THE HINDU Business Line

Dealing with the new competition laws

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The benefit of the merger control regulations in the long run will outweigh any burden that a transaction may experience in complying with these laws.

In March this year, the Government issued guidelines on the much-debated and dreaded provisions of the Competition Act, 2002 ("Act") relating to merger control regulations. This pronouncement has been viewed by the public at large with much caution, leading to debates on how Corporate India will in turn stand affected. This article attempts to analyse some similar situations.

The Act deals with 'combinations' that broadly include an acquisition of control through shares, voting rights or assets by a person; and mergers or amalgamations between enterprises, all of which must cross the financial thresholds relating to asset value/turnover value test set out in Section 5 and described below.

Regulation of combination

The Act makes void any combination which causes an appreciable adverse effect ("AAE") on competition within India. There have been subjective criteria prescribed for the Competition Commission of India (CCI) to use as a benchmark in its determination of what constitutes an AAE.

Every acquirer has to notify the CCI of a combination and seek its approval prior to effectuating the same. There are, however, certain exemptions to this rule.

Acquisitions of enterprises that have an asset value of less Rs 250 crore (approx $56 million) or a turnover of less than Rs 750 crore (approx $167 million) are exempt for a period of five years.

In certain transactions such as acquisitions of less than 15 per cent shares or voting rights, consolidation of holdings beyond 50 per cent, acquisitions by way of rights or bonus issues, and so on, the onus of determining whether or not such transactions need to be notified lies with the acquirer.

Acquisitions by public financial institutions, venture capital funds, financial institutional investors and banks have been exempted; however, a post-facto filing is required.

What does this mean for ‘deals' in India?

Strategic vs private equity investments

Private equity investments of shares less than 15 per cent may not trigger the notification requirements under the Act. However, when such acquisitions are coupled with affirmative voting rights, rights to appoint directors on the board and other similar rights, it is questionable as to whether this may be deemed to be an acquisition of control. Under the Act, ‘control' includes the ability to control the affairs or management of the investee entity with no other objective criteria prescribed.

The regulation pertaining to acquisitions lies only with respect to equity investments and not investments by way of subscription to non-convertible preference shares or non-convertible debentures. It may be worthwhile to explore these instruments while structuring a transaction.

Strategic investments, on the other hand, may be subject to the provisions of the Act. Acquisitions of smaller enterprises having an asset value of less Rs 250 crore or a turn over value of less than Rs 750 crore will not trigger the notification requirements of the Act. However, it has not been clarified as to whether these financial thresholds are limited to the value in India or to the enterprise value as a whole.

Amalgamations

Mergers/amalgamations that meet the combination qualifications would now require to approach the CCI in addition to the High Courts to obtain a sanction. The High Court approval to the scheme of amalgamation could be subject to the CCI approval, if the same has not been granted at the time of the High Court order.

Although investments by FIIs, PFIs, banks and VCFs are exempt from seeking approval of the CCI, a subsequent disinvestment by these entities is not exempt. To this extent, the transferability of such investments may be restricted. Global acquisitions that meet the combination qualifications would have to add the CCI to their pool of approvals.

Although combinations taking place entirely outside India with insignificant local nexus and effect on markets in India are ordinarily exempt from transactions under the Combination Regulations, there are no objective criteria to determine what ‘ insignificant local nexus' is.

Common issues

Timing: The maximum period that the CCI is permitted under the Act to make a decision is 210 days from the date of the filing the prescribed form or else the transaction is deemed approved. This large window is a cause for concern since the dynamics and viability of the transaction may undergo changes in this period.

Costs: The costs will now go up exponentially. The filing fees itself range between Rs 50,000 and Rs 10 lakhs. With this come legal costs, publication costs and other varied costs to meet the obligations of the parties under the Act and the orders of the CCI.

Confidentiality: There is no presumption of confidentiality in relation to the information filed with the CCI, unless confidentiality is requested. Further, there is no bar on the CCI to share such information, if required, by other regulatory/sectoral authorities under applicable law.

Inter-regulatory loops: Transactions that involve seeking approvals from multiple regulators will add to the time lines required to complete a transaction.

With every introduction of a new law, there comes a buzz of anxiety among the various sections of the industry as to the implications of the unknown.

But this new law is here to stay and, so, over a given time span, the anxieties will settle and players in the market will adjust.

The benefit of this merger control regulations law in the long run will outweigh any burden that a transaction may experience in complying with these laws. The onus is now on the regulator to achieve this objective.

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Keywords: Competition Commission of India, mergers, appreciable adverse effect, Acquisitions, Private equity

