to the merger.

Imposition of penalty on Thomas Cook: A case of market purchase as part of composite transactions:

As the above combination was notified to the CCI to seek approval for the proposed demerger from SHRIL to TCISIL and amalgamation of SHRIL, with its residual business, into TCIL, and with the parties claiming exemption in respect to other steps of the transactions relating to acquisition of shares of SHRIL, pursuant to shares subscription, shares purchase, open offer and market purchases, under then prevailing *de minimis* target exemption, the CCI reasoned that all the steps of acquisitions described above were inter-related and interdependent with the demerger and amalgamation transaction, and out of all the steps involved, 'market purchases' had been consummated at the time of notification, and thus amounted to gun jumping.

In the appeal[6] directed against the aforementioned order of the CCI, the COMPAT observed that the agency declined to offer the benefit of *de minimis* target exemption, mainly on the grounds that the market purchases were intrinsically connected with other transactions. However, in doing so, the CCI failed to recognize the fact that the implementation of the scheme for demerger/amalgamation was not dependent on the market purchase of equity shares of SHRIL by TCISIL and *vice versa*.

Appeals in the Thomas Cook case before the Supreme Court of India:

In the second statutory appeal, via its judgement dated 17.04.2018, the Supreme Court ruled on the controversy as follows:

> *"26. It is apparent that in the notification made under section 6(2) on 14.2.2014 notifiable transactions were shown regarding merger and amalgamation. It was also mentioned that parties have also contemplated certain other transactions in view of the notifiable transactions, they were the substitution of equity shares, SPA, open offer and market purchase. It is crystal clear from the aforesaid application itself that all these transactions were part of the same transactions and even before notifying the transactions of purchase from the market on 14.2.2014, it was consummated between 10.2.2014 to 12.2.2014. It is crystal clear that market purchases being a part of the composite combination was consummated before giving notice to the Commission. Joint Press Release dated 7.2.2014 clearly indicated SPA as an open offer. The Board of Directors of the respective parties authorized market purchases on the same day. All the said transactions are intrinsically connected and interdependent with each other and form part of one viable business transaction.*
>
> *27. Though market purchases have no references in MCA, SA, SPA and the scheme, the facts, and circumstances of the case, as the scheme was prepared on the same day and the three companies passed the resolution on the same day. All other acquisitions were made on the same day. Market purchases having been consummated between 10.2.2014 to12.2.2014, which is almost after finalizing the composite combination clearly suggested that market purchases would not have taken place in the absence of scheme and the other acquisitions. In case they were not part of the same scheme that would not have been referred to in the notice filed by them with the Commission on 14.2.2014. Thus, in our considered opinion market purchases were not independent and were intrinsically related to the scheme and other acquisitions."*

As regards the issue of exemption, particularly of market purchases that was claimed by the parties, the court observed:

> *"28.....While it is open for the parties to structure their transactions in a particular way the substance of the transactions would be more relevant to assess the effect on competition irrespective of whether such transactions are pursued through one or more step/transactions. Structuring of transactions cannot be permitted in such a manner so as to avoid compliance with the mandatory provisions of the Act. For ensuring the compliance with the requirements of the Act it is open to considering whether the particular step was an individual transaction or part of the whole of the transaction. It was evident in the facts and circumstances of the case as TCISIL would not have made market purchase in the absence of any one transaction. Thus, market purchases could not have been termed to be independent transaction."*

It is worth mentioning here that the requirement to comply with the merger regulations in India is not limited to transactions that involve the acquisition of or change in control, as is the case in European Union. The Indian merger regime, like the HSR Act, is a procedural law and does not differentiate between acquisitions that may raise anti-competitive concerns and those that do not. Accordingly, it is necessary to comply with the pre-merger filing requirements even in relation to cases which may not lead to control or an AAEC (appreciable adverse effect on competition), failing which it is liable to be treated as gun jumping, attracting penalties.

SCM Soilfert case[7]:

Notification in this case was made to the CCI on 22.05.2014 by SCM Soilfert Limited, a wholly owned subsidiary of Deepak Fertilizers and Petrochemicals Corporation Limited ("DFPCL"), for acquisition of 0.8% of the equity share capital of Mangalore Fertilizers and Chemicals Limited ("MCFL") through open market transactions ("Second Acquisition") and the acquisition of up to 26% of the equity share capital of MCFL through an open offer as per the relevant provisions of the Takeover Regulations, pursuant to a public announcement made on 23.04 2014. However, in this regard, the CCI observed that the acquirers also held 24.46 % equity share capital of MCFL, prior to filing notification under section 6 (2), which was acquired by them on a single day on 03.07.2013, through a number of block and bulk deals on the Bombay Stock Exchange ("First Acquisition"). The CCI observed that DFPCL, in its press release dated 03.07.2013 filed with the stock exchanges, had stated that "given DFPCL's considerable strengths in the fertilizer business", the purchase of equity shares amounting to 24.46% of the capital shares of MCFL was a "very strategic and good fit with the company's [i.e. DFPCL's] business" and that, "DFPCL looks forward to working closely with MCFL to enhance long term value for the shareholders of both companies."

In this regard, the acquirers pleaded that the First Acquisition was not made with any intent to acquire control of MFCL, but was made 'solely for investment purposes' and, thus was exempt from notification under Item 1 of Schedule I of the Combination Regulations." (Statutory provisions in this context explained later in this article). In this regard, the CCI also noted that as per media reports, the acquirers and the Zuari group had engaged in a takeover bid for MCFL, as in April 2013, Zuari group had purchased shares amounting to 16.43% of MCFL's share capital and immediately thereafter DFPCL had made the First Acquisition. The CCI noted that the acquirers and MCFL were engaged in similar businesses and that the acquirers had not provided any evidence to support their claim that there was no intention on their part to gain control over MCFL. Accordingly, the CCI concluded that the First Acquisition was not made solely as investment or in the ordinary course of business, and should have been notified in terms of section 6 (2) of the Act. The CCI, accordingly held the acquirers liable for penalty under section 43A of the Act.

Further, as regards the Second Acquisition, the acquirers pleaded that this had been duly notified to the CCI and had not been consummated since the shares acquired, representing 0.8 % stake in MCFL, had been kept in an escrow account with the acquirers not exercising any beneficial interest, including the voting rights. In this regard, the CCI noted that since the Act or the Combination Regulations did not exempt a situation wherein a buyer acquired shares but decided not to exercise legal/beneficial rights attached to them, the acquirers' plea that the Second Acquisition was not consummated was untenable under the law. The CCI also noted in this regard that the non- exercise of voting rights for a limited period of time with respect to the Second Acquisition was a self-imposed contractual obligation taken upon by the acquirers, and, therefore, the acquirers had consummated the Second Acquisition prior to giving notice in terms of section 6 (2) of the Act.

While upholding the CCI order,[8] the COMPAT noted that the term 'other document' as used in section 6 (2)(b) of the Act and explained in Regulation 5(8) of the Combination Regulations[9], covers any document executed to acquire the shares and even the order placed with the broker for purchasing shares, which becomes a trigger for notice under section 6(2).

Appeal in Soilfert case before the Supreme Court of India:

In the statutory appeal, via its judgement dated 17.04.2018, the Apex Court ruled that:

> *"8.Per contra, the Commission has rightly imposed the penalty. There was a breach of provisions contained in section 6(2). The penalty imposed is meager. The first acquisition*

of shares was notifiable. It could not have been termed solely as an investment. Reliance has been placed on Press Release issued on 3.7.2013, which referred investment being "very strategic", and the appellant also notified to the public that they "look forward to working closely with MCFL in the future". The knowledge of acquisition by the Zuari group of 9.72% shares in MCFL on 2.4.2013 was admitted in the reply filed by the appellants. There was the acquisition of a large number of shares on the same day through the block and bulk deals. MCFL was not very profitable. Therefore, purchase of shares could not be said to be a sound investment by a prudent investor.

Concerns & ambiguities under the CCI's merger regulations:

Composite transaction:

With reference to the S.C. order passed in the Thomas Cook case, it is obligatory on the part of the acquirer to file a single notice for a composite transaction covering all the inter-connected transactions, including market purchases, if any. In this regard, the CCI via its order passed on 02.05.2016 in combination notice no. C-2015/02/249 (Piramal Enterprises), while quoting from the European Commission's Consolidated Jurisdictional Notice, had also observed that 'if two or more transactions (each of them bringing about an acquisition of control) take place within a two-year period between the same persons or enterprises, they shall be qualified as a single concentration, irrespective of whether or not those transactions relate to parts of the same business or concern the same…. It is sufficient if the transactions, though not carried out between the same companies, are carried out between companies belonging to the same respective groups.'

Market purchases not considered 'solely as an investment':

The CCI lists certain categories of combinations mentioned in Schedule I as Combination Regulations which are normally not subject to mandatory notification. A significant exemption provided under Item I of Schedule I pertains to acquisition, directly or indirectly, of less than 25% of shares or voting rights, if made 'solely as an investment' or in the 'ordinary course of business', not resulting in control. An acquisition is considered 'solely as an investment' if the acquirer is not engaged in the same line of business and / or the investment does not lead to control. Further, the acquisition of shares by a public financial institution or mutual fund companies is considered as in the 'ordinary course of business', if made without control.

In combination notification no. C-2015/08/301, the acquisition by Alibaba.com Singapore E-Commerce of 4.14% of a non-controlling minority stake in Jasper Infotech was not exempt from notification since the acquirer and the target were competitors. In combination notice no. C-2014/08/202 (New Moon/Mylan case), the CCI noted that acquisition of less than 25% shares or voting rights may raise competition concerns if either the acquirer and the target are engaged in business of substitutable products/services or are engaged in activities at different stages or levels of the same production chain.

Via Amendment Regulations 2016, whereby Explanation to Item I of Schedule I was inserted, the CCI earmarked another threshold providing that an acquisition of less than 10% of total shares or voting rights shall be treated as 'solely an investment' provided the acquisition is carried out without (i) rights which would not be exercisable by ordinary shareholders (ii) rights/intention to nominate a CEO and (iii) the intention to participate in the affairs or management of the target company. However, it is noted that the acquisition of a non-controlling stake below a 10% threshold, when in a horizontal or vertically linked business, is still subject to mandatory notification. For example, in merger case no.

C-2017/12/538, a filing was made for the acquisition of a non-controlling minority stake of 5 % in Shoppers Stop by the investment arm (a category III foreign portfolio investor) of online retailer Amazon.com Inc.

With reference to the S.C. order passed in the SCM Soilfert case, it was held that since the acquirers and the target were engaged in similar businesses, the market purchase of equity share capital of MCFL made on a single day by DFPCL through a number of block and bulk deals, not being solely as an investment or in ordinary course of business, ought to have been notified. It is also relevant to mention here that, in the merger case no. C-2014/06/181, involving the acquisition of 16.43 % equity interest in MFCL by Zuari Fertilisers and Chemicals ("ZFCL") in separate tranches of open market purchases, the CCI observed that the exempt categories under Item I of Schedule I do not include mergers that are likely to cause a change in control or are of the nature of strategic mergers, and rejected the plea to treat market purchases as solely for investment.

Notification of 'market purchases':

It may be insightful to mention that, under the provisions of Article 7 (1) of EUMR, a concentration cannot be completed or implemented either before its notification to the competition authority or until it has been declared compatible with the common market. However, an exception under Article 7(2) has been provided in the case of a public bid or a series of transactions in securities in a stock exchange, provided that the concentration has been notified to the Commission without delay and the acquirer does not exercise voting rights attached to the securities, or does so only to maintain the full value of its investments based on a derogation granted by the Commission under Article 7(3). As it concerns the U.S., in cases involving tender offers and other acquisitions of voting securities from third parties, the waiting period under the HSR Act begins as soon as the acquiring entity has made the requisite filing. However, the parties may request the antitrust agencies for early termination of the waiting period, which the agencies may grant at their discretion.

Unlike the EUMR, there is no provision under Indian law regarding 'derogation' or exemptions to gun jumping applicable to public bids and transactions in securities on a stock exchange. Similarly, there is also no provision of early termination of the waiting period, as in the U.S.

As discussed above in the SCM Soilfert case, the CCI had noted that non-exercise of voting rights voluntarily for a limited period of time by way of keeping the shares in an escrow account will be treated as consummation due to the absence of any provision in this regard under the Act or the Merger Regulations. The Supreme court, in its order on the appeal in the SCM Soilfert case, has endorsed the above view held by the CCI. As regards the transaction of market purchases, the court has also ruled that notification under section 6(2) is to be given prior to the consummation of the acquisition, and provisions made in Regulation 5(8) buttresses the said conclusion. In light of the above, the Supreme Court observed that *ex post facto* notification is not contemplated under the provisions of section 6(2) as the same would be in violation of the provisions of the Act.

Conclusion:

In view of the above, it is extremely important for the parties to make a proper assessment at the time of filing pre-merger notification to determine whether the proposed combination is in the nature of a composite transaction or whether it is exempt from notification, being solely for investment purposes. However, until such time as the CCI comes out with an official guideline, market purchases, if not exempt for being solely for an investment or in the ordinary course of business, must be notified under the provisions of section 6 (2) of the Act to rule out gun jumping or any violation under the Act.

[1] Ajay Goel is a Partner at Saikrishna & Associates. Subodh Prasad Deo is a Partner and Head of Competition Law Practice at Saikrishna & Associates.

[2] (1) Civil Appeal no.13578 of 2015; CCI vs. Thomas Cook (India) Ltd. & Anr and (2) Civil Appeal no. 10678 of 2016; SCM Solifert Ltd. & Anr.

[3] Combination case No.C-2014/02/153, CCI order dated 21.05.2014.

[4] The words "*or inter-dependent on each other*" were deleted via Amendment to Combination Regulations 2016.

[5] The words "*may be filed*" were replaced by the words "*shall be filed*" via Amendment to Combination Regulations 2015.

[6] Appeal No. 48 of 2014 decided by COMPAT via order dated 26.08.2015.

[7] Combination case no. C-2014/05/175, CCI order dated 10.02.2015

[8] Appeal no. 59/2015 decided by COMPAT via its order dated 30.08.2016.

[9] Regulation 5(8) of the Combination Regulations:

"(8) The reference to the "other document" in clause (b) of subsection (2) of section 6 of the Act shall mean any binding document, by whatever name called, conveying an agreement or decision to acquire control, shares, voting rights or assets: Provided that if the acquisition is without the consent of the enterprise being acquired, any document executed by the acquiring enterprise by whatever name called, conveying a decision to acquire control, shares or voting rights shall be the "other document".