COMPETITION COMMISSION OF INDIA

Case No. 2 of 2017

In Re:

Informant

Shri Rathi Steel (Dakshin) Ltd.

And

GAIL (India) Ltd. **Opposite Party**

CORAM:

Mr. Devender Kumar Sikri
Chairperson

Mr. S. L. Bunker
Member

Mr. Sudhir Mital
Member

Mr. Augustine Peter
Member

Mr. U. C. Nahta
Member

Mr. Justice G. P. Mittal
Member

Order under Section 26 (1) of the Competition Act, 2002

1. The information in the present case has been filed by Shri Rathi Steel (Dakshin) Ltd. (hereinafter referred to as the '**Informant'**) under Section 19(1) (a) of the Competition Act, 2002 (hereinafter referred to as the **"Act"**) against GAIL

(India) Ltd. (hereinafter referred to as the '**Opposite Party**') alleging contravention of the provisions of Section 4 of the Act.

2. The Informant is a limited company incorporated in 2006 engaged in the manufacture and sale of TMT bars. The Informant entered into a Gas Sale Agreement (hereinafter referred to as '**GSA**') with the Opposite Party on 31st March, 2009 to procure natural gas as fuel for the purpose of manufacturing at its plant located at Khushkhera, Alwar, Rajasthan.

3. The Opposite Party is a government company and is stated to be engaged, *inter alia,* in production, transmission and distribution of natural gas across India. As per the Annual Report of the Opposite Party for the FY 2014-15, it had 60% market share in supply of natural gas in India.

4. The Informant has alleged abuse of dominant position by the Opposite Party on account of incorporation of unfair terms and conditions in the GSA and for imposition of take or pay liability (hereinafter referred to as "**ToP liability**") by it despite intimation to it by the Informant that due to regular increase in the prices of Re-gasified Liquefied Natural Gas (hereinafter referred to as 'RLNG'), the Informant has been forced to reduce its daily contracted quantity. Brief details of the allegations made in the information are as under:

4.1. Alleged unfair terms and conditions in the GSA:

(a) *Make Good Gas*: The quantum of gas which has not been taken by the buyer pursuant to Downward Flexibility Quantity (DFQ) mechanism envisaged under the GSA could be requested later on by it as Make Good Gas. As per the Make Good Gas stipulation, if a buyer is unable to lift or avail the DFQ, it is liable to make good the same later on during the subsistence of the tenure of the GSA. Even if the buyer does not take the short-lifted quantity of gas, he will have to make payment for the same. In contrast, the GSA vests untrammelled discretion with the seller not to fulfil the request of the buyer for make good gas without any liability whatsoever.

(b) *Restoration Quantity*: If the gas could be supplied or taken owing to any *force majeure* event, the buyer could request the delivery of such deficiency (*Force Majeure* Deficiency [FMD]) at a later point of time. Such quantity requested is referred to as the Restoration Quantity. The buyer shall purchase and take such Restoration Quantity at the price prevailing on the date of delivery. However, the GSA does not foist any liability on the Opposite Party if it fails to supply the Restoration Quantity.

(c) *Recovery Period Gas*: Recovery Period Gas denotes the total gas outstanding at the end of the basic term of GSA. The GSA does not envisage any liability upon the seller if it fails to deliver the Recovery Period Gas despite request made by the buyer. On the contrary, if the seller tenders for delivery of the Recovery Period Gas, the buyer must take it and pay for such gas or incur ToP liability.

(d) *Quality*: As per the GSA, the Opposite Party has to supply gas of a certain specification. However, no procedure has been outlined in the GSA for testing, which would certify the gas to be specification compliant. This crucial aspect is totally left to the unilateral whims of the Opposite Party. Moreover, the Informant is powerless to raise a challenge regarding the quality of gas supplied if it finds the same not adhering with the specification standard stipulated upon carrying out inspection thereof at its own cost.

(e) *ToP liability*: Under Art. 14 of the GSA, the buyer is obliged to pay for the quantities of gas not taken but agreed to be taken. The said clause in the GSA relating to ToP liability is most abusive and unfair as the buyer has been made liable to Take or Pay for a quantity of gas which is less than the Adjusted Annual Contract Quantity (AACQ). The exploitative contents of this Article are so sweepingly worded that even if the buyer terminates the GSA by

exercising its right, its liabilities would still continue. On the contrary, there is no such liability on the Opposite Party if it withdraws from the GSA.

(f) *Force majeure*: The clause of the GSA concerning *force majeure* operates pretty unevenly between the parties in as much as while the provision identifies a large number of events as *force majeure* events for the seller, the number of *force majeure* events identified for the buyer are limited. Non-inclusion of acts of government agency in buyer's *force majeure* events and listing of a large number of events attributed to failure of LNG Tankers as *force majeure* events for the seller are unfair and abusive.

4.2. Alleged unfair conduct of the Opposite Party:

(a) Unfair conditions imposed by the Opposite Party extend beyond the GSA. For instance, in terms of the GSA, the Informant has to maintain a Letter of Credit (LoC) as security. The Opposite Party prescribes the format of the LoC from time to time, and the same is not in consonance with the GSA. The format requires a Minimum Guaranteed Off-take to be covered by the LoC. This condition sources out of nowhere and reflects the abusive mind-set of the Opposite Party manifesting through the format of the LoC prescribed by it.

(b) Another unfair element which vitiates the LoC requirement is the condition to cover ToP liability. The standard format of the LoC prescribed by the Opposite Party goes beyond the ambit of the GSA, as the same does not require the LoC to cover ToP liability.

(c) Also, the Opposite Party has not made necessary nomination in terms of the GSA thereby giving details of the monthly quantities and daily contract quantities during 2014. Without these nominations, it is impossible to compute the seller's Daily Shortfall

which in turn makes it impossible to compute the buyers' ToP liability. However, the Opposite Party has imposed ToP liability for the calendar 2014, which therefore, is not in adherence to GSA.

(d) Lastly, imposition of ToP liability despite intimation of the Informant that procurement of gas has become economically unviable is alleged to be extremely unfair. In this regard, the Informant has furnished copies of various correspondence between the Opposite Party and itself from 21st June, 2013 to 30th November, 2016. Brief details of the correspondence as presented in the information are as under:

21.06.2013	The Informant, in categorical terms, communicated to the Opposite Party that due to regular increase in the price of RLNG, it is forced to reduce its daily contracted quantity from 13500 M^3/ day to 4000 M^3/day as RLNG has become unviable.
11.12.2013	The Opposite Party insisted upon renewal of LoC which was valid upto 12.12.2013 and threatened the Informant with initiation of action as per Article 19.4 of GSA if LoC is not renewed.
05.01.2015	The Opposite Party forwarded the Annual Plan for the year 2015 for supply of 182074 MMBTU RLNG to the Informant and insisted that the Informant provides LoC as per the terms of the GSA.
19.01.2015	The Informant communicated that the same is not economically viable and therefore, it cannot afford procurement of RLNG from the Opposite Party.

20.02.2015	The Opposite Party stated that as per the GSA, the Informant has no option to stop drawl of RLNG and asked the Informant to draw RLNG as per the Annual Programme dated 05.01.2015.
27.02.2015	The Opposite Party imposed ToP liability upon the Informant by invoking Article 14(1)(c) of the GSA thereby demanding a sum of Rs.6.39 crores for the contract year 2014.
12.03.2015	The Informant challenged such demand of the Opposite Party by stressing that no liability is accrued against it as per Article 14.1 of GSA read with Article 12.2 thereof.
16.03.2015	The Opposite Party responded to the Informant again raising claim of Rs. 6.39 crores as ToP liability.
27.07.2015, 17.09.2015, 23.10.2015 and 10.12.2015	The Opposite Party asked the Informant to take gas in line with the annual contracted quantity/ Annual Programme for the Calendar Year 2015.
31.08.2015	The Opposite Party sent another demand for Rs. 10.3 crores as ToP liability of the Informant for the period January to July, 2015.
02.11.2015	The Informant strongly protested denying any obligation to make payment towards ToP for the CY-2014 or CY-2015. The Informant also reiterated that it never accepted to take gas from calendar year 2014 onwards.

03.11.2015	The Opposite Party denied the averment of the Informant and insisted that the payments demanded by it as per Article 14 of the GSA be released by the Informant.
15.12.2015	The Informant responded asserting that the Opposite Party cannot unilaterally dictate terms on the Informant who has only relative bargaining strength under the pretext of a completely one-sided, unfair and discriminatory agreement.
07.01.2016	The Opposite Party sent Annual Programme for the Calendar Year 2016 of 182074 MMBTU RLNG.
11.02.2016 and 31.03.2016	The Informant reiterated that taking RLNG gas supply was not economically viable for it and that it has already requested the Opposite Party to desist from raising any claim against it.
24.06.2016	The Opposite Party served a legal notice calling upon the Informant to pay Rs.6.39 crores towards ToP liability for the Calendar Year 2014 within 15 days failing which legal recourse would be taken.
08.07.2016	The Informant denied liability to make any payment for Calendar Year 2014 or any other year.
22.08.2016	Arbitration envisaged under Article 15.6 of the GSA was invoked by the Opposite Party.

22.10.2016	The Informant replied that no arbitrable issue had arisen between the parties. It also sought amicable settlement as per Article 15.1 of the GSA.
18.10.2016 and 30.11.2016	The Opposite Party pressurised the Informant to take RLNG in line with the annual contracted quantity for the Calendar Year 2016.

5. The Commission considered the information in its ordinary meeting held on 21st March, 2017 and decided to pass an appropriate order in due course. The Commission has given careful consideration to the information and the material available on record.

6. The Informant has alleged abuse of dominant positon by the Opposite Party in imposing unfair and discriminatory conditions in the GSA and also for indulging in unfair conduct that is not contemplated in the GSA. For the purpose of examining the allegations of the Informant under the provisions of Section 4 of the Act, it is necessary to first determine the relevant market; thereafter, assess whether the Opposite Party enjoys a position of strength required to operate independent of the market forces in the relevant market so delineated and only when such a position is found to be enjoyed by the Opposite Party, it will be imperative to examine whether the impugned conduct amounts to an abuse or not.

7. The Commission has dealt with similar issue in various cases. In Case No. 71 of 2012 (*Faridabad Industries Association (FIA) Vs M/s Adani Gas Limited*), the Commission, while examining the relevant product market, divided the consumers of natural gas into two different categories *i.e.*, industrial and domestic, based on the intended use and the price of natural gas. While industrial consumers use the purchased gas to meet fuel and energy requirements of their plants, the end use of gas in case of domestic consumers is self-consumption/ domestic cooking which is entirely different from industrial consumers. The Commission is of the view that the same reasoning

applies to the instant case as well. As the Informant is a buyer of natural gas from the Opposite Party for commercial/industrial use, the relevant product market in this case would be the market for '*supply and distribution of natural gas to industrial consumers*'.

8. As far the relevant geographic market is concerned, natural gas is generally transported through either city gas distribution network or through pipeline. Laying down of city gas distribution network or pipeline is authorised by the Petroleum and Natural Gas Regulatory Board (PNGRB) in every city/ state. While the city gas distribution network is confined to a particular city, a pipeline may pass through various States. In the instant case, the Informant is located at Khushkhera, Alwar, Rajasthan. The Informant cannot choose a supplier distributing gas in an area different from where its plant is located. Therefore, the relevant geographic market appears to be the '*district of Alwar*'. Accordingly, the relevant market in the instant matter is the *market for supply and distribution of natural gas to industrial consumers at Alwar.*

9. The Informant has claimed that the Opposite Party was and is the sole and prominent supplier of RLNG to industrial consumers including the Informant in the district of Alwar. The Commission has already noted in its earlier orders dated 3rd October, 2016 passed in Cases No. 16, 17, 18, 19 and 20 of 2016, that the Opposite Party is a significant player in the business of supply of natural gas across India with relatively larger size, resources and expertise when compared to any other player. In view of this, the Commission is of the *prima facie* view that the Opposite Party enjoys a position of dominance in the relevant market delineated in the preceding para.

10. Coming to the preliminary assessment of the alleged abusive conduct, the Commission notes that the issue of purported unfair terms of the GSA has already been dealt with in various earlier orders of the Commission including the order dated 3rd October, 2016 passed in Cases No. 16 to 20 of 2016. The Commission has held that mere possibilities under an agreement entered into

prior to the enforcement of the Act cannot be a subject-matter of examination under Section 4 of the Act. However, unfair conduct of a dominant enterprise that is aimed at exploiting consumers or excluding competition can be subjected to investigation in context of Section 4 of the Act.

11. In the instant matter, the Informant has alleged that the Opposite Party imposed ToP liability for the calendar years 2014 and 2015 notwithstanding the intimation of the Informant that procurement of RLNG has become economically unviable for it. The Informant has also alleged that the Opposite Party has not complied with various requirements of the GSA that are pre-requisites to impose ToP liability. These include failure to intimate daily contract quantities that is essential to compute seller's shortfall, which in turn is stated to be a pre-requisite to compute ToP liability. Further, the Opposite Party is alleged to have mandated the Informant to maintain a LoC for purposes not even envisaged in the GSA. These, according to the Informant, amount to abuse of dominant position by the Opposite Party in contravention of Section 4 of the Act.

12. As per the GSA, the Informant is required to take 90% of the contracted quantity every year failing which it will be obliged to pay for the quantities not taken. Such liability is termed as ToP liability. With experience from the earlier cases [Cases No. 16 to 20 of 2016], the Commission notes that the GSAs of the Opposite Party largely envisage such liability upon all customers located across different regions. All these GSAs examined by the Commission are long term contracts with a term of 20 years. This would mean that: (a) potential buyers have to estimate their demand for gas for the next two decades to procure gas from the Opposite Party; (b) a contracted buyer has limited flexibility of 10% and it has to pay Take or Pay charges if consumption of gas by it is less than 90% of the contracted quantity although the buyer could request for the unlifted quantity later as Make Good Gas; and (c) a buyer who is locked into a contract with the Opposite Party cannot terminate the contract if the price of gas becomes economically unviable for it or it wants to shift to

other cheaper alternatives as breach of obligation under the GSA would trigger ToP liability.

13. It has already been noted by the Commission in its earlier order dated 3rd October, 2016 passed in Cases No. 16 to 20 of 2016 that take or pay liability has been imposed by the Opposite Party only from the year 2015 and there was no such imposition earlier. In the case of the Informant, the Opposite Party, *vide* letter dated 27th February, 2015, has demanded Rs. 6.39/- crores as ToP charges for the calendar year 2014 as against ToP liability of Rs.16.7 crores. In 2015, the Opposite Party issued another letter dated 31st August, 2015 to the Informant demanding Rs.10.3 crores as ToP charges for the period January 2015 to July 2015. This time, full charges were demanded from the Informant and strangely, the demand seems to have been raised for a part of the year and even before issuing the annual statement of settlement.

14. The conduct of Opposite Party in implementing such ToP liability from the year 2015 appears to be a modus to ensure *de facto* exclusivity of the contractual arrangement. This, besides prohibiting the buyers from shifting to alternatives or terminating the GSA in the event of closure of their business, also appears to create entry barriers for alternative suppliers to enter the market or build up a viable customer base. It is observed that while imposition of ToP liability as per contractual terms cannot *per se* be regarded as abuse of dominant position, the same being imposed in an exploitative manner without justification or to ensure *de facto* exclusivity thereby hurdling potential entries or expansion of competitors warrants investigation under the provisions of the Act prohibiting abuse of dominant position. The Commission is, hence, convinced that the facts presented in the instant information *prima facie* suggest contravention of Section 4(2)(a) and Section 4(2)(c) of the Act.

15. The Commission is already seized with the issue of unfair imposition of ToP liability by the Opposite Party in Cases No. 16 to 20 of 2016. In those cases, the Opposite Party's stand was that *take or pay liability, as imposed on the customers, was only to neutralize the losses borne by the Opposite Party due*

to non off-take or under-drawal by the customers as per the respective GSAs, and was not to make any profits on account of take or pay deficiency. The same also formed basis of reduction in the take or pay claim by the Opposite Party. However, in the instant matter, full ToP liability has been imposed on the Informant for the calendar year 2015. In the earlier cases, the Opposite Party also contended that it faces ToP obligation under its contracts with certain upstream suppliers. In this regard, the Commission finds it relevant to inquire into: the different sources of gas procurement by the Opposite Party and the nature of arrangements with each supplier including price and ToP liability under each such arrangement; whether the gas supplied to the customers of the Opposite Party is supplied from a commingled stream, in which case, what is the basis for price determination/ revision from time to time; whether ToP liability was imposed on the Opposite Party by its upstream suppliers for the contract year 2015; whether the Opposite Party has suffered any loss on account of non off-take or under-drawl of gas by its contracted customers during the contract year 2015; what were the total ToP liabilities levied by the Opposite Party on all its customers located across India for the contract year 2015; whether the Opposite Party had adopted any discriminatory practice in imposition of ToP liability upon its customers located across India; whether the Opposite Party imposed full ToP liability only in cases where the concerned buyer contested the legality of the ToP claim or resorted to litigation/ arbitration proceedings; and the policy, if any, of the Opposite Party regarding imposition of different liability upon different class of customers. It would also be relevant to appreciate the rationale behind the Opposite Party committing ToP liability to its upstream suppliers for a long period *i.e.* whether the Opposite Party took into consideration the potential inclusions and exclusions in its customer base, fluctuations in prices, different modes of risk management *etc*.

16. In view of the above, the Commission deems it fit to order an investigation in the present case. Since the allegations in the instant matter are similar to and connected with the issues in the earlier matters already being investigated by the DG *i.e.* Cases No. 16 to 20 of 2016, in exercise of the powers conferred

under *proviso* to Section 26 (1) of the Act read with Regulation 27 of the Competition Commission of India (General) Regulations, 2009, the Commission decides to club the present case with pending Cases No. 16 to 20 of 2016. The DG shall file a consolidated investigation report in all the above-mentioned cases.

17. Accordingly, the Secretary is directed to send a copy of this order to the DG, along-with a copy of the information.

Sd/-
(Devender Kumar Sikri)
Chairperson

Sd/-
(S. L. Bunker)
Member

Sd/-
(Sudhir Mital)
Member

Sd/-
(Augustine Peter)
Member

Sd/-
(U. C. Nahta)
Member

Place: New Delhi
Date 14/07/2017

Sd/-
(Justice G. P. Mittal)
Member