

Sun Pharma – Ranbaxy

A Panacea for Ranbaxy's ills?

December 2014

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1. Prologue

Sun Pharmaceutical Industries Limited (“**Sun Pharma**”) and Ranbaxy Laboratories Limited (“**Ranbaxy**”) set the Indian pharmaceutical industry abuzz with excitement on April 6, 2014 when they released a press statement announcing that they had entered into definitive documents under which Sun Pharma would acquire 100 percent of Ranbaxy (“**Transaction**”).¹ The Transaction which was a heavily guarded secret until the public announcement, is to be effected by means of a merger/ amalgamation between Sun Pharma and Ranbaxy. The combined entity, upon successful consummation of the Transaction, would be the fifth-largest specialty generics company in the world and the largest pharmaceutical company in India.² The scale of operations of the resulting entity would be massive, with operations spanning across 65 countries and 47 manufacturing facilities across 5 continents, as well as a sizeable portfolio of specialty and generic products sold across the world, including 629 abbreviated new drug applications (“**ANDAs**”).^{3 4}

The announcement of the Transaction was of particular interest to the pharmaceuticals industry as it came at a crucial time for Ranbaxy. Ranbaxy's manufacturing facilities in Toansa, Paonta Sahib, Dewas and Mohali in India have been under the scanner of the United States Food and Drug Administration (“**USFDA**”) following observation of certain lapses in complying with current good manufacturing practices during the course of inspection of these facilities by the USFDA.⁵ As a result, the USFDA had prohibited Ranbaxy from distributing drugs manufactured using active pharmaceutical ingredients (“**APIs**”) from these facilities, in the United States. The USFDA sanctions on Ranbaxy and certain other companies in India have caused the multi-billion dollar Indian generic pharmaceutical industry severe loss in international markets. The acquisition by Sun Pharma may result in a turnaround for the beleaguered Ranbaxy and is therefore, welcome news for Ranbaxy as well as its

Japanese parent Daiichi Sankyo Co Ltd (“**Daiichi**”). The Competition Commission of India (“**CCI**”) by way of its order dated December 5, 2014 approved the Transaction subject to satisfaction of certain conditions.

The Transaction comes in the wake of various big-ticket deals entered, or proposed to be entered into by pharmaceutical companies across the globe, such as Novartis' and GlaxoSmithKline's (~USD 23 billion) business swap, Pfizer's USD 100 billion offer for AstraZeneca, Bayer's acquisition of Merck's consumer care business for USD 14.2 billion and Valeant's USD 47 billion offer for Allergan. On the home front, Sun Pharma itself has been gearing up for an acquisition drive, with its open offer to the shareholders of Zenotech Laboratories Limited immediately after the announcement of the Transaction.⁶

Several reasons may be attributed to such M&A activity by pharma companies, some of them being:

- i. Attaining the scale necessary in those therapeutic areas where they intend to focus, by building a broader product portfolio and services;⁷
- ii. Pressure by governmental agencies, insurance companies in North America and Europe to reduce cost of medicines, due to difficulty in meeting mounting healthcare costs etc.⁸

Building a product portfolio is research-intensive and cost-prohibitive for pharmaceutical companies. Therefore, pharmaceutical companies may opt to achieve their objectives through inorganic growth by way of M&A. Further, M&A activity in certain industries such as pharmaceuticals follows a cyclical trend, with acquisitions ramping up over five-year periods. This is evident from the spurt of M&As in 2008-2009 with Pfizer's acquisition of Wyeth, Merck's acquisition of Schering-Plough Corp, Novartis' acquisition of Alcon Inc., as well as Daiichi's acquisition of Ranbaxy.⁹

1. <http://www.ranbaxy.com/sun-pharma-to-acquire-ranbaxy-in-a-us4-billion-landmark-transaction/>, last accessed on June 24, 2014

2. Ibid

3. An ANDA is an application for a U.S. generic drug approval for an existing licensed medication or approved drug. The ANDA is submitted to USFDA's Center for Drug Evaluation and Research, Office of Generic Drugs, which reviews and approves a generic drug product for manufacture and marketing the generic drug product as an effective, low cost alternative, to the American public.

4. <http://www.ranbaxy.com/sun-pharma-to-acquire-ranbaxy-in-a-us4-billion-landmark-transaction/>, last accessed on June 24, 2014

5. <http://www.fda.gov/NewsEvents/Newsroom/PressAnnouncements/ucm368445.htm>, last accessed on June 24, 2014

6. http://www.bseindia.com/corporates/anndet_new.aspx?newsid=68185c15-8a2b-4ee3-8854-4846897f04fb, last accessed on June 24, 2014

7. http://www.jmijitm.com/papers/130245123339_47.pdf, last accessed on June 24, 2014

8. Ibid

9. <http://www.gfmag.com/tools/global-database/economic-data/9976-mergers-and-acquisitions-largest-maa-deals-2009-and-2008.html>, last accessed on June 24, 2014

Indian pharmaceutical companies hold considerable advantage over foreign pharmaceutical manufacturers in terms of cost-effectiveness of manufacturing processes as well as research and development. Thus, the Transaction has the potential to give rise to a formidable force in pharmaceutical manufacturing leading to wider presence and broader product portfolio. This M&A Lab analyzes in detail, the legal, regulatory, tax and commercial considerations behind the Transaction.

2. Glossary of Terms

Terms	Definitions
AAEC	Appreciable adverse effect on competition
ANDA	Abbreviated new drug application
API	Active pharmaceutical ingredient
BSE	Bombay Stock Exchange
CA 1956	Companies Act, 1956
CA 2013	Companies Act, 2013
Caraco	Caraco Pharmaceutical Laboratories
CCI	Competition Commission of India
Combination Regulations	Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011
Competition Act	Competition Act, 2002
Daiichi	Daiichi Sankyo Co Ltd
EBITDA	Earnings before tax, depreciation and amortization
FDI	Foreign direct investment
February 4 Circular	SEBI Circular No. CIR/CFD/DIL/5/2013 dated February 4, 2013
FIPB	Foreign Investment Promotion Board
GDR	Global depository receipts of Ranbaxy
HSR Act	Hart-Scott-Rodino Antitrust Improvements Act, 1976
INR	Indian Rupees
ITA	Income Tax Act, 1961
JV	Joint venture
LLP	Limited liability partnership
M&A	Mergers and acquisitions
May 21 Circular	SEBI Circular No. CIR/CFD/DIL/8/2013 dated May 21, 2013
NSE	National Stock Exchange
ODI Regulations	RBI's Master Circular on Direct Investment by Residents in Joint Venture (JV)/ Wholly Owned Subsidiary (WOS) Abroad dated July 1, 2013
R&D	Research and development
Ranbaxy	Ranbaxy Laboratories Limited
Ranbaxy ESOPs	Employee stock options of Ranbaxy
RBI	Reserve Bank of India
RD	Regional Director, Company Law Board
SEBI	Securities and Exchange Board of India
SEBI Insider Trading Regulations	SEBI (Prohibition of Insider Trading) Regulations, 1992
Sun Pharma	Sun Pharmaceutical Industries Limited
Sun Pharma ESOPs	Employee stock options of Sun Pharma issued in exchange of Ranbaxy ESOPs in accordance with the scheme
Takeover Code	SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011

Glossary of Terms

Provided upon request only

Transaction	Acquisition of 100% of Ranbaxy by Sun Pharma by way of scheme of merger
UKMHRA	Medicines and Healthcare products Regulatory Agency
USFDA	United States Food and Drug Administration
US	The United States of America
USD	United States Dollars
VAT	Value-added tax
WOS	Wholly-owned subsidiary
Zenotech	Zenotech Laboratories Limited

3. Details of the Deal

I. Parties Involved

A. Sun Pharma

Sun Pharma is an Indian origin, specialty pharmaceutical company, established in 1983 with a portfolio of five psychiatric medications and a manufacturing facility in Vapi, Gujarat.¹⁰ Sun Pharma established its first research center in 1991, driving further growth for the company.¹¹ It went public in 1994 and is currently listed on the Bombay Stock Exchange (“BSE”) as well as the National Stock Exchange (“NSE”). Approximately 64 percent of the shareholding of Sun Pharma is still held by the promoters and promoter group. In addition to its formulations in various therapeutic areas, Sun Pharma also manufactures APIs to facilitate the manufacture of complex formulations such as anti-cancers, peptides, sex hormones and controlled substances.¹²

In 30 years of its existence, Sun Pharma has become one of the world’s most profitable pharmaceutical manufacturers. Sun Pharma has complemented its growth by way of extensive acquisitions and joint ventures in India and abroad. The acquisition of Tamilnadu Dadha Pharma has helped Sun Pharma’s entry into oncology and gynecology.¹³ The company’s initial investment in and subsequent takeover of Gujarat Lyka Organic Ltd provided access to a manufacturing facility for cephalexin for supply to the international market.¹⁴ Sun Pharma’s 2002-acquisition of MJ Pharma has provided Sun Pharma a USFDA and UKMHRA approved plant which is currently a manufacturing base for the European generic market.¹⁵ In 1997, Sun Pharma invested in Caraco, a Detroit-based manufacturer of generics and in 2010, completely acquired Caraco,

enabling its entry into the U.S generic market. The acquisition of majority stake in Taro Pharmaceutical Industries Limited in 2010, an established multinational generics manufacturer, increased the company’s U.S presence, as well as in Israel and Canada.¹⁶ In addition to developed markets, Sun Pharma has also focused on emerging markets with its joint venture with MSD.¹⁷

B. Ranbaxy

Established in 1961, Ranbaxy is an Indian company listed on the BSE, NSE and the Luxembourg stock exchange, with ground operations in 43 countries and 21 manufacturing facilities spread across 8 countries. It is engaged in development, manufacture and marketing of pharmaceutical products and APIs.¹⁸ In 1988, Ranbaxy’s Toansa plant achieved USFDA approval, thereby enabling it to manufacture pharmaceuticals for the US market.

Ranbaxy has also engaged in acquisitions to further its growth objectives. The company’s acquisition of Crosland Research Laboratories, Rima Pharmaceuticals etc. provided it a foothold in niche, high-value markets in the European Union.¹⁹ The acquisition of RPG Aventis helped Ranbaxy achieve a turnover of USD 1 billion, making it the first Indian company to reach such global status.²⁰

In 2008, Daiichi entered into definitive agreements with the erstwhile promoters of Ranbaxy (the Singh family) to acquire a controlling stake in Ranbaxy. This was an off-market transaction, pursuant to which Daiichi was required to make an open offer to the public shareholders of Ranbaxy.²¹ Pursuant to the conclusion of the open offer, Daiichi acquired an additional 20 percent equity stake in Ranbaxy,

10. <http://www.sunpharma.com/formulations>, last accessed on June 24, 2014

11. <https://www.sunpharma.com/history>, last accessed on June 24, 2014

12. <http://www.sunpharma.com/api>, last accessed on June 24, 2014

13. <https://www.sunpharma.com/acquisitions>, last accessed on June 24, 2014

14. Ibid

15. Ibid, also see http://www.jmijitm.com/papers/130245123339_47.pdf

16. For more information regarding Sun Pharma’s acquisition of Taro, please refer to our M&A Lab available at: <http://www.nishithdesai.com/information/navigation/navigation2/ma-lab/ma-lab/article/sun-pharma-ndash-taro-pharma-deal-dissection.html>, last accessed on June 24, 2014

17. Merck & Co., Inc., is known as Merck, Sharp and Dohme (MSD) outside the United States and Canada.

18. <http://www.ranbaxy.com/about-us/overview/>, last accessed on June 24, 2014

19. http://www.jmijitm.com/papers/130245123339_47.pdf, last accessed on June 24, 2014

20. Ibid

21. Under the provisions of Regulations 10 and 12 of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997, acquisition of shares / voting rights in a listed company, which will, in aggregate, give the acquirer 15 percent or more of the voting rights in the company or acquisition of control over a listed company, would trigger an open offer requirement.

resulting in an aggregate shareholding of 63.92 percent in Ranbaxy.²²

Following the acquisition of controlling stake by Daiichi however, Ranbaxy has had a number of entanglements with the USFDA for issues related to quality-control, making it difficult to keep a clean name.²³ Ranbaxy's plants at Dewas and Paonta Sahib were slapped with import alerts by the USFDA in 2008.²⁴ In May 2013, Ranbaxy also pleaded guilty to felony charges in the US, relating to the manufacture and distribution of certain adulterated drugs made at Ranbaxy's manufacturing facilities in India and had to pay a fine of USD 500 million.²⁵ Further, in September 2013, the company's Mohali facility was

also banned from manufacturing pharmaceuticals which were intended to be exported to the US.²⁶ This was followed by the ban on the Toansa facility in Punjab for lapses in quality control and adherence to procedure.²⁷

C. Daiichi

Daiichi is a global pharmaceutical company with corporate origin in Japan.²⁸ In 2008, Daiichi acquired a controlling stake in Ranbaxy. However, the value of Daiichi's investments has halved over the years, as Ranbaxy has not been able to ensure compliance of its factories supplying to the US, with USFDA guidelines.²⁹

II. Deal Snapshot

Merging Company	Ranbaxy
Surviving Company	Sun Pharma
Share Swap Ratio	0.8 share of Sun Pharma of face value of INR 1/- each will be allotted to the shareholders of Ranbaxy for each share of INR 5/- each held by them in Ranbaxy.
Implied value per share	INR 457 for each Ranbaxy share, representing an 18 percent premium to Ranbaxy's 30-day volume weighted average share price ³⁰
Total equity value of the Transaction	USD 3.2 billion (USD 4 billion including payment to NCD holders)

A brief chronology of events pertaining to the Transaction is provided below:

Date	Event
April 6, 2014	Resolutions regarding the amalgamation agreement and other matters passed at the Board of Directors meetings of Sun Pharma and Ranbaxy
April 30, 2014	Andhra Pradesh High Court issues notices to the Securities and Exchange Board of India ("SEBI"), BSE, NSE, Sun Pharma, Ranbaxy and Silver Street Developers LLP to maintain status quo, based on a writ petition alleging insider trading in the shares of Ranbaxy in the days prior to the announcement of the Transaction
May 11, 2014	Daiichi files a petition before the Andhra Pradesh High Court requesting it to vacate the 'status quo' order ³¹
May 13, 2014	Sun Pharma moves the Supreme Court against the status quo order of the Andhra Pradesh High Court

22. For more information regarding the acquisition of controlling stake by Daiichi in Ranbaxy, please refer to our M&A Lab at <http://www.nishithdesai.com/information/navigation/navigation2/ma-lab/ma-lab/article/ranbaxy-daiichi-deal-dissected.html>, last accessed on June 24, 2014

23. <http://www.fda.gov/Drugs/GuidanceComplianceRegulatoryInformation/EnforcementActivitiesbyFDA/ucm118411.htm>, last accessed on June 24, 2014

24. <http://in.reuters.com/article/2013/09/16/ranbaxy-fda-alert-idINDEE98Fo2M20130916>, last accessed on June 24, 2014

25. <http://www.justice.gov/opa/pr/2013/May/13-civ-542.html>, last accessed on June 24, 2014

26. <http://in.reuters.com/article/2013/09/16/ranbaxy-fda-alert-idINDEE98Fo2M20130916>, last accessed on June 24, 2014

27. <http://businesstoday.intoday.in/story/fda-flies-in-ranbaxy-toansa-plant-sample-storage-room/1/202719.html>, last accessed on June 24, 2014

28. <http://www.daiichisankyo.com>, last accessed on June 24, 2014

29. http://www.business-standard.com/article/companies/sun-pharma-buys-ranbaxy-from-japan-s-daiichi-114040700737_1.html

30. <http://forbesindia.com/article/special/daiichi-could-be-the-biggest-beneficiary-of-the-sun-pharmaranbaxy-deal/37546/1>, last accessed on June 24, 2014

31. <http://economictimes.indiatimes.com/industry/healthcare/biotech/pharmaceuticals/daiichi-sankyo-contests-andhra-pradesh-high-court-fiat-on-ranbaxy-deal/articleshow/34992210.cms>, last accessed on June 24, 2014

May 13, 2014	FIPB to take up Daiichi's FDI proposal in Sun Pharma ³²
May 21, 2014	Supreme Court directs the Andhra Pradesh High Court to decide the matter and posts the case for hearing on May 27, 2014
May 24, 2014	Andhra Pradesh High Court vacates status quo order
July 11, 2014	Approval for the scheme from BSE and NSE ³³
August 22, 2014	Court-convened extraordinary general meeting of shareholders of Sun Pharma conducted pursuant to an order dated August 5, 2014 of the High Court of Punjab and Haryana ³⁴
August 27, 2014	Competition Commission of India ("CCI") directs the Company to publish the details of the proposed combination in the prescribed format
September 4, 2014	CCI invites comments from public in respect of the Transaction
September 19, 2014	Court-convened extraordinary general meetings of shareholders Ranbaxy to be conducted pursuant to an order dated August 5, 2014 of the High Court of Punjab and Haryana ³⁵
December 5, 2014	CCI grants conditional approval to the Transaction
December-end, 2014 / January 2015 (estimated)	Merger/ amalgamation completed with approval from high courts in India, the Indian central government and relevant state governments, stock exchanges and approval under the Hart-Scott-Rodino Act in the US ³⁶

III. Key Terms of the Deal

Ranbaxy will merge into Sun Pharma pursuant to a scheme of merger under Companies Act, 1956. At present, Daiichi owns approximately 63.41 percent of the shares of Ranbaxy. Both Daiichi and the promoters of Sun Pharma have irrevocably agreed to vote in favour of the Transaction at the general meetings of Ranbaxy and Sun Pharma respectively. ³⁷

Under the terms of the Transaction, 0.8 share of Sun Pharma of face value of INR 1/- each will be allotted to the shareholders of Ranbaxy for each share of INR 5/- held by them in Ranbaxy. Like other subsidiaries of Ranbaxy, Ranbaxy (Netherlands) B.V., which is a wholly owned subsidiary of Ranbaxy, will also become a subsidiary of Sun Pharma pursuant to the Transaction.

A. Shareholding Post Consummation of Transaction

Post closing of the Transaction, Daiichi will become the second largest shareholder in Sun Pharma with a stake of ~9 percent, while the shareholding of the promoter group of Sun Pharma will stand reduced to ~55 percent.³⁸ The public shareholders of Ranbaxy are expected to hold ~14 percent and existing public shareholders of Sun Pharma will hold ~22 percent in Sun Pharma, post-closing of the Transaction.³⁹

B. Daiichi Director

Daiichi shall also have the right to nominate one director on the board of Sun Pharma.⁴⁰ This right will terminate when Daiichi's shareholding falls below 5 percent of the equity shareholding of Sun Pharma.⁴¹

32. <http://economictimes.indiatimes.com/news/economy/finance/fipb-to-take-up-34-fdi-proposals-on-tuesday/articleshow/34964423.cms>, last accessed on June 24, 2014

33. <http://www.livemint.com/Companies/PwftvxqaZovojwb8GzWEEdK/Sun-PharmaRanbaxy-deal-in-CCI-crosshairs.html>

34. http://www.bseindia.com/xml-data/corpfiling/AttachHis/Sun_Pharmaceutical_Industries_Ltd2_300714.pdf, last accessed on September 11, 2014

35. http://www.bseindia.com/xml-data/corpfiling/AttachHis/Ranbaxy_Laboratories_Ltd_220814.pdf, last accessed on September 11, 2014

36. http://www.bseindia.com/xml-data/corpfiling/AttachHis/Ranbaxy_Laboratories_Ltd1_070414.pdf, last accessed on June 24, 2014

37. M&A Critique, Vol. XXIII, Issue No. 9, May 2014

38. https://research.standardchartered.com/configuration/ROW%20Documents/India_pharmaceuticals_Sun_Pharma-Ranbaxy_merger_-_A_new_journey_on_an_insecure_terrain_07_04_14_16_55.pdf, last accessed on June 24, 2014

39. M&A Critique, Vol. XXIII, Issue No. 9, May 2014

40. http://www.business-standard.com/article/companies/sun-pharma-buys-ranbaxy-from-japan-s-daiichi-114040700737_1.html, last accessed on June 24, 2014

41. http://www.bseindia.com/xml-data/corpfiling/AttachHis/Ranbaxy_Laboratories_Ltd_220814.pdf, last accessed on September 11, 2014

C. Indemnity

Ranbaxy has recently received a subpoena⁴² from the United States Attorney for the District of New Jersey requiring Ranbaxy to produce certain documents relating to issues previously raised by the USFDA with respect to Ranbaxy's Toansa facility in Punjab, India. In connection with the Transaction, Daiichi has agreed to indemnify Sun Pharma and Ranbaxy for, among other things, certain costs and expenses that may arise from the proceeding.⁴³ Such indemnity may be essential for the consummation of the Transaction as any liability which may arise as a result of an adverse order by the judicial authority may have implications for the successor entity post the merger.

In addition, under the scheme, Sun Pharma is required to indemnify each present or former officer or director of Ranbaxy or any of its subsidiaries, for a period of 6 years from the effective date of the scheme, to the extent such officers and directors are indemnified under the policies of Ranbaxy and its subsidiaries, in the manner and to the extent mutually agreed between Sun Pharma and Ranbaxy.⁴⁴

D. Global Depository Receipts of Ranbaxy

The board of directors of Sun Pharma may elect, at its sole discretion, to pursue either of the below options for the global depository receipts of Ranbaxy ("GDRs").⁴⁵

- i. Equity option: effect the exchange and cancellation of the GDRs for a proportional number of equity shares of Sun Pharma based on the Share Swap Ratio; or
- ii. Cash-out option: cash out existing GDR holders following the effectiveness of the scheme.

E. ESOPs of Ranbaxy

Upon the scheme being approved by the High Courts, Sun Pharma shall issue stock options ("Sun Pharma ESOPs") to employees of Ranbaxy holding stock options of Ranbaxy ("Ranbaxy ESOPs"), which shall entitle the eligible employees to purchase equity

shares of Sun Pharma. The number of Sun Pharma ESOPs issued shall equal the product of the number of Ranbaxy ESOPs (whether vested or unvested) outstanding at the time the scheme comes into effect, multiplied by the Share Swap Ratio, with any fractional shares rounded down to the next higher whole number of shares (i.e. for every Ranbaxy ESOP held by an eligible employee which entitles such eligible employee to acquire 1.00 equity share in Ranbaxy, such eligible employee will be conferred a Sun Pharma ESOP to acquire 0.80 equity shares in Sun Pharma).

The terms and conditions applicable to the Sun Pharma ESOPs shall be no less favourable than those provided under the Ranbaxy ESOPs. Such Sun Pharma ESOPs will be issued under a new employee stock option scheme created by Sun Pharma, *inter alia* for the purpose of granting stock options to the eligible employees pursuant to the scheme.

F. Reduction of Share Capital and Reserves and Surplus of Ranbaxy

An amount equal to the balance lying to the debit in statement of profit and loss in the books of Ranbaxy on the close of March 31, 2014 shall be adjusted/reduced as follows in accordance with Sections 391 to 394, sections 78 and 100 to 103 of the Companies Act, 1956 ("CA 1956") and Section 52 of the Companies Act, 2013 ("CA 2013") and any other applicable provisions of law:

- i. Firstly, against reduction of the capital reserve account of Ranbaxy amounting to ~INR 1.762 billion;
- ii. Secondly, against reduction of securities premium account of Ranbaxy amounting to ~INR 35.014 billion;
- iii. Thirdly, against reduction of the general reserve of Ranbaxy amounting to ~INR 5.519 billion, to the extent available or required;
- iv. The balance, if any remaining in the debit in statement of profit and loss in the books of Ranbaxy shall be carried in the books of Ranbaxy as on March 31, 2014.

42. A subpoena is a written order to compel an individual to give testimony on a particular subject, often before a court, but sometimes in other proceedings (such as a Congressional inquiry). Failure to comply with such an order to appear may be punishable as contempt. Please see, <http://www.law.cornell.edu/wex/subpoena>.

43. http://www.business-standard.com/article/companies/sun-pharma-ranbaxy-deal-how-makov-convinced-daiichi-to-sell-114040700827_1.html, last accessed on June 24, 2014

44. http://www.bseindia.com/xml-data/corpfiling/AttachHis/Ranbaxy_Laboratories_Ltd_220814.pdf, last accessed on September 11, 2014

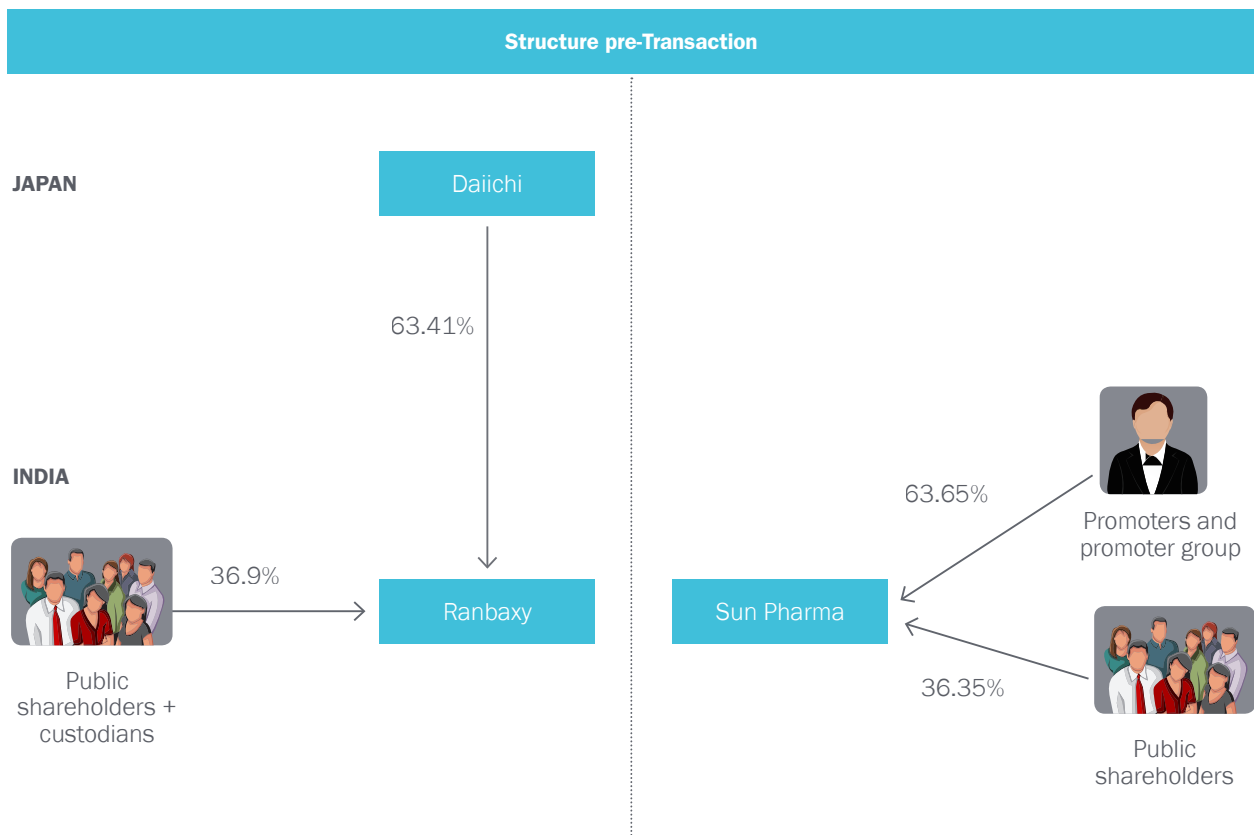
45. Ibid

G. Appointed Date and Effective Date

The 'appointed date' implies the date of amalgamation, that is, the date from which the undertaking including assets and liabilities of the transferor company vest in the transferee company. Typically, accounts of the transferor company on the appointed date form the basis for valuation of shares and determination of the share exchange

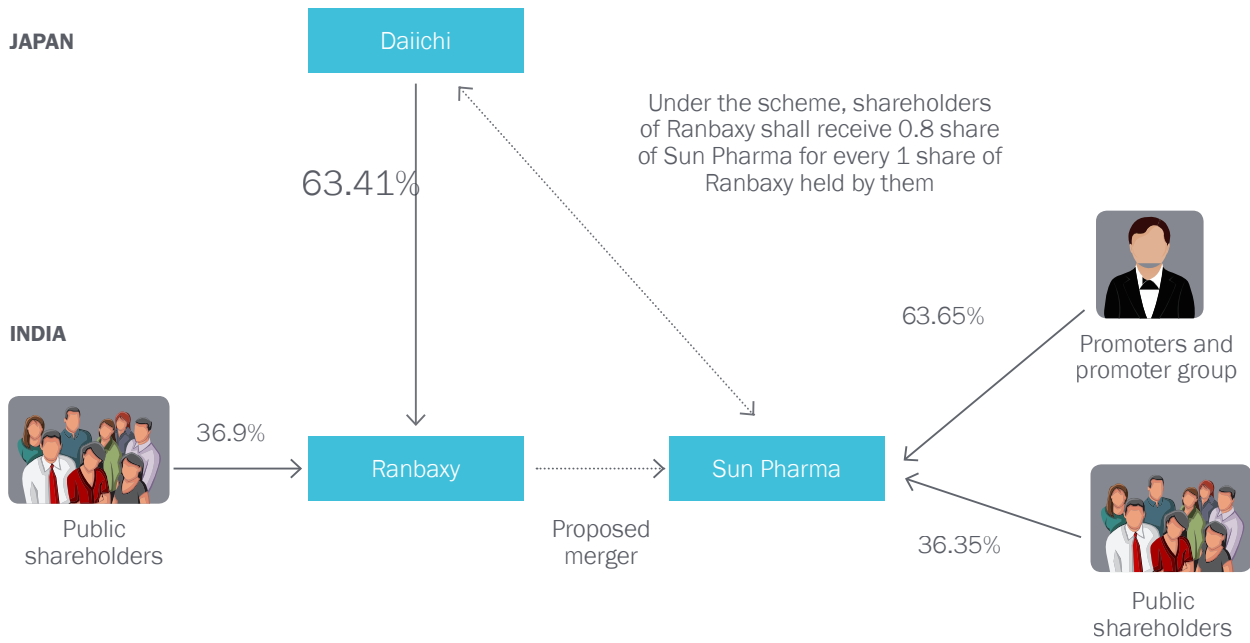
ratio. Appointed date is relevant for the purpose of assessment of income of the transferor and transferee companies. The 'effective date' is the date on which the formalities of the merger / amalgamation are completed, i.e., when the certified copy of the High Court's order is filed with the registrar of companies or the final approvals in relation to the scheme have been obtained. From the effective date, the merger becomes effective.

IV. Deal Structure⁴⁶

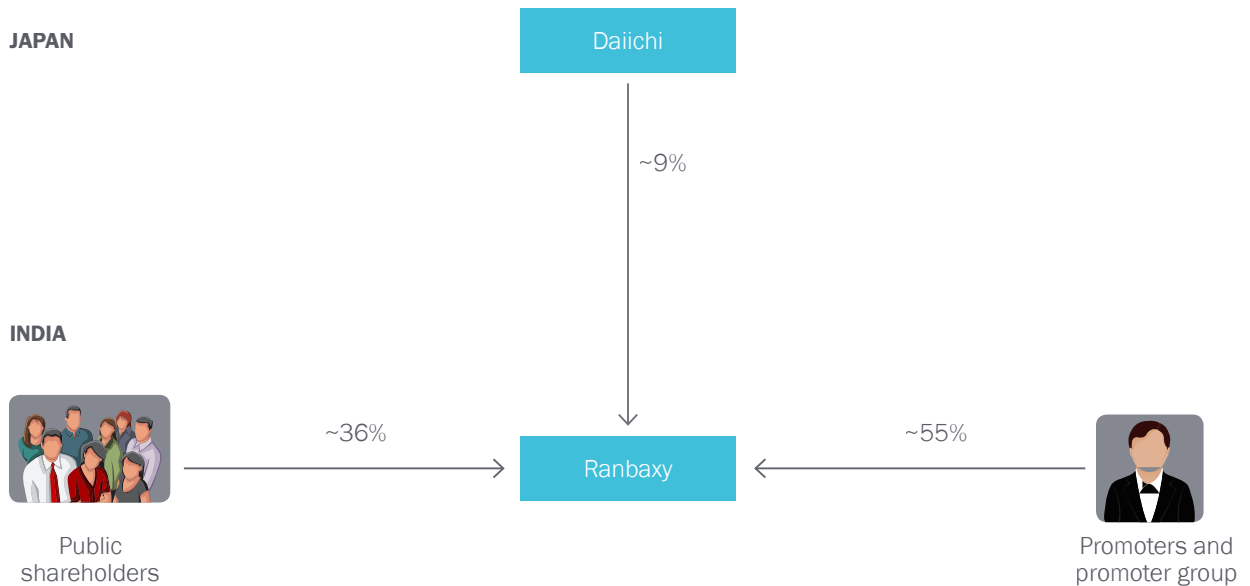


46. http://www.bseindia.com/xml-data/corpfiling/AttachHis/Ranbaxy_Laboratories_LtdI_070414.pdf, last accessed on June 24, 2014

Transaction



Structure post-Transaction



Legend: Holding structure ———> Transaction mechanics>

4. Commercial Considerations

I. What was Sun Pharma's rationale for acquiring Ranbaxy, despite the troubles faced by Ranbaxy in foreign markets?

A. Increased Market Penetration and Entry into New Markets

A merger or amalgamation is essentially an integration of synergies and one of the prime considerations for the Transaction includes the integration of product portfolio (including APIs), supply chain and manufacturing. Ranbaxy has a significant presence in the Indian market (21 percent sales) and in the US (29 percent sales). Sun Pharma on the other hand, has a strong presence in the US (60 percent of sales) and India (23 percent), while the rest of the world accounts for 17 percent sales of Sun Pharma. Thus, the combined entity will be more diversified with the US, the rest of the world and India contributing 47 percent, 31 percent and 22 percent of sales respectively. In the emerging markets (50 percent of Ranbaxy's sales), it provides a platform which complements Sun Pharma's strengths.⁴⁷ Through the Transaction, along with the emerging markets, Sun Pharma will also gain entry into Japan, a market with high growth potential and low penetration of generic drugs.⁴⁸ Sun Pharma has estimated that it will save ~USD 250 million in the third year of the merger/ amalgamation because of operating synergy.⁴⁹ The Transaction will create the No. 1 drug company in India with a market share of approximately 9% and the fifth largest generic drug firm globally.

B. Diversified Product Portfolio

A combined Sun Pharma and Ranbaxy will have a diverse, highly complementary portfolio of specialty

and generic products marketed globally, including 445 ANDAs. Additionally, the combination will create one of the leading dermatology platforms in the United States.⁵⁰ Sun Pharma will also get access to Ranbaxy's new product pipeline including a generic version of AstraZeneca's heartburn drug Nexium.⁵¹ A diversified product portfolio is important from a business risk control perspective, with emerging markets leaning towards generic drugs and customers in developed markets preferring to use branded products. Further, rising healthcare costs and increasing awareness of the efficacy of generics has also led to a surge in demand for generics in the developed world.

Mr. Dilip Shanghvi, the promoter of Sun Pharma, had mentioned that resolving Ranbaxy's regulatory troubles would be his priority, saying "*For Sun, it is not the size of the deal which matters...it is the quality of business (we acquire) and its integration*".⁵² He further said that Sun Pharma's primary focus will be to comply with regulatory standards, a key issue Ranbaxy is facing now, and make it healthy "*before jumping into the business priorities*".⁵³

Sun Pharma is believed to have chalked out a detailed turnaround plan for Ranbaxy and prepared a three-pronged strategy which includes integration of supply chain and field force for enhanced efficiency and productivity, resolution of regulatory issues and higher growth through synergy in domestic and emerging markets.⁵⁴ It is believed that Sun Pharma is targeting a three- to four-year period after the closure of the transaction to engineer the full turnaround of Ranbaxy.⁵⁵

47. <http://businesstoday.intoday.in/story/ranbaxy-acquisition-good-for-sun-pharma-shareholders-experts/1/205526.html>, last accessed on June 24, 2014

48. Ibid

49. <http://www.livemint.com/Companies/7eHPFVf901sTO45WGBZtvI/Sun-Pharma-Ranbaxy-deal-Layoffs-supply-synergy-key-to-25.html>, last accessed on June 24, 2014

50. <http://www.ranbaxy.com/sun-pharma-to-acquire-ranbaxy-in-a-us4-billion-landmark-transaction/>, last accessed on June 24, 2014

51. <http://in.reuters.com/article/2014/04/07/daiichi-sankyo-ranbaxy-sunpharma-idINDEEA3600G20140407>, last accessed on June 24, 2014

52. <http://www.livemint.com/Companies/vgtqo21KleW4Cl8Wcf9ymL/Sun-Pharmas-another-bold-acquisitionRanbaxy-Laboratories.html>, last accessed on June 24, 2014

53. Ibid

54. http://www.business-standard.com/article/companies/sun-pharma-draws-up-plan-to-fix-ailing-ranbaxy-114091101300_1.html

55. Ibid

II. Will Dilip Shanghvi be able to turn around Ranbaxy?

In spite of the troubles experienced by Ranbaxy from the USFDA, the Transaction offers a great value proposition to Sun Pharma as Ranbaxy's manufacturing units, along with the range of globally-marketed specialty and generic products and new drug launches will belong to Sun Pharma, on successful consummation of the Transaction.⁵⁶ Apart from Sun Pharma, two private equity funds and one strategic investor too were eyeing Ranbaxy.⁵⁷ Sun Pharma, with its experience may help implement a solution to the quality control issues plaguing Ranbaxy. Sun Pharma has a successful track record of turning around distressed assets.⁵⁸ For example, in 2010, Sun Pharma bought all the outstanding shares of U.S.-based Caraco Pharmaceutical Laboratories ("Caraco") at a time when Caraco was struggling to address manufacturing quality concerns that led to USFDA bans on its plants.⁵⁹ Sun Pharma was able to resolve those issues and Caraco plants resumed production in 2012.⁶⁰ A major upside from the deal could be Ranbaxy's product portfolio. Though many of the first-to-file applications of Ranbaxy are pending in the US, they have the potential to give a major boost to revenues once approval comes through. Sun Pharma's efforts towards resolving Ranbaxy's regulatory issues with the USFDA can reap lucrative results in future.⁶¹ Further, it would be interesting to see how Sun Pharma handles Daiichi's misrepresentation allegation against the former shareholders of Ranbaxy for concealment of certain critical information relating to Ranbaxy at the time of acquisition by Daiichi.

The combined entity's revenues are estimated at USD 4.2 billion with EBITDA⁶² of USD 1.2 billion for the twelve month period ended December 31, 2013.⁶³ The transaction value implies a revenue multiple of 2.2 based on 12 months ended December 31, 2013.⁶⁴

III. Why was the Transaction structured as a merger?

In the past, M&As in the pharmaceuticals sector have been effected through various modes such as direct acquisition of shares of the target entity or through business transfer.⁶⁵ The Transaction has been structured as a merger for variety of commercial, legal and tax reasons.

In addition to the legal, regulatory and tax implications of a merger structure, there may also be certain commercial reasons for the structure adopted for the Transaction. For a direct acquisition, an acquirer needs to have significant reserves of cash available or accessible sources of leverage for purchasing the shares of the target from its shareholders. While Sun Pharma may have sufficient cash surplus for direct acquisition of the shares of Ranbaxy, a direct acquisition would have taken away a significant chunk out of Sun Pharma's cash reserves. Such cash reserves may be more effectively deployed for future expansion or R&D activities or in ensuring compliance of Ranbaxy's facilities with USFDA norms.

Further, since the Transaction is a domestic transaction with both the acquirer and the target based in India, it would be difficult to obtain leverage for the purpose of acquisition of shares. Indian banks are prohibited by the Reserve Bank of India ("RBI") from lending for the purpose of acquiring shares of an Indian company.⁶⁶ Further, availing of foreign debt may have been prohibitively expensive for Sun Pharma. Section 14A of the Income Tax Act, 1961⁶⁷ ("ITA") states that no deduction shall be allowed for expenditure incurred in relation to earning tax-exempt income. The interest expense incurred in respect of such loans may not be allowed as a deductible expense for Sun Pharma as the income derived from the shares of Ranbaxy by way of

56. http://www.business-standard.com/article/management/expert-take-brand-ranbaxy-may-be-axed-114040701135_1.html, last accessed on June 24, 2014

57. http://www.business-standard.com/article/companies/sun-pharma-draws-up-plan-to-fix-ailing-ranbaxy-114091101300_1.html

58. <http://in.reuters.com/article/2014/04/07/us-daiichi-sankyo-ranbaxy-sunpharma-idINBREA3600L20140407>, last accessed on June 24, 2014

59. Ibid

60. Ibid

61. http://www.business-standard.com/article/companies/sun-pharma-draws-up-plan-to-fix-ailing-ranbaxy-114091101300_1.html

62. Earnings before interest, tax, depreciation and amortization

63. <http://www.ranbaxy.com/sun-pharma-to-acquire-ranbaxy-in-a-us4-billion-landmark-transaction/>, last accessed on June 24, 2014

64. Ibid

65. The acquisition of the formulations business of Piramal Healthcare Limited by Abbott Healthcare Private Limited was done through a business transfer. For more information regarding the Piramal – Abbott deal, please refer to our M&A Lab at <http://www.nishithdesai.com/information/navigation/navigation2/ma-lab/ma-lab/article/piramal-ndash-abbott-deal-the-great-indian-pharma-story.html>, last accessed on June 24, 2014.

66. RBI's Master Circular- Loans and Advances – Statutory and Other Restrictions dated July 1, 2013, http://www.rbi.org.in/scripts/BS_ViewMasCirculardetails.aspx?id=8135, last accessed on June 24, 2014

67. Section 14A of the Income-tax Act, 1961 provides for disallowance of expenditure in relation to income not "includible" in total income.

dividends would not have been taxable in the hands of Sun Pharma.

Overall, the structure adopted for the Transaction appears to be a win-win strategy for Sun Pharma as well as the shareholders of Ranbaxy. Sun Pharma retains its cash surplus, while the shareholders of Ranbaxy receive shares of Sun Pharma in exchange.

5. Legal and Regulatory Considerations

I. What are the exchange control implications of the Transaction?

A. FDI in Pharmaceuticals – History

Prior to 2011, foreign direct investment (“FDI”) up to 100 percent was permitted in the pharmaceutical sector under the automatic route. However, following the acquisitions of various home grown Indian pharmaceutical companies such as Ranbaxy by Daiichi in 2008, Shanta Biotech by Sanofi Aventis of France in 2009 and Piramal Health Care’s formulation business by Abbott Laboratories of the US in 2010⁶⁸, the Indian Government adopted a cautious approach in 2011⁶⁹ bringing all the investment in the brownfield pharmaceutical sector, under the government approval route. The Indian Government’s actions may have been driven by the concern that the entry of foreign pharmaceutical manufacturers into the Indian market may drive up prices of essential drugs, leading to basic healthcare becoming expensive and therefore, inaccessible to a large chunk of the Indian population.

B. FDI Issues and Approval from the Foreign Investment Promotion Board

Under Circular 1 of 2014 notified by the Department of Industrial Policy and Promotion (“FDI Policy”), foreign investment in the pharmaceuticals sector is permitted up to 100 percent in both greenfield and brownfield projects.⁷⁰ In a greenfield project, FDI of up to 100 percent is permitted under the automatic route and in a brownfield project, FDI of up to 100 percent is permitted with approval from the Foreign Investment Promotion Board (“FIPB”). Also, for both such kind of investments, ‘non-compete’ clause is not allowed except in special circumstances with the approval of the FIPB. It is to be noted that the general approach of the FIPB seems to be positive as it has been granting approvals to most of the FDI proposals in brownfield projects.

As discussed above, as a result of the Transaction, Daiichi will become the second largest shareholder in Sun Pharma with a stake of ~9 percent. Since Daiichi’s holding in Sun Pharma, on successful consummation of the Transaction will be a brownfield investment, Daiichi shall be required to obtain approval from the FIPB. Similarly, approval of the FIPB would also be required for the other non-resident shareholders of Ranbaxy obtaining shares in Sun Pharma.

C. ODI Filings

Ranbaxy has a subsidiary in the Netherlands, which will be owned by Sun Pharma post the successful consummation of the Transaction. Under the provisions of RBI’s Master Circular on Direct Investment by Residents in Joint Venture (JV) / Wholly Owned Subsidiary (WOS) Abroad dated July 1, 2013 (“ODI Regulations”), Sun Pharma would be required to report the details of such change in shareholding pattern of the overseas subsidiary to the RBI, within 30 days of the approval of the decision by the board of the subsidiary in terms of local laws of the host country and include the same in the Annual Performance Report required to be forwarded to the AD Category-I bank.

Further, under the ODI Regulations, an Indian party is permitted to invest in overseas Joint Ventures (“JV”) / Wholly Owned Subsidiaries (“WOS”), not exceeding 400 percent of the net worth as on the date of last audited balance sheet of the Indian party. Post successful consummation of the Transaction, Sun Pharma would have to make filings in Form ODI along with all prescribed enclosures/ documents and ensure that its combined investments in JVs and WOS abroad does not exceed 400 percent of its net worth as on the date of its last audited balance sheet. If an Indian company proposes to directly invest more than 400 percent of its net worth in an offshore JV or WOS, the RBI may consider such proposal under the approval route. However, any financial commitment exceeding USD 1 billion (or its equivalent) in a financial year by an Indian party would require prior approval of the RBI even when

68. http://zeenews.india.com/business/news/economy/fdi-in-pharma-ministerial-group-may-take-final-call-tuesday_56426.html, last accessed on June 24, 2014

69. RBI/2011-12/296 A. P. (DIR Series) Circular No.56 dated December 09, 2011

70. A greenfield investment is a type of venture where finances are employed to create a new physical facility for a business in a location where no existing facilities are currently present, whereas a brownfield investment implies investment into an existing production facility, typically for the purpose of a new product release.

the total financial commitment of the Indian party is within the limit of 400% of its net worth as per the last audited balance sheet.

II. What is the procedure under the Companies Act, 1956 for merger/ amalgamation of companies?

Even though most provisions of CA 2013 have been notified by the Ministry of Corporate Affairs, the provisions relating to M&A have not been notified as of April 1, 2014. Therefore, the scheme of merger/ amalgamation would have to be executed under the provisions of CA 1956.

Sections 391 to 394 of the CA 1956 lay down the procedure for mergers and amalgamations.

- Following approval of the scheme by the boards of the merging and surviving companies, the companies are required to file the scheme with the High Court situated in the jurisdiction of their respective registered offices.
- Prior to the scheme being presented before the court, listed companies are also required to file the proposed scheme with the stock exchanges where the equity shares of such companies are listed, for approval.
- On receiving the scheme, the High Court shall give directions fixing the date, time and venue and quorum for the members' meeting and appoint a Chairman to preside over the meeting and submit a report to the Court. The scheme should be approved by a majority of the shareholders representing at least three-fourths in value of the shareholders of each of the companies, present and voting.
- The resolution of the shareholders approving the scheme should be filed with the Registrar of Companies within 30 days of passing the resolution.
- Within 7 days from the date of the meeting of shareholders, the chairman of the general meeting is required to submit a report to the High Court, setting out the number of persons who attended personally or by proxy and the percentage of shareholders who voted in favor of the scheme as well as the resolution passed by the meeting.
- Within 7 days of the chairman submitting the report, the merging and surviving companies shall make a joint petition to the High Court for approving the scheme.
- On receipt of the petition for amalgamation under Section 391 of the CA 1956, the court is required to give notice of the petition to the Regional Director, Company Law Board ("RD") and will take into consideration, any representations made by him.
- The Ministry of Corporate Affairs, has by way of General Circular 01/ 2014 dated January 15, 2014, instructed the RDs to obtain inputs and comments from the Income Tax Department, while furnishing their report to the court.⁷¹ This is to ensure that the proposed scheme of amalgamation has not been designed in such a way as to defraud the tax department.⁷²
- If there are no objections to the scheme from the RD or any other person entitled to oppose the scheme, the court may after hearing the petition, pass an order approving the scheme.
- The companies may then file the court's order with the Registrar of Companies in their respective jurisdictions, as required under Section 394(3) of the CA 1956.

It would be interesting to analyze the situation where the M&A provisions under CA 2013 are notified prior to approval of the scheme by the High Courts. In such a case, the Ministry of Corporate Affairs may issue a notification exempting all companies which have filed their schemes prior to the notification of the M&A provisions under CA 2013 from the requirement of following the process for scheme of merger under CA 2013.

71. http://www.mca.gov.in/Ministry/pdf/General_Circular_1_2014.pdf, last accessed on June 24, 2014

72. http://www.itatonline.org/info/wp-content/files/CBDT_directive_mergers.pdf, last accessed on June 24, 2014

III. What are the compliances to be carried out by Sun Pharma and Ranbaxy with respect to SEBI and the Stock Exchanges?

A. Stock Exchange

Sun Pharma and Ranbaxy both being listed on the BSE as well as the NSE, are required to comply with the existing Clause 24(f) of the Listing Agreement which mandates them to file a proposed scheme with the stock exchange, for approval, at least a month before it is presented to the court or tribunal.

B. SEBI Circulars

Further, under the provisions of the SEBI Circular No. CIR/CFD/DIL/5/2013 dated February 4, 2013⁷³ (“**February 4 Circular**”), read with the provisions of SEBI Circular No. CIR/CFD/DIL/8/2013 dated May 21, 2013 (“**May 21 Circular**”), there are certain obligations required to be met by listed companies:

- i. Paragraph 5.2 of the February 4 Circular requires the listed company to place the valuation report obtained from an independent chartered accountant before their audit committee for approval.
- ii. Companies listed on any stock exchange having nationwide terminals and/ or a regional stock exchange are required to choose the stock exchange having nationwide trading terminals as the designated stock exchange for the purpose of coordinating with SEBI, under Paragraph 5.3 of the February 4 Circular read with Paragraph 5 of the May 21 Circular.
- iii. Under Clause 5.4 of the February 4 Circular, listed companies shall be required to: (a) include the observation letter of the stock exchanges, in the notice sent to the shareholders seeking approval of the scheme; and (b) bring the same to the notice of the High Court at the time of seeking approval of the scheme.
- iv. Under Clause 5.11 of the February 4 Circular, the listed company shall disclose the draft scheme and all the relevant documents on its website

immediately upon filing of the draft scheme with the stock exchanges. It shall also disclose the observation letter of the stock exchanges on its website within 24 hours of receiving the same.

- v. In addition, under Clause 5.13 of the February 4 Circular, all complaints/comments received by SEBI on the draft scheme shall be forwarded to the designated stock exchange, for necessary action and resolution by the company. The company shall submit to stock exchanges a ‘Complaints Report’ which shall contain the details of complaints/comments received by it on the draft scheme from various sources prior to obtaining observation letter from stock exchanges on the draft scheme.

C. Insider Trading Regulations

Further, there are certain disclosure obligations on Ranbaxy’s directors, officers, promoters or persons belonging to the promoter group under the provisions of Regulation 13 of SEBI (Prohibition of Insider Trading) Regulations, 1992 (“**SEBI Insider Trading Regulations**”) which are required to be made with the stock exchange on which the company is listed, in case of change in shareholding or voting rights of such persons.

D. Takeover Code

Since the Transaction is structured by way of merger, Sun Pharma would be exempt from the obligation to make an open offer, since under the provisions of Regulation 10(1)(d) of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (“**Takeover Code**”), an acquisition pursuant to a scheme of arrangement involving the target company as a transferor company or as a transferee company, including merger pursuant to an order of a court, is exempt from the requirement to make an open offer under Regulations 3 and 4 of the Takeover Code subject to certain reporting requirements.⁷⁴

Ranbaxy and Daiichi hold ~46 percent and ~20 percent in Zenotech Laboratories Limited (“**Zenotech**”). Since the Transaction would involve Sun Pharma acquiring 55 percent of the shareholding in Ranbaxy, post consummation of the Transaction, it would enable Sun Pharma to exercise ~25 percent voting rights indirectly in Zenotech. This would be considered as indirect acquisition of voting rights under the provisions of Regulation 5 of the Takeover

73. http://www.sebi.gov.in/cms/sebi_data/attachdocs/1359986006632.pdf, last accessed on June 24, 2014

74. Reporting as required under Regulation 10(6) of the Takeover Code would have to be complied.

Code. Accordingly, Sun Pharma on April 11, 2014, made an open offer to the equity shareholders of Zenotech for shares constituting 28.1 percent of the fully diluted voting capital of Zenotech.

IV. What were the challenges faced by the Transaction in respect of the SEBI Insider Trading Regulations?

On April 30, 2014, the Andhra Pradesh High Court ordered the BSE and NSE not to approve the Transaction until it decided on a petition alleging insider trading in the shares of Ranbaxy in the days leading to the announcement of the Transaction. The court issued the order pursuant to a writ petition filed by a group of investors who claimed that entities with prior knowledge of the deal illegally profited to the extent of INR 2.85 billion.⁷⁵ Shares of Ranbaxy, which is majority-owned by Japan's Daiichi-Sankyo, saw an unusual increase in price and turnover during six trading days before the deal was announced on April 6.⁷⁶ The price of Ranbaxy shares rose by almost 33 percent between March 28, 2014 and April 4, 2014.⁷⁷ Retail investors say that Ranbaxy and Sun Pharma, as well as Silverstreet Developers LLP, an entity related to Sun Pharma⁷⁸ had used price sensitive information to their benefit, and to the detriment of the retail investors.

Silverstreet Developers LLP held ~1.64 percent stake in Ranbaxy as on March 31, 2014.⁷⁹ Sun Pharma clarified that the purchase of shares of Ranbaxy by Silverstreet Developers LLP does not

violate insider trading rules, since both partners of Silverstreet Developers LLP are wholly owned subsidiaries of Sun Pharma.⁸⁰ Hence, all benefits flowing from the investment in Ranbaxy shall accrue to Sun Pharma.⁸¹ Further, it is also understood that such shares held by Silverstreet Developers LLP shall be cancelled and no further shares of Sun Pharma will be issued to Silverstreet upon the completion of the merger.

Based on the writ petition, the Andhra Pradesh High Court, issued notices to SEBI, BSE, NSE, Sun Pharma, Ranbaxy, Daiichi Sankyo and Silver Street Developers LLP to maintain status quo. On May 13, 2014, Sun Pharma moved the Supreme Court of India against the status quo ordered by the Andhra Pradesh High Court in the Transaction.⁸² On May 21, 2014, the Supreme Court of India, after hearing the appeal, directed the Andhra Pradesh High Court to decide the issue and posted the case for hearing on May 27, 2014.⁸³ On May 24, 2014, the Andhra Pradesh High Court vacated the status quo order it issued, clearing the way for the BSE, the NSE and SEBI to scrutinize the scheme and grant their assent to the Transaction.

Under the provisions of the SEBI Insider Trading Regulations, an “insider”⁸⁴ is prohibited from dealing in securities of a listed company, either on his behalf or on behalf of any other person, when in possession of any unpublished price sensitive information.⁸⁵ Silverstreet Developers LLP may be considered an “insider” by virtue of its shareholding in Ranbaxy. However, with the Andhra Pradesh High Court exonerating Silverstreet, all claims as to insider trading have been dropped.

75. <http://economictimes.indiatimes.com/industry/healthcare/biotech/pharmaceuticals/andhra-pradesh-high-court-puts-on-hold-sun-ranbaxy-deal-till-insider-trade-verdict/articleshow/34374788.cms>, last accessed on June 24, 2014

76. Ibid.

77. M&A Critique, Vol. XXIII, Issue No. 9, May 2014

78. Silverstreet Developers LLP has two partners, both of whom are wholly owned subsidiaries of Sun Pharma.

79. <http://www.bseindia.com/corporates/shpperent.aspx?scripcd=500359&qtrid=81&CompName=RANBAXY%20LABORATORIES%20LTD%20&QtrName=March%202014>, last accessed on June 24, 2014

80. <http://businesstoday.intoday.in/story/sun-pharma-denies-insider-trading-charges-in-ranbaxy-deal/1/205032.html>, last accessed on June 24, 2014

81. Ibid

82. <http://www.livemint.com/Companies/bIIFzrFQoZvWgTEuPhB2v/Sun-Pharma-moves-SC-against-stay-on-Ranbaxy-merger.html>, last accessed on June 24, 2014

83. <http://www.thehindubusinessline.com/companies/apex-court-to-consider-on-may-27-pleas-of-sun-pharma-ranbaxy-challenging-stay-order/article6032265.ece>, last accessed on June 24, 2014

84. For the purposes of the SEBI Insider Trading Regulations, an “insider” means any person who is or was connected with the company or is deemed to have been connected with the company and is reasonably expected to have access to unpublished price sensitive information in respect of securities of a company, or has received or has had access to such unpublished price sensitive information.

85. Price sensitive information means any information which relates directly or indirectly to a company and which if published is likely to materially affect the price of securities of company, and may include (i) periodical financial results of the company, (ii) intended declaration of dividends (both interim and final), (iii) issue of securities or buy-back of securities, (iv) any major expansion plans or execution of new projects, (v) amalgamation, mergers or takeovers, (vi) disposal of the whole or substantial part of the undertaking, (vii) and significant changes in policies, plans or operations of the company etc.

V. Which Anti-Trust approvals would be required for the consummation of the Transaction?

A. Competition Commission of India

i. Competition law in Respect of Merger

Competition law in India is governed and regulated by the Competition Act, 2002 (the “**Competition Act**”) together with Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011 (“**Combination Regulations**”). Sections 5 and 6 of the Competition Act prohibit a ‘combination’ which causes or is likely to cause an ‘appreciable adverse effect on competition’ (“**AAEC**”)⁸⁶ in the relevant market in India, and treat such combinations as void. “Combination”, for the purposes of the Competition Act includes a merger or amalgamation between or among enterprises that exceed the ‘financial thresholds’ prescribed under the Competition Act.

ii. Timeline for CCI notification in Case of Mergers

In case of merger, Section 6 of the Competition Act requires the enterprises to notify the CCI of a combination within 30 calendar days of final approval of the proposal of merger or amalgamation by the board of directors of the enterprises concerned. Within 30 days of the notification to CCI, the CCI shall issue a prima facie opinion of whether there would be AAEC. CCI’s order dated August 14, 2012 in the matter of Aditya Birla Nuvo Limited (“**Order**”) suggests that the ‘final’ board approval would be the one where the swap ratio, the draft scheme, the valuation and the assets to be transferred amongst other things, are approved by the board. However, the Order does not clarify whether the 30 day time limit for notifying the CCI begins from the date of the last of the merging companies’ boards approving the

merger or the first of such merging companies’ board of directors approving the merger.⁸⁷

iii. Compulsory waiting period for a Combination to take Effect

The Combinations Regulations mandate CCI to form a prima facie opinion on whether a combination has caused or is likely to cause an AAEC within the relevant market in India, within 30 days of filing. The combination will become effective only after the expiry of 210 days from the date on which notice is given to the CCI, or after the CCI has passed an order approving the combination or rejecting the same

iv. Trigger for CCI notification in Case of Merger

If the combination exceeds the financial thresholds then the merger is subject to pre clearance of the CCI. Financial thresholds prescribed under the Competition Act for determining ‘combinations’ are as follows⁸⁸:

- A merger or amalgamation where the transferor and transferee jointly have, or where the resulting entity has, (i) assets valued at more than INR 15 billion (~USD 250 million) or turnover of more than INR 45 billion (~USD 750 million), in India; or (ii) assets valued at more than USD 750 million in India and abroad, of which assets worth at least INR 7.5 billion (~USD 125 million) are in India, or, turnover more than USD 2,250 million in India and abroad, of which turnover in India should be at least INR 22.5 billion (~USD 375 million).
- A merger or amalgamation where the group⁸⁹ to which the resulting entity belongs, has (i) assets valued at more than INR 60 billion (~USD 1,000 million) or turnover of more than INR 180 billion (~USD 3,000 million), in India; or (ii) assets valued at more than USD 3 billion in the aggregate in India and abroad, of which assets worth at least INR 7.5 billion (~USD 125 million) should be in India, or turnover of more than USD 9 billion in India and abroad, including at least INR 22.5 billion (~USD 375 million) in India.

86. Under the Competition Act, certain horizontal agreements – price fixing, bid-rigging and market allocation – are presumed to have an appreciable adverse effect on competition. Other restraints, including vertical restraints, mergers and alleged abuse of dominance are analyzed under a balancing test to determine whether they have an appreciable adverse effect on competition.

87. Our analysis of the Order is available at http://www.nishithdesai.com/information/research-and-articles/nda-hotline/nda-hotline-single-view/article/fit-conference-1.html?no_cache=1&cHash=4c83eb5c9d11eda65cb403885ffdcda1, last accessed on June 24, 2014

88. Assuming the exchange rate to be 1 USD = INR 60.

89. For the purposes of Section 5 of the Competition Act, “group” means two or more enterprises which, directly or indirectly, are in a position to —
 (i) exercise twenty-six percent. or more of the voting rights in the other enterprise; or
 (ii) appoint more than fifty percent. of the members of the board of directors in the other enterprise; or
 (iii) control the management or affairs of the other enterprise;

It is important to note that in case of a merger under Section 5(c) of the Competition Act, the thresholds need to be determined with respect to the surviving entity after the merger; or the group to which the enterprise remaining after the merger would belong after the merger. In calculating the assets and turnover of the group, it is necessary to do so assuming that the merger has already taken place.

iv. How is AAEC determined?

While determining whether there is AAEC, the CCI looks at the following factors:

- Whether there is likelihood that the combination would enable the parties to significantly and sustainably increase prices or profit margins.
- Whether there is any adverse effect on competition likely to be suffered by the 'relevant market'.
- To what extent would substitute products be available or are likely to be available in the market.

VI. What steps did the CCI take for investigating the Transaction?

On July 29, 2014, the CCI issued a show cause notice to Sun Pharma and Ranbaxy, asking the companies why a public investigation should not be ordered into the Transaction, stating that the Transaction would result in significant market domination by one company and could affect the prices of life-saving drugs in the domestic market.⁹⁰ The major concern of the CCI appears to be the combined entity's highly concentrated market in its portfolio of certain drug formulations.⁹¹

On August 28, 2014, after the first phase of investigation, CCI found that there would be AAEC if the Transaction is consummated, and ordered a second stage inquiry into the Transaction and issued orders to Sun Pharma and Ranbaxy under Section 29(2) of the Competition Act, 2002 to make public, specific details of the Transaction in Form IV within 10 days of the date of the order.⁹² The CCI has stated that the public consultation process has been initiated "in order to determine whether the combination has or is likely to have an appreciable adverse effect on competition in the relevant market in India".⁹³

On September 4, 2014, CCI invited comments/objections/ suggestions in writing, from any person(s) adversely affected or likely to be affected by the combination, in terms of Section 29(3) of the Competition Act. The comments were to be submitted to CCI by September 25, 2014.

VII. Did CCI approve the Transaction?

The CCI approved the Transaction subject to certain conditions.

A. Observations of CCI

The CCI in its order observed that both Sun Pharma and Ranbaxy are engaged in the manufacture, sale and marketing of various pharmaceutical products including formulations/ medicines and APIs. Both Sun Pharma and Ranbaxy are predominantly generics manufacturers.

The CCI, in its order noted that:

"The various generic brands of a given molecule are chemical equivalents and are considered to be substitutable. Therefore, the molecule level would be most appropriate for defining relevant markets on the basis of substitutability. Alternatively, pharmaceutical drugs falling within a therapeutic group may also be considered as constituting a potential relevant market. However, in this regard

90. <http://www.livemint.com/Companies/PwftvxqaZovojwb8GzWEEdK/Sun-PharmaRanbaxy-deal-in-CCI-crosshairs.html>, last accessed on September 8, 2014

91. Ibid

92. http://www.bseindia.com/xml-data/corpfiling/AttachHis/Ranbaxy_Laboratories_Ltd_280814.pdf, last accessed on September 8, 2014

93. http://articles.economictimes.indiatimes.com/2014-09-04/news/53563606_1_ranbaxy-labs-cci-chairman-ashok-chawla-molecules, last accessed on September 8, 2014

*it is noted that the pharmaceutical drugs within a group may not be substitutable because of differences in the intended use, mechanism of action of the underlying molecule, mode of administration, contra-indications, side effects etc. Moreover, in generics markets, competition primarily takes place between different brands based on the same molecule.*⁹⁴

Based on the above observation, the CCI defined the relevant product market at the molecule level, i.e., medicines and formulations based on the same API may be considered to constitute a separate relevant product market. CCI determined that, post the consummation of the Transaction, the combined entity would have a cumulative market share of 9.2 percent. In addition, there would also have been a significant horizontal overlap in terms of the molecules/ formulations offered by the combined entity, i.e., 37 molecules/ formulations where the combined market share would be more than 15 percent, 2 molecules/ formulations where the combined market share would be above 90 percent and multiple molecules/ formulations where market share is above 50 percent.

B. Order of CCI

The CCI by way of its order dated December 5, 2014 approved the Transaction with certain conditions, such as divestment of 7 brands.⁹⁵ The CCI was of the opinion that the Transaction is likely to have an AAEC in India for 7 formulations.

Accordingly, CCI proposed modifications to the scheme in terms of Section 31(3) of the Competition Act, by way of letters dated November 27, 2014 and November 28, 2014. The CCI proposed that:

i. Sun Pharma shall Divest

- a. All products containing Tamsulosin + Tolterodine which are currently marketed and supplied under the Tamlet brand name.

- b. All products containing Leuprorelin which are currently marketed and supplied under the Lupride brand name.

ii. Ranbaxy shall Divest

- a. All products containing Terlipressin which are currently marketed and supplied under the Terlibax brand name.
- b. All products containing Rosuvastatin + Ezetimibe which are currently marketed and supplied under the Rosuvas EZ brand name.
- c. All products containing Olanzapine + Fluoxetine which are currently marketed and supplied under the Olanex F brand name.
- d. All products containing Levosulpiride + Esomeprazole which are currently marketed and supplied under the Raciper L brand name.
- e. All products containing Olmesartan + Amlodipine + Hydrochlorothiazide which are currently marketed and supplied under the Triolvance brand name.

Further, under the order, Ranbaxy and Sun Pharma would be required to divest the above brands within 6 months of the date of the order.

VIII. Which approvals are required for the Transaction from a US anti-trust perspective?

The Hart-Scott-Rodino Antitrust Improvements Act, 1976 (“**HSR Act**”) was first passed into law in 1976. The law generally establishes the requirements for filing notifications with the Federal Trade Commission and the Assistant Attorney General at the time of combination/ mergers between two corporate entities.

There are three parts to test the proposing transactions for filing under HSR Act, and all three parts need to be concurrently fulfilled in order to file under the HSR:

94. <http://cci.gov.in/May2011/OrderOfCommission/CombinationOrders/C-2014-05-170.pdf>

95. <http://cci.gov.in/May2011/OrderOfCommission/CombinationOrders/C-2014-05-170.pdf>

i) Commercial test	Where the target or buyer is engaged in U.S. commerce.
ii) Size of transaction test (New threshold, with effect from February 24, 2014)	Any transaction with a deal value above USD 75.9 million. ⁹⁶
iii) Size of parties test (New threshold, with effect from February 24, 2014)	(A) the bigger party in the transaction has annual sales or total assets greater than USD 151.7 million or (B) the smaller party in the transaction has annual sales or total assets greater than USD 15.2 million. ⁹⁷

The size of Parties Test would be inapplicable in case of transactions over USD 303.4 million and will require filing/reporting under the HSR Act.⁹⁸

The Deal is qualified to come under the purview of the HSR Act as both Sun Pharma and Ranbaxy have sizeable business in the US. There is a 30-day mandatory review period after filing before consummation. The approval from the Federal Trade Commission is still pending.⁹⁹ It has been reported that the Transaction is close to obtaining approval from the Federal Trade Commission. Post consultation with the Federal Trade Commission, the combined entity would most likely be required to divest only one drug for the Transaction to be approved.¹⁰⁰

IX. What are the other regulatory issues involved in the Transaction?

A. Pharmaceutical Licenses

Upon successful consummation of the Transaction, the licenses issued by the Drug Controller General of India and the State Drug Licensing Authorities (such as State Food and Drug Administration) to Ranbaxy for all of its products will be extinguished. Sun Pharma will be required to make fresh applications to the State Drug Licensing Authorities for manufacturing and sale of Ranbaxy's products under the Drugs and Cosmetics Act, 1940 read with the Drugs and Cosmetics Rules, 1945. In addition, Sun Pharma would also have to obtain a no-objection certificate from the Drug Controller General of India for exporting its products, if such products include unapproved or approved new drugs or prohibited drugs.

B. Indirect Tax Registrations

Post the consummation of the Transaction, Sun Pharma would be required to obtain fresh VAT registrations in the states where Ranbaxy's products are sold.

C. Successor Liability

In case of a merger of two corporations, a successor corporation will be liable for the debts and liabilities of the predecessor corporation. In the event of the successful consummation of the merger between Ranbaxy and Sun Pharma, the surviving entity, i.e., Sun Pharma would have to shoulder the debts and liabilities of Ranbaxy which existed prior to the merger. As discussed earlier, Ranbaxy had recently received a subpoena from the United States Attorney for the District of New Jersey in respect of USFDA compliance of its plants, as well as several other regulatory actions that are still pending. Daiichi may have agreed to indemnify Sun Pharma against all liabilities arising out of such regulatory actions and/or existing liabilities of Ranbaxy. However, the scope of such indemnity is not known as the definitive documents are not available in the public domain. In the event of any losses arising out of previously existing liabilities of Ranbaxy, Sun Pharma would have to make a claim against Daiichi for indemnity against such loss.

D. Delisting

The shares of Ranbaxy will be delisted from the NSE and BSE if the merger is successfully consummated.

96. <http://www.cooley.com/revised-2014-hart-scott-rodino-antitrust-thresholds-effective-feb-24-2014>, last accessed on June 24, 2014

97. Ibid

98. Ibid

99. <http://in.reuters.com/article/2014/12/09/ranbaxy-lab-sun-pharma-regulator-idINKBN0JMIAY20141209>

100. http://www.moneycontrol.com/news/cnbc-tv18-comments/sun-ranbaxy-deal-may-soon-get-us-ftc-go-ahead_1253435.html?utm_source=ref_article

E. Change of Control Provisions Under Contracts or Financing Arrangement

Considering that Ranbaxy has operations spanning continents, it has entered into a large number of agreements with suppliers, financiers, lenders etc. The terms of these agreements may dictate that change of control of Ranbaxy shall not occur without prior notification to/ consent of the parties to such agreements. Accordingly, Ranbaxy may have to obtain prior consent/ notify the opposite parties to its agreements, prior to entering into the Transaction.

6. Tax Considerations

I. Is the Transaction tax-exempt?

Under the provisions of Section 47(vi) of the ITA, “any transfer, in a scheme of amalgamation, of a capital asset by the amalgamating company to the amalgamated company if the amalgamated company is an Indian company”, will not be considered as a ‘transfer’ for the purpose of assessment of capital gains.

Section 2 (1B) of the ITA defines ‘amalgamation’ as follows:

“amalgamation”, in relation to companies, means the merger of one or more companies with another company or the merger of two or more companies to form one company (the company or companies which so merge being referred to as the amalgamating company or companies and the company with which they merge or which is formed as a result of the merger, as the amalgamated company) in such a manner that—

- i. all the property of the amalgamating company or companies immediately before the amalgamation becomes the property of the amalgamated company by virtue of the amalgamation;*
- ii. all the liabilities of the amalgamating company or companies immediately before the amalgamation become the liabilities of the amalgamated company by virtue of the amalgamation;*
- iii. shareholders holding not less than three-fourths in value of the shares in the amalgamating company or companies (other than shares already held therein immediately before the amalgamation by, or by a nominee for, the amalgamated company or its subsidiary) become shareholders of the amalgamated company by virtue of the amalgamation,*

otherwise than as a result of the acquisition of the property of one company by another company pursuant to the purchase of such property by the other company or as a result of the distribution of such property to the other company after the winding up of the first-mentioned company

As a result of the Transaction, (i) the property of Ranbaxy immediately before the merger will become the property of Sun Pharma, (ii) all liabilities of Ranbaxy immediately before the merger will become the liabilities of Sun Pharma and (iii)

current shareholders of Ranbaxy will become the shareholders of Sun Pharma and hence, this should result in a tax-neutral transaction for both Ranbaxy and its shareholders.

II. What are the tax implications for holders of ESOPs and GDRs?

A. ESOPs

The Transaction should have tax implications for stock option holders of Ranbaxy. Post the consummation of the transaction, the Ranbaxy ESOPs will be cancelled and the holders of the Ranbaxy ESOPs will be issued Sun Pharma ESOPs in exchange. While exchange of ESOPs may be considered as transfer as per the ITA, if Ranbaxy ESOPs do not have cost of acquisition, an argument can be made that such exchange should not be subject to tax. Upon vesting of the Sun Pharma ESOPs, the difference in fair market value of Sun Pharma ESOPs and the exercise price may be taxed as salary income in the hands of such stock option holders. Further, upon transfer of the Sun Pharma shares, the difference between the consideration received and fair market value of Sun Pharma ESOPs may be taxable as capital gains.

B. GDRs

Sun Pharma would have two options to deal with the GDRs – the equity option and the cash-out option, as mentioned in the section titled ‘Details of the Deal’. One view is that the equity option is akin to conversion of the GDRs into equity shares. The report of the Committee to Review the FCCBs and Ordinary Shares (Through Depository Receipt Mechanism), 1993 had recommended that the conversion of depository receipts not be treated as a taxable event. However, currently there are no specific provisions in the ITA which exempt the conversion of GDRs from taxation and hence it’s a taxable event. The other view is that depository will receive Sun Pharma shares in exchange for Ranbaxy shares which is a tax neutral transaction and then cancel Ranbaxy GDRs against *in specie* distribution of Sun Pharma shares. The second leg will be a tax exempt transaction for the GDR holders since transfer will be from non-

resident to non-resident but may be taxable for the depository since depository may transfer shares of an Indian company to depository receipt holder off the floor of the exchange. To that extent, there is an ambiguity with respect to the tax implications of the equity option.

The cash-out option would effectively be extinguishment of the GDRs. Under Section 2(47) of the ITA, 'transfer' in relation to capital asset is defined to include the extinguishment of any rights

in such capital asset. The cash-out option may hence be treated as a transfer of capital asset from a non-resident to a resident. Section 115AC of the ITA provides for taxation of capital gains arising from transfer of global depository receipts. Therefore, capital gains arising from the exercise of the cash-out option of the GDRs may be taxable at 10 percent in the hands of the GDR holders under Section 115AC of the ITA.

7. Epilogue

The Transaction promises to bring some cheer to the Indian pharmaceutical industry. However, post the consummation of the Transaction, Sun Pharma has plans to gradually phase out the fifty-year old Ranbaxy brand, with Ranbaxy drugs sold in the United States being gradually rebranded as Sun Pharma treatments.¹⁰¹ The brand is likely to continue to be present in other markets.¹⁰²

The interest of the pharmaceuticals industry in the Transaction is fueled by two reasons – the size and reach of the resulting entity which may lead to

anti-trust issues in India as well as abroad, and the strategy to be adopted by Sun Pharma to turn around Ranbaxy. Mr. Dilip Shanghvi, the managing director of Sun Pharma is well known for acquiring and turning around distressed companies. The industry waits with bated breath to see whether Mr. Shanghvi will repeat his magic, this time with Ranbaxy. Only time will tell whether Mr. Shanghvi's magic will convert Ranbaxy into a 'crown jewel' or a 'white elephant' for Sun Pharma.

101. <http://in.reuters.com/article/2014/04/09/ranbaxy-sunpharma-idINDEEA3808E20140409>, last accessed on June 24, 2014

102. Ibid

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