Competition Act of India and M & A

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1. It gives me great pleasure to address this audience of business people, chartered accountants and eminent lawyers representing some of the best minds in Bangalore. It was this very group which made valuable suggestions as regards modifications of the Regulations on Combinations (M & A) about a year ago. Since then the Regulations have been further modified for simplicity, clarity and speedy disposal of cases prompted by the experience of the Commission and frequent interactions with trade bodies such as yours. My talk today will cover the new regulations and the Commissions intent behind these modifications. I will also by way of glimpses of the M&A cases before the Commission provide an idea of the kind of M&A deals that have been cleared by the Commission and also the analysis undertaken prior to clearance. The strategic factors driving M&A in our country from a regulators perspective will provide the required input which is critical to both investors and industrialists present in the audience..

M&A Scenario

2. The Commission has so far cleared 42 cases. Interestingly all the cases except one are of Form I notwithstanding the fact that companies under the new regulations have the option of filing Form I or Form II. A break-up of the 42 cases shows that a majority of the cases are merger cases and within merger they mainly relate to intra-group mergers. There a few cases of acquisition, one case each of Restructuring (Rearrangement) and one of Form III.

3. The table below gives a tabular break up of the M&A deals cleared by the Commission.

M&A as defined under Sec 5 & 6 of the Competition Act.

No. of cases	Mergers	Acquisitions	Amalgamations Rearrangements	Form III
42	28 (7 pure mergers and 21 intra group mergers.	12	1	1

4. The table above presents a very interesting trend in the Indian corporate sector. Be it mergers, amalgamations or restructuring the deals reflect a process among companies to focus on core business by a suitable process of streamlining. The focus on business is broadly to keep core and related business together and then attempt to move forward. A related feature observed is that pure mergers are attempting to build and develop on their basic core strengths either to expand in an upcoming market (viz. India) or to face competition. A fallback to the restructuring and mergers may perhaps have been due to the prevalence of licensing policies followed by the government under the Industries Development and Regulation Act where concerns of business was more in acquiring licenses rather than in concentrating and developing core strengths. Taxation policies only contributed to the kind of haphazard and unconnected business conglomeration where the intention was more on avoiding taxes.

5. It is equally important to note that the market analysis done by the Commission in these cases cleared indicate that none of the M&A deals raised concerns of (AAEC) viz. appreciable adverse effect on competition. The Indian market is open, dynamic confirming what has been stated in the previous paragraph.

6. Nippon Steel Corporation and Sumitomo Metal Industries is an interesting case among the pure merger cases. On the other hand intra-group mergers to mention a few are: i) Reliance Infraventures Ltd, Reliance Property Developers Ltd., Reliance Infrastructures Engineer Pvt Ltd and Reliance Infrastructure Ltd; ii) Siemens ltd and Siemens Power Engineering Private Ltd. In the case of pure mergers what is noticed is the building of core strengths and expansion along familiar lines. In the case of intra-group mergers the emphasis is more on restructuring to focus on core strengths. Similar to intra-group mergers is that of the Composite Scheme of Arrangement (Restructuring) undertaken by Sundaram Clayton, Anusha Limited and Sundaram Investments Ltd. Among acquisition mention should be made of NHK Automotive Components India Pvt Ltd and NHK Spring Co. Ltd which is a restructuring vide a slump sale. Later some of these cases will be discussed.

Regulations as Now

7. It maybe appropriate at this point to mention a few of the recent amendments relating to Regulations of Combinations which are of relevance to market analysis. (Procedure in Regard to the Transaction of Business Relating to Combination Amendment Regulations, 2012) which came into force on 23/February, 2012. These amendments as stated earlier have been made by the Commission from the experience of implementation of the Combination Regulation for almost nine months. The intent to reiterate basically is to provide relief to the corporate entities from making filing for combinations which are unlikely to raise adverse competition concerns; reduce their compliance requirement; make filing simpler and to move towards certainty in the application of the Act and the Regulations. Some of the procedures in the Regulations have also been amended to make them come in tune with the substantive provisions of other Acts in force. The amendments make the Regulations market friendly.

8. Amendments to regulation 5(2) have incorporated both procedural and substantive issues. Firstly is the removal of the distinction of Part 1 and Part II of Form 1 as regards transactions outlined in Regulation 5 sub-section 2 under notice issued under sub-section 2 of Section 6 of the Act. Form – I now remains the default form providing greater clarity and uniformity. Significant for market analysis is however, the amendment to sub-regulation (3) to Regulation 5(2). By this amendment while Parties retain the option of filing Form – II, trigger points have been defined in combinations of horizontal overlap> 15% and/or significant vertical relation > 25%. In fact, by fixing thresholds AAEC gets a trigger point or red flag which is noticeable absent in the Competition Act.

9. A small point of procedure to be noted is that the nature of cases where Form II would be required is critical and in all such cases the Commission requires adequate time for assessment of the combination. The amendment seeks to compute the period of assessment from the day on which Form II is filed.

10. The Commission has received cases where assets are transferred to small companies (new or existing subsidiaries) for the purpose of effecting combination with non group enterprises. Such cases involve issues of brown field joint ventures as well as applicability of government notification dated 4th March, 2011 on target exemptions. Accordingly, the amendment involving insertion of Sub regulation (9) in Regulation 5 relates to attribution of financials to a new or an existing company to which assets have been or proposed to be transferred for the purpose of effecting a combination. The new regulation is related to direct v/s indirect acquisition and merger/ amalgamations. Where assets are transferred to a new or existing company for the purpose of effecting a combination, the financials of the transferor enterprise would also be considered for the purpose of determining a combination under section 5 of the Act. The Amendment, therefore, is in consonance with the '*effects doctrine*' as such transactions, in effect, relate to the transfer of assets/business of the transferor.

11. An interesting amendment is the inclusion of sub-regulation (1A) after sub-regulation (1) in regulation 13 which stipulates that filing be accompanied by a 2000 word summary of the proposed combination incorporating among other details pertaining to the transaction and details of related business the 'likely impact of the combination on the state of the competition in the relevant market(s) in which the parties to the combination operation…" Market analysis a critical process for Orders is facilitated and hastens the process of clearance when information is forthcoming from business who files cases with the Commission, especially where time is a major factor in M&A sanctions.

12. It was observed by the Commission that filing of form III pursuant to Section 6(4) and 6(5) are not accompanied by agreement referred in the said provisions. The extant regulations do not mandate filing of copies of the said agreements. Copies of the agreement would be relevant in determine the triggering event for filing as well as examination of the nature of the transaction to examine whether the transaction actually falls within the category of transactions mentioned in section 6(4).

13. Prior to the amendment, there was no explicit requirement of filing the investment or loan agreement with Form III. In order to determine whether the transaction reported in Form III actually falls within the nature of the transaction mentioned in Section 6(4), it was considered necessary to seek copy of such documents.

14. In terms of the Act, notice under section 6(5) has to be filed within 7 days from the triggering event mentioned therein. Regulation 7 deals with admission of belted filing of form I or form II pursuant to regulation 5. The regulations do not contain similar provisions for admission of belated form III. The Commission has come across belated filing of form III with request for condonation of delay. To address such case, the amendment empowers the Commission to admit belated filing of Form III.

15. In terms of regulation 13, the parties are required to file one from with two copies of the same. The filings received from the parties are kept in the Combination Registry which could be inspected by the members of the Commission. Sine limited copies of notice are received; inspection by members is facilitated, instead of forwarding copy of the filing, to each of the members. Therefore, keeping in mind the confidentiality of the whole process the amendment that parties provide a summary on the combination with adequate details which could be forwarded to the Chairperson and ach of the members was necessary. Hence, the new regulation 13 (1A) was introduced.

16. Keeping in mind that generally there would not be acquisition of control or change in control unless at least a person acquires/holds more than 25% of the voting capital of the target company, the existing limit of 15% in category – I of Schedule – I was amended to be increased to 25% in line with business practices.

17. Substitution in category 6 of Schedule – I was the result of the desire to include acquisitions through buybacks, as strictly speaking there is no positive intent to acquire in such transactions. Further, it was also felt to broaden acquisitions to rights issue to incorporate all acquisitions pursuant to the rights issue and not restricting it to only acquisition to the extent of entitled proportion.

18. Category 8, Schedule – I read with regulation 4 dispenses filing requirement in respect of intra group acquisition as the same is not likely to have AAEC. Similar provisions for intra group merger or amalgamation is not contained in the regulation. Therefore, by an amendment, a new category similar to Category 8 regarding intra group merger or amalgamation involving holding companies and /or its wholly owned subsidiaries was introduced in the form of category 8A to Schedule – I.

19. Currently, the Regulations require the managing director, or in his absence, a director authorized by the board of directors, of Companies to sign and verify forms filed under the regulations. The requirement was considered rigid and infeasible in some genuine occasions. Therefore, it is considered desirable to enable company secretaries, in addition to the above persons, to sign and verify the forms filled pursuant to the regulations. Hence, the insertion of sub regulations (1) and (3) to regulation 9.

20. The present fee structure was considered not proportional to the resources diploid in the assessment of the notices filed. Therefore, the amendment to substitute regulation 11 came into force. In terms of the said provision the fee for filling Form – I and Form – II are INR 50,000 and INR 10,00,000 respectively. Accordingly, the fee has been increased from INR 50,000 to INR 10,00,000 in respect of Form – I and from INR 10,00,000 to INR 40,00,000 in respect of Form – II.

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Analysis by the Commission

23. In outlining the approaches adopted in the analysis of the Commission and in assessing the possible competitive constraints of a combination well established mechanisms have been put into practice. Data and evidence gathering, use of quantitative techniques and the scope for innovative approaches that combination analysis world over have been used are well illustrated in the EU 'Commission Notice' and the US 'Horizontal Merger Guidelines'. What is attempted is to provide glimpses of enquiry with reference to some of the Orders of the Commission. It must however, be remembered that since all combination cases cleared so far are Form 1 cases i.e. those which the parties involved do not consider as raising concerns of market domination and competitive constraints. No doubt given the criticality of market dimension for competition assessment the criteria adopted and the tools used by the Commission gains significance.

24. Regulation 5(3) the Commission sets the trigger points in examining mergers or acquisitions where market share is >15% in the case of horizontal combinations and >25% in the case of vertical combinations. Nonetheless market analysis covering product definition is carried out for all filings a priori to closure or for shifting to Form 2. The Act defines relevant market in Sec. 2 (r); relevant product Sec. 2(t); and relevant geographic market sec 2(s). Where combination cases are concerned market definition identifies the boundaries of competition and unlike 'Abuse of Dominance' cases (Section (4)) substitutability of products is examined both from demand and supply side. Scope for potential competition must also be part of market definition in so far as it impacts on competitive constraint. Section 20(4) lists out the factors that 'would have the effect or likely to have an appreciable adverse affect on competition in the relevant market'. The concept of market as is well known is much wider than the definition in other anti-

trust cases which also provides for innovative and flexible methods of determining market boundaries.

25. In defining the relevant product, attention is on the functional dimension or purpose of the product. Customer choice as reflected in responses to pricing is the starting point and for economists demand substitution is a critical factor. The commonly used tool is the SNNIP test. There are however alternative measure using econometric analysis to arrive at delineating the market. Before the application of SNNIP test, market survey of the range of products which could be considered as substitutes, is undertaken.

NHK Automotives and Burmah Trading Corporation:

26. An interesting case before the Commission was of that of automotive springs (case No C-2011/08/03) NHK Automotive with the springs division of Bombay Burmah Trading Corporation (BBTCL).NHK itself is a wholly owned subsidiary of NHK Japan and NHK Japan has presence in India through its subsidiary NHK Springs. The first aspect therefore examined was the nature and purpose of combination. The Acquirers stated that NHI Japan wishes to expand its presence in India.

27. The relevant product market in this case was that of manufacture and supply of customized springs for industrial application in the automotive sector. The range of products in this market definition is wide. Products can be classified on the basis of shape (coil springs, flat springs, machined springs). They can be classified on the basis of industrial application (automotive industry, railway carriage, rolling stock, desktops, laptops hard disk etc). They can also be distinguished on the basis of process, cold formed or hot formed. In each product segment howsoever classified the above parties have a presence.

28. The wide range of products distinguished on well defined criteria in the above case brings to focus the scope of supply substitution by other suppliers in terms of switching from one product to another. It was interesting to observe how technology as seen in product differentiation (or even in the process used) and in terms of price differentials can create opacity in market contours. Switching product lines of possible competitors depends on costs of switching.

29. By a process of elimination the relevant market was defined. The complexity of this case lay in analyzing the product overlap of the parties involved where it looked the entire sequence was associated with one or the other company of the acquirer and of the entity acquired. Assurance that there was no product overlap or geographic overlap and whether the parties to the combination could lead to strong vertical linkages information on which was sought after the filing.

30. The SNNIP test was not used in this case. Discussions were held with customers. Market studies on springs were used and there was no data constraint at the macro level as the sector is well represented by associations. SNNIP however was not required as the relevant market was the OEM segment for 2-wheeler'. Functional inter changeability or product substitutability is not an issue in customized markets customized as these markets by the main customers and in this case most of them are well known international brands. There are two parts to the relevant market - original equipment market (OEM) for components and spare parts. It was observed that every major automobile manufacturer in India invites several lines of suppliers for OEM components thereby ensuring competitive play of market forces. Further technical collaborations among the selected vendors ensured that the vendors were not dominant The OEM segment is almost 80% of market share.

31. The Commission on detailed analysis based on the facts on record and other details gleaned from several sources including the acquirers themselves opined that the proposed transaction is not likely to give rise to any adverse competition concern.

Alok Industries and Grabal Alok Impex:

32. The scope for market domination through vertical linkages was analyzed in a recent case (Case No. C-2012/01/28) involving Alok Industries and Grabal Alok Impex both belonging to the same group and under the same management, having operation in textile industries with the difference that AIL manufactures apparel fabrics, home textiles, garments and polyester yarn. GAIL produces embroidered products. The concern of the Commission was whether the combination would enable a dominant company to emerge. Investigations and analysis revealed that although the parties are in the same broad market the individual products do not overlap and are not identical or substitutable products. Moreover both parties are involved in independent activities including sourcing of raw materials have minimal vertical relationships.

SML Isuzu, Isuzu Japan and Sumitomo:

33. Equally interesting was the proposed combination of SML Isuzu, Isuzu Japan and Sumitomo. SML Isuzu was engaged in the business of manufacturing and sale of four wheeled commercial vehicles, earlier known as Swaraj Mazda Limited. Sumitomo, holding 54.96% equity shares in SML Isuzu, supplied power trains and chassis components to SML Isuzu. After the proposed combination (acquisition), Sumitomo and Isuzu (Japan) would hold 43.96% and 15% equity shares respectively in SML Isuzu. According to the Notification No S.O. 481 dated 4th March 2011 issued by the Government of India, group exercising less than 50% of the voting rights in other enterprises are exempt from the provisions of section 5 of the Competition Act. The Commission took note of the said notification and decided accordingly. As there was no horizontal overlap as assessed by the Commission, it opined that the present acquisition is not likely to have an appreciable adverse effect on the competition in India and therefore, was approved by the Commission.

Nippon Steel Corporation and Sumitomo Metal:

34. The next interesting case of merger analysed by the Commission was of Nippon Steel Corporation and Sumitomo Metal, the former engaged in the sale of steel products and the latter in the business of manufacturing and sale of variety of iron and steel products, NSC being present in India through its group companies which included Nippon Steel India Pvt Limited. By virtue of the proposed merger, the parties would have entered into an integration agreement in order to integrate all of their business including the core business of steel making and steel fabrication. In India, the operations of the parties to the combination mainly related to the sale of various types of steel products. The Commission analysed that the parties were engaged in manufacturing of various steel products ranging from crude steel to finished steel. Steel product may be distinguished on the basis such as composition, application, and physical characteristics. On the basis of the above, two broad categories of steel are flat steel and long steel the parties were found to have eight similar/ identical/substitutable products which included steel bars, wire rods, heavy medium plates. HR steel Sheets and Cols, CR Steel sheets and cols, surface treated steel sheets, NO's and seamless pipes. The Commission was of the opinion that it may not be necessary to define the relevant market for the purpose of assessment of the proposed merger, notwithstanding that the parties stated that they were engaged in the sale of eight similar/ identical/substitutable steel products in India, as the competitive assessment did not change substantially, even if the relevant market in respect of the steel products which the parties sold, was not conclusively delineated.

GS mace Holding acquisition of shares of Max India:

35. Another case that requires a mention here is the acquisition filed by GS Mace Holdings Limited, a Mauritius based sub account of the Goldman Sachs & Co which is a Foreign Institutional Investor, for acquisition of the shares of Max India Limited. The details of the said acquisition was filed inform III and till date is the

only case filed so. As a result of the acquisition of shares in Max, the acquirer's shares had increased to 15.602% of the issued and the paid up equity share capital of Max. The Commission observed that the provisions of sub section (4) of section 6 of the Act apply to share subscription or financing facility or any acquisition by a public financial institution, foreign institutional investor, bank or venture capital fund, only if it is made pursuant to any covenant of a loan agreement or investment agreement. In pursuant to the amended Combination Regulations, acquirer holding 25% of the voting rights or shares, is not likely to cause an AAEC in India, and now in respect of such acquisitions, notice under section 6 (2) need not normally be filed. Therefore, in view of the amended regulations the Commission was of the view that the proposed merger was not likely to have any AAEC on competition in India.

Conclusions

From the case analysis a few points worth considering are given below.

a. Market definition is critical in all combination cases. Market definition combines both behavioural and structural dimensions in the range of products under consideration. A third source of competitive constraint that is examined is of 'potential competition'.
b. From the examples given a question that is often posed is: What type of evidence does the Commission use? All authentic evidence and to that extent the Commission is open in its approach and does appreciate when filings come with sufficient information. Of course the evidence is circumscribed by the specific product or market being examined. It may be worthwhile mentioning that development of data base on past experience namely, archival data of experience that can be critical in some cases, for a young Commission such as ours, suggests recourse to the vast untapped data base the Indian Government and Trade Bodies

c. Markets so defined are then evaluated with respect to market size and share of the parties in the products of the case and in their respective products. The practice has been to source market share from company estimates, available studies or commissioned studies. Information given by parties is used only after verification including from the stock exchanges. Market studies do provide concentration ratios and where data permits use of data bases such as CMIE of calculating HHI index is also undertaken.

As may be seen from my talk M&A are vibrant in India and their strategy is more towards facing competition by concentrating on developing core strengths. The Commission looks forward not only to more M&A's as a process of facilitating growth. Suggestions to the outlined procedures are always welcome.

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