COMPETITION COMMISSION OF INDIA

(Combination Registration No. C-2016/04/387**)**

11/05//2018

Notice given by LT Foods Limited and LT Foods Middle East DMCC

CORAM

Mr. Devender Kumar Sikri
Chairperson

Mr. Sudhir Mital
Member

Mr. Augustine Peter
Member

Mr. U. C. Nahta
Member

Mr. Justice G. P. Mittal
Member

Appearances during the oral hearing held on 2nd August, 2017	:	Mr. Neeraj Chaudhary, Advocate Mr. Praveen Raju, Advocate

Order under Section 43A of the Competition Act, 2002

Background:

1. On 7th April, 2016, LT Foods Limited (**LT Foods**) and LT Foods Middle East DMCC (**LT DMCC**) (hereinafter both LT Foods and LT DMCC

shall collectively be referred to as the **Acquirers**) gave a notice to the Competition Commission of India (**Commission**) under Section 6(2) of the Competition Act, 2002 (**Act**), wherein the Acquirers sought the approval of the Commission for their proposed acquisition of the business of processing of raw material for rice, marketing, distribution, export and sale of various types of rice, including trademarks and associated goodwill (**Combination**), from Hindustan Unilever limited (**HUL**). The notice was filed pursuant to the execution of a Framework Agreement on 17th March, 2016, between HUL, LT DMCC, LT Foods and Sona Global Limited, a wholly owned subsidiary of LT Foods (**Framework Agreement**).

2. The Commission approved the combination *vide* its order dated 11th May, 2017, passed under Section 31(1) of the Act. This approval was granted without prejudice to the proceedings under Section 43A of the Act.

Section 43A Proceedings:

3. Upon a perusal of the notice and further submissions made by the Acquirers, the Commission in its meeting held on 11th May, 2016 noted that in terms of Clause 3.1 (i) of the Framework Agreement, the Acquirers were required to pay an advance consideration of INR 1.70 crore to HUL, at the time of execution of the Framework Agreement. In their submission dated 27th April, 2016, the Acquirers further clarified that they had deposited the advance consideration with HUL as an indication of good faith intention to complete the proposed combination. Based on these facts, the Commission was convinced that there exist a *prima facie* case of contravention of the obligation under Section 6(2) of the Act, as the Acquirers paid a part of the consideration for combination to the HUL

even before the approval of the combination by the Commission. Therefore, the Commission decided to initiate penalty proceedings against the Acquirers under Section 43A of the Act by issuing a notice in terms of Regulation 48 of the Competition Commission of India (General) Regulations, 2009 (**General Regulations**).

4. In accordance with the directions of the Commission, a notice dated 13th June 2016 was issued to the Acquirers to show cause, in writing, within 15 days of the receipt of notice, as to why penalty in terms of Section 43A of the Act, should not be imposed upon them. The Acquirers filed their response on 24th June, 2016 along with a request for oral hearing.

5. The Commission noted that certain measures to be undertaken by HUL, in terms of the Framework Agreement, as a condition precedent to the combination or an obligation post execution of the Framework Agreement *prima facie* appear to be in contravention of the obligation of the parties under Section 6(2) read with Section 6(2A) of the Act. The details of such measures as under:

(a) *Clause 5.1 of the Framework Agreement*: HUL shall deliver upon execution date, and no later than 7 days thereof, all documents like posters, packaging labels, art work, distribution marketing materials, slogans and all such materials as would enable LT Foods to commence preparation and production of packing material as is required for the sale of the finished products;

(b) *Clause 5.4 (vi) of the Framework Agreement*: As a condition precedent, HUL shall register the trademarks being transferred in certain territories;

(c) *Clause 5.4 (ix) of the Framework Agreement*: HUL shall introduce, within seven days of the execution of the Framework Agreement, LT DMCC to designer and printer engaged by HUL for packaging and artwork of the products being transferred;

(d) *Clause 6.2(vi) of the Framework Agreement*: Between the Execution Date and the Closing Date, HUL shall not incur any new promotional spends in respect of the business being acquired;

(e) *Clause 6.2 (vii) of the Framework Agreement*: HUL shall not exit or enter into any market in respect of the business being acquired; and

(f) *Clause 6.5 of the Framework Agreement*: HUL shall provide all documents in relation to the trademarks being transferred within 30 days of the execution date of the Framework Agreement.

The Acquirers filed their submissions again on 20th February, 2017.

6. The Commission considered the matter in its meeting held on 28th June, 2017 and allowed the request of the Acquirers for an oral hearing. Accordingly, the Acquirers were heard on 2nd August, 2017. A summary of the oral and written submission of the Acquirers is as under:

Payment of advance consideration:

6.1. It is not uncommon in transaction of this nature for the acquirer to pay advance consideration/good faith deposit. The advance

consideration given is essentially a token returnable in case of the termination of the Framework Agreement. Payment of advance consideration does not result in "giving effect" to the combination as this does not result in direct or indirect acquisition of any share, voting right or asset, or acquisition of control.

6.2. In terms of the Framework Agreement, approval of the Commission under Section 31(1) of the Act is a condition precedent to the closing of the transaction. At no stage, whatsoever, it was contemplated that the combination would be given effect to pending the formal approval of the Commission.

6.3. Payment of advance consideration alone cannot determine the ability to influence the state of competition and such ability would arise only if the Acquirers exercise control over the target business.

6.4. Regulation 9(5) of The Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011 (**Combination Regulations**) provides that notification requirement shall be determined with reference to the substance of the transaction and structure of the transaction is immaterial. Drawing a parallel with the said provision, any pre-merger coordination shall also be assessed with reference to the substance of the transaction and not the structure of the same.

6.5. In international jurisdictions such as European Commission, the United States and Brazil, there have been no instances where

refundable advance consideration has been treated as violation of standstill obligations.

Obligation of HUL as a condition precedent or an obligation post execution of the Framework Agreement:

6.6. None of the measures to be undertaken by HUL, as a condition precedent to the combination or an obligation post execution of the Framework Agreement, has the effect of lessening competition between the Acquirers and HUL in India. These provisions in the Framework Agreement does not result in a combination coming into effect. Accordingly, there is no contravention of the obligation under Section 6(2) read with Section 6(2A) of the Act. The said provisions of the Act prohibit the parties from giving effect to the combination prior to the Commission's approval but do not bar ancillary or preparatory action, which are necessary to protect the value of investment by the Acquirer.

6.7. Clause 5.5 (i) of the Framework Agreement states that receipt of all necessary authorizations is a condition precedent to the closing of combination. Further, Clause 5.3 (i) states that receipt of the Commission's approval is a condition precedent to the completion of the combination. At no stage, whatsoever, it was contemplated that any effect would be given to the combination pending receipt of formal approval under Section 31(1) of the Act.

6.8. With respect to the requirement of filing applications for registration of trademarks in certain territories [Clause 5.4 (vi)], it is submitted that the same was a perfection measure, on the part of

HUL, to protect its intellectual properties and the same does not amount to pre-merger coordination. Further, HUL had not registered/applied for trade marks in Oman and UAE despite significant business interest.

6.9. On the restriction on promotional spends [Clause 6.2(vi)], it is submitted that the same was envisaged with a view to protect the investment of the Acquirers. Such stipulation protects investment from material adverse change before the closing of the combination. Promotions and advertising have a significant impact on brand outlook. It is in the *bona fide* interest of the Acquirers to prevent any new promotional spends with respect the business being acquired, which may be detrimental to the brand outlook. Similarly, the restriction on HUL to enter or exit markets in relation to the target business [Clause 6.2(vii)], is also with a view to protect investments. Entering or exiting a territory can have a significant effect on the target business and the said restriction is a standstill obligation on HUL to prevent any adverse material adverse change.

6.10. As regard the requirement to handover documents relating to the trademarks being acquired [Clause 6.5], it is submitted that procurement of documents evidencing title to the asset being purchased, similar in the case of acquisition of shares or land or any other asset, is usual and norm for any transaction of the nature contemplated by the parties. Providing these materials do not in any manner lessen competition between the Acquirers and HUL.

7. The Acquirers have also submitted that they could not anticipate that impugned conduct would amount to a violation of the standstill obligation under Section 6(2) read with Section 6(2A) and are therefore entitled to leniency. Voluntary disclosure of the impugned conduct in the notice filed by the Acquirers and small size and scale of the combination were also suggested as mitigating circumstances.

Commission's Determination:

8. The Commission has gone into the material on record as well as heard the Acquirers. The determination of the Commission is as under:

8.1. The gist of the allegations contained in the notices issued by the Commission is that Acquirers paid/ deposited a part of the consideration for the Combination, even before the approval of the Commission. Further, the Framework Agreement envisaged certain measures to be taken by HUL that are alleged to be contrary to the standstill obligations contained in Section 6(2) read with 6(2A) of the Act.

8.2. Before getting into the merits of the contentions of Acquirers, it would be appropriate to look into the relevant provisions of the Act. It is observed that the Act envisages *ex-ante* regulation of combinations. Section 6(1) of the Act prohibits combination that causes or likely to cause appreciable adverse effect on combination and Section 6(2) of the Act obliges parties to the combination to give notice to the Commission of their proposed combination. Further, Section 6(2A) of the Act provides that a combination notified to the Commission shall not come into effect for a period of 210 days from the date of

notification. For ease of reference, relevant extract of these provisions is reproduced below:

> "***Regulation of combinations***
>
> **6** *(1) No person or enterprise shall enter into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and such a combination shall be void.*
>
> *(2) Subject to the provisions contained in sub-section (1), any person or enterprise, who or which proposes to enter into a combination, shall give notice to the Commission, in the form as may be specified, and the fee which may be determined, by regulations, disclosing the details of the proposed combination, within thirty days of ….*
>
> *(2A) No combination shall come into effect until two hundred and ten days have passed from the day on which the notice has been given to the Commission under sub-section (2) or the Commission has passed orders under section 31, whichever is earlier."*
>
> (emphasis added)

8.3. In order to enforce above provisions, including the *ex-ante* obligation of the parties thereunder, Section 43A was inserted into the Act, by way of an amendment in 2007, to empower the Commission to impose penalty in cases where parties fail to give notice in terms of Section 6(2) of the Act. The text of Section 43A reads as under:

> ***"Power to impose penalty for non-furnishing of information on combinations***
>
> ***43A***. *If any person or enterprise who fails to give notice to the Commission under sub- section (2) of*

section 6, the Commission shall impose on such person or enterprise a penalty which may extend to one percent, of the total turnover or the assets, whichever is higher, of such a combination."

8.4. The scheme and purpose of the Act is to provide an opportunity to the Commission to evaluate the likely effects of the proposed combination on relevant market(s) and regulate them appropriately. If parties to the combination forfeit this statutory opportunity provided to the Commission, the same would attract penalty under Section 43A of Act.

8.5. Coming back to the facts of the case, the Acquirers have argued that payment of advance consideration and the other impugned measures do not amount to giving effect to their combination. Further, all along, they have contended that all necessary approvals, including that of the Commission, are a condition precedent to the completion of the combination. In this is regard, it is observed that the obligation under Section 6(2) read with Section 6(2A) of the Act not only prohibits completion or closure of the transaction before the approval of the Commission but also the coordination between the parties to the combination. The intention of the parties to acquire, merge or amalgamate shall necessarily remain merely a proposal, and they shall not act upon their proposal, in part or full, until the approval of the Commission. Any coordination between them to the contrary would be a violation of the standstill obligation contained in Section 6(2) read with Section 6(2A) of the Act. For these reasons, the reliance placed by the Acquirers upon Regulation 9(5) of the Combination Regulations is also found misplaced.

8.6. The Acquirers sought to argue that the impugned conduct has not resulted in lessening of competition in any manner and therefore, penalty under Section 43A is not warranted. The Commission notes that lessening of competition or appreciable adverse effect on competition are not prerequisites for imposition of penalty under Section 43A of the Act. Such position has already been affirmed by the erstwhile Hon'ble Competition Appellate Tribunal, in its order dated 30th August, 2016, in Appeal No. 59/2015 titled *SCM Soilfert Limited and Anr. v. Competition Commission of India*. The Hon'ble Tribunal has even refused to take absence of appreciable adverse effect on competition as a mitigating factor while levying penalty under Section 43A of the Act. The relevant extract of the order is as under:

> *"10.1 We are in complete agreement with the learned counsel for the respondent* [Commission]. *Sections 31 and 43A of the Act operate in two different fields. The Commission has the power to approve a combination under Section 31 and such approval neither obliterates nor condones the contravention, for which penalty is to be imposed under Section 43A. Approval under Section 31 is not even listed as a mitigating circumstance under Regulation 48 of the General Regulations which deals with the procedure for imposition of penalty. Accordingly, in our view Penalty under section 43A of the Act is leviable even if the combination has no appreciable adverse effect on competition."*
>
> (emphasis added)

8.7. The Commission is also not in agreement with the Acquirers on the point that the standstill obligation under the Section 6(2) and Section 6(2A) of the Act is applicable only to acquisition of control. Neither the provisions of the Act nor the regulations made thereunder postulate that penalty under Section 43A could be imposed only in cases were the pre-approval coordination between the parties has

resulted in acquisition or change in control. Even the legal norms and best practises across the globe, including the jurisdictions cited by the Acquirers, though not applicable to the instant proceedings, recognises gun jumping *i.e.* pre-merger coordination and prohibits the same.

8.8. With respect to the impugned terms of the Framework Agreement, the Acquirers have submitted that they are preparatory in nature and does not amount to giving effect to the combination. Considering the submissions of the Acquirers, the Commission finds that the requirement to handover certain inventories to the Acquirers [Clause 5.1], Acquirer's introduction and interaction with the suppliers of the seller [Clause 5.4(ix)], restriction on promotional spending [Clause 6.2(vi)], and the restriction on seller to enter or exit territories [Clause 6.2(vii)], along with the pre-payment of consideration amount to a contravention of the standstill obligation contained in Section 6(2) read with Section 6(2A) of the Act.

9. Having concluded a contravention of Section 6(2) of the Act, the Commission can impose penalty that may extend to one percent, of the total turnover or the assets, whichever is higher of the combination. In this case, the combined value of turnover and assets of the parties to the combination, for the financial year 2014-15, were around INR 35,473.49/- crore and INR 16,898.3/- crore, respectively. Hence, a penalty of around INR 354/- crore could be imposed upon the Acquirer. However, considering the conduct of the parties and the circumstances of the case, wherein the contravention has been established based on the information voluntarily disclosed by the parties, who have extended full cooperation in furnishing information and the consideration of the Proposed Combination being small, the Commission has taken these as mitigating factors and considers it appropriate to impose a

nominal penalty of INR 5,00,000/- (Indian Rupees Five Lakhs only) on the Acquirer, which is only 0.14% of the maximum penalty that could be imposed.

10. The Acquirers shall pay the penalty within sixty (60) days from the date of receipt of this order.

11. The Secretary is directed to transmit a copy of this order to the Acquirers forthwith.