Deconstructing
The Merger Review Regime

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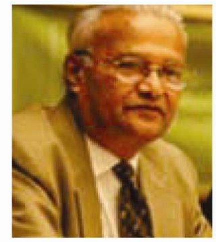

On June 1, 2011, the Merger Regulations of the Competition Commission of India (CCI) (formally called Combination Regulations - Procedure in regard to the transaction of business relating to combinations) came into force. With this, a new phase in the competition regime starts as the merger review process becomes fully operational. The launch of the new regulations, which have been discussed extensively with all stakeholders, provides the procedures to implement the recently notified provisions of the Competition Act 2002 relating to mergers or combinations, principally Sections 5 and 6. In this article, we explain some of the ideas motivating the introduction of this new regime and briefly discuss their likely impact on the Indian economy. The basic criterion used for evaluation of combinations is to see whether they have the potential to cause an appreciable adverse effect on competition (AAEC) within the relevant market in India. Hence, a broad competition test is used to evaluate mergers.

India's Merger Control Regime

Broadly speaking, the merger control regime in India envisages two categories of mergers, among those which are considered worthy of scrutiny at all (after satisfying the financial thresholds and the exemptions). The first category consists of mergers which can hopefully be disposed of within 30 days by the Commission because they raise no competition issue. It is expected on the pattern in other jurisdictions that the bulk of mergers will fall in this category. The second category of mergers are those which perhaps do cause an AAEC within the relevant market in India and therefore, require a more detailed scrutiny and a longer period of time (180 days) to determine whether this is indeed the case. The Act requires that the Commission give its prima facie opinion within 30 days, its first opinion, generally based on the initial filing. The informational requirements for the first category is very much less detailed (Form 1); here the basic idea is that if firms have no overlapping markets in India and therefore, no horizontal issues, the merger can be cleared without further scrutiny.

The second category, (analogous to the practice followed under the US antitrust regime such as DOJ second request), where there are overlapping markets in India, which means that there are competition issues, require a detailed investigation in order to determine whether in fact the merger is on balance anticompetitive, a detailed balancing of its costs (in terms of increased market power) and benefits (in terms of potential merger synergies). The information required for this purpose (stated in Form 2) relates to the definition of the relevant market, the demand the industry faces, the nature of competition in the industry and barriers to entry into the industry. Such information is the longest part of the regulations and is needed to make a thorough determination of the competitive impact of the merger. Schedule 1 consists of a list of combinations which are exempt from filing because they are unlikely to cause an AAEC. However, they can well be challenged under other relevant provisions of the Competition Act.

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Determination of AAEC

Once it has been determined that an AAEC is likely to take place, the CCI conveys this to the parties within 4 days, who are then required to publish the details of the combination in a suitable format (Form 4 of Schedule 2), within 10 days and submit this to the CCI whence this info is displayed on the CCI website, at the websites of the parties and in all India editions of four leading daily newspapers, including at least 2 business papers. This format basically invites comments on the combination from any person or persons likely to be adversely affected by the combination within 15 days of the announcement. As per Regulation 29(3), the CCI may, in practice, invite public comments so that the problem of consultation may not arise at all.

In the event that the Commission concludes that there is a prima facie AAEC, it issues notice to the parties to respond within 30 days as to why an investigation should not be conducted. After receipt of the response to the notice to show cause from the parties, the Commission may direct the DG to write a report. He/she is required to explain the

basis for his conclusions, (Secs 20-21). A modification may be proposed by the CCI. If the parties accept the modification, then these may take place, else the AAEC stays in place. The financial thresholds are not mentioned in the regulations, but in Section 5 of the Competition Act and two subsequent notifications on the CCI website. The financial thresholds taking these into account work out to the following:

• If two firms merge and the combination has combined assets of atleast Rs 1500 cr or turnover of Rs 4500 cr, they must file notice.

• If the group to which the combined firm belongs has assets of more than Rs 6000 cr or turnover of Rs 18,000 cr, they must file notice.

• When the target company has assets of less than Rs 250 cr or turnover of less than Rs 750 cr, the acquisition has a blanket exemption from filing for 5 years.

Impact of New Regulations on The Economy

Now that the new merger provisions and regulations are in place, their impact on the economy is required to be gauged. There are two important routes by which the merger regulations have no impact. Firstly, when a merger is not thought to affect the relevant market in India and secondly, when it does not meet the minimal financial thresholds to be inspected. The logic of both these is impeccable; the first needs no explanation, the second is there because it is thought that small mergers are unlikely to have large impacts and that the cost of evaluating a merger may be greater than the expected benefit from doing so. It becomes important to isolate those mergers which, due to either of these reasons, do not get evaluated at all.

It is expected that the period April 2011- March 2012 will see a sizable number of mergers, just like in the previous year, April 2010 - March 2011. Moreover, the number of mergers in the period Jan 2011- March 2011 itself has been high with a total volume of transactions of $18.31 billion. One may categorize mergers into four categories for the purpose of the analysis below: outbound mergers, inbound mergers, domestic mergers and foreign country mergers, which take place outside the country and may have a local nexus.

Outbound Mergers

In the recent past, there have been several outbound mergers with cash rich domestic firms on the hunt for companies globally for natural resources like coal mines, oil, gas, coking coal, iron ore from Africa to Australia, for production facilities, to enter new markets or several of these simultaneously. Thus, for instance, Tata Chemicals' purchase of British Salt, Mahindra's purchase of Ssang Vong (South Korean Auto major), Aditya Birla Group's purchase of US based Columbian Chemicals, Tata Chemicals' purchase of US based potash miner EPM Mining Ventures, Vedanta's purchase of 10% of Cairn, Airtel's purchase of the African telecom assets of Kuwaiti group Zain, Fortis Health Care's purchase of Hong Kong's Quality Health Care Asia and Hindalco's purchase of Novelis, a major North American aluminium manufacturer, all fall into one or more of these categories. As long as these mergers involve purchases of companies that are not operating in India in the same market as that of the buying firm, they do not affect the relevant market in India and therefore, most of such mergers will not even have to be notified to the Indian competition authority, the CCI. Of the above, if Ssang Vong was, prior to purchase, selling automobiles in India within the same relevant market as Mahindra, the merger may have to be filed. Thus, the merger legislation is unlikely to have much impact on such mergers.

Foreign Country Mergers

A foreign country merger, where one company buys another outside the country and both companies have operations in India, is required to file with the CCI provided that they affect a relevant market in India and satisfy the financial thresholds. Thus, for instance, the recent purchase by Unilever of Alberto Culver, both of which operate in India, certainly meets the financial thresholds requirement and probably affects the relevant market in India as well.

The present merger regulations do not work with retrospective effect; only mergers which take place after June 1, 2011 will come under the purview of the merger regime. This simply depends on where such mergers are taking place and likely to take place worldwide in the near future, whether they have a local nexus and if they meet the filing requirements. However, unless such mergers are filed with the CCI, there is requirement of seeking the same, as it has to first build its experience in the area with purely domestic mergers. Thus, while such mergers are to be filed with the CCI on their own, it is expected that the authority will initially take a somewhat lenient view towards such mergers.

Inbound Mergers

Similar in terms of analysis to the above are inbound mergers where foreign companies intend buying companies operating in India. In this case, if the foreign company is already present in the Indian market, either through a subsidiary or a local distributor, which is how foreign companies normally enter new markets, then they may have an effect on the relevant market in India, and if they meet the filing requirement, may need to be scrutinized. Such may be the case in auto parts companies, pharmaceutical companies (Abbott's purchase of Piramal Healthcare's branded generics business), personal care products (FMCG) like the recently announced purchase of Paras Pharma by Reckitt Benckiser, where the regulations will probably come into play. In 2008, Japan's Daiichi Sankyo acquired a majority stake in Ranbaxy Laboratories, while Abbott Laboratories acquired Piramal Healthcare's domestic formulations business last year.

There is a growing apprehension that the rising takeovers of Indian companies by foreign MNCs may lead to a shift in the intellectual property rights regime and cause the flexibilities under TRIPS to become redundant. It could affect the affordability of cheap, generic medicines as a rise in prices resulting from such takeovers is apprehended along with marginalization of homegrown companies. Thus, merger regulations would be useful in conducting the ex-ante analysis necessary to determine the likely impact of mergers in the pharma sector.

Subsequent impact will depend on the vigour of the competition authority and the strength of their analysis which will take time to evolve as ours is a young jurisdiction with absolutely no prior experience of dealing with mergers, either within the authority (CCI) or in other regulatory bodies.

Domestic Mergers

Finally, there are the purely domestic mergers which are taking place in sectors such as telecom where mergers are taking place mostly among owners of telecom towers for cellular services. Thus, GTL Infrastructure bought Aircel Towers for rolling out its 3G services. Here mergers will probably affect the relevant market and perhaps meet the financial threshold requirements as well. Similarly in the banking sector, one has the purchase of Bank of Rajasthan by ICICI. There has been considerable consolidation in the steel sector in the recent past as well as in insurance. In the absence of clear demarcations with regard to jurisdictional issues, both telecoms and banking mergers may have to be reviewed by the Competition Authority and will thus be affected by the new merger regime. The insurance sector will also be affected as per the mandate of IRDA. Since the CCI is a relatively new body, it needs to first start with these purely domestic mergers to obtain the expertise in dealing with this new area of the competition legislation.

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In conclusion, we expect that the primary impact of the new merger regime is unlikely to be on any mergers, other than domestic mergers particularly in telecom, banking and insurance. Of the others, some of the inbound mergers which are filed with the CCI may perhaps be scrutinized, but at the present stage of learning, lenient treatment of such mergers is expected, till such time there is enlargement in the capacity of the competition authority.

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