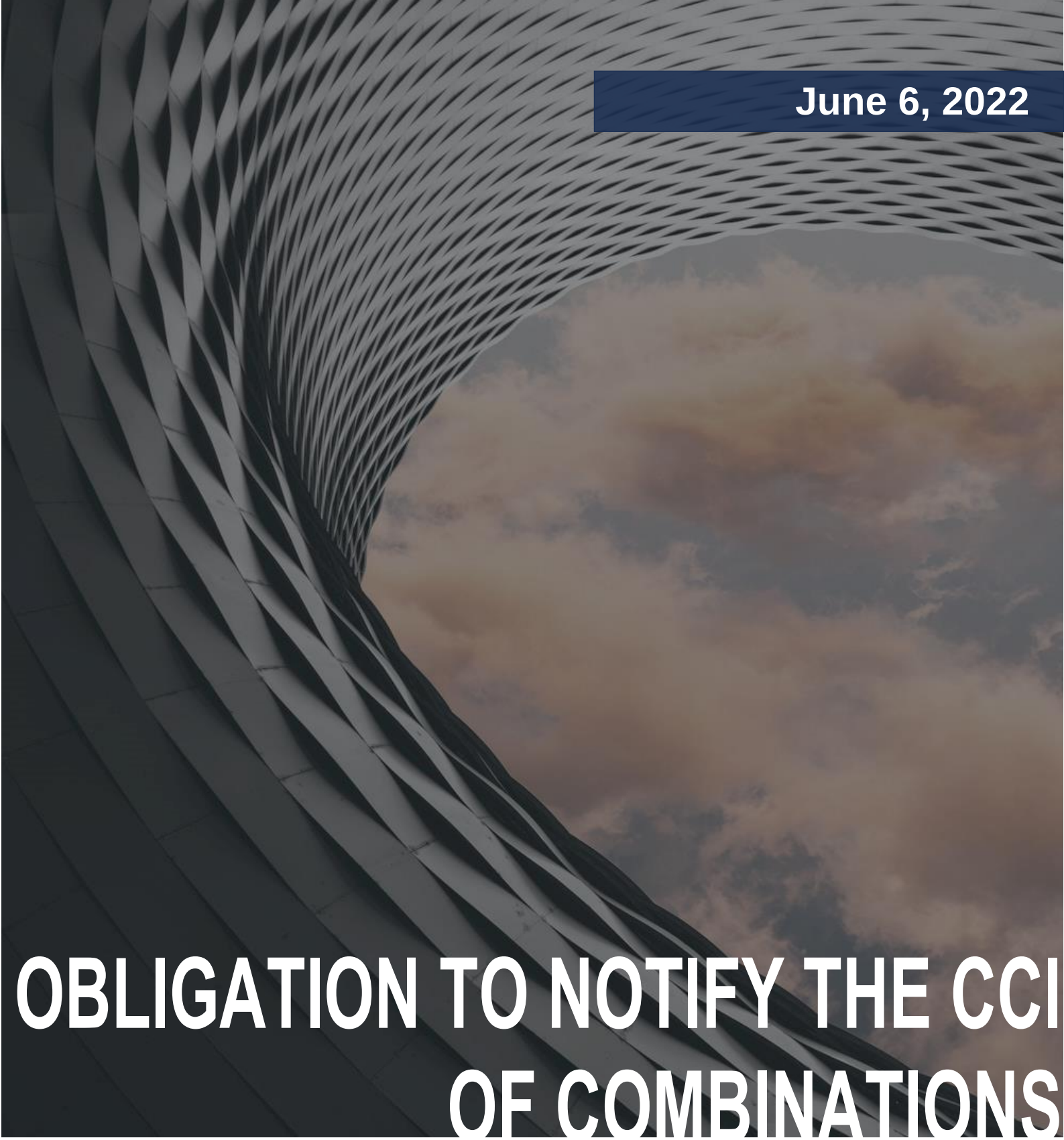

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OBLIGATION TO NOTIFY THE CCI OF COMBINATIONS

AN ANALYSIS FROM THE PERSPECTIVE OF AIFs

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Obligation to Notify Combinations

Section 6(2) of the Competition Act, 2002 ("**Competition Act**") provides that any person or enterprise which proposes to enter into a combination shall give a notice to the Competition Commission of India ("**Commission**") upon execution of any agreement or other document in relation to such combination (of the nature of an acquisition). No combination shall come into force until the commission has approved the notified combination, or a period of 210 (two hundred and ten) days has passed since the said notification. A combination includes an acquisition of assets, shares, voting rights or control, wherein the value of the assets and the turnover of the acquirer and the enterprise whose assets, shares, voting rights or *control* have been acquired/are being acquired exceed the following thresholds laid down in the Section 5 of the Competition Act:

THRESHOLDS FOR FILING NOTICE				
		Assets		**Turnover**
Enterprise Level	**India**	> INR 2000 crore	**OR**	> INR 6000 crore
	Worldwide with India leg	> USD 1 bn with at least > INR 3000 crore in India		> USD 3 bn with at least > INR 3000 crore in India
OR				
Group Level	**India**	> INR 8000 crore	**OR**	> INR 24000 crore
	Worldwide with India leg	> USD 4 bn with at least > INR 1000 crore in India		> USD 12 bn with at least > INR 3000 crore in India

The requirement to notify combinations falling within the aforesaid thresholds is subject to the following exceptions:

- Regulation 4 of the Competition Commission of India (Procedure in regard to the transaction of business relating to combination) Regulations, 2011 ("**Combination Regulations**") provides that the categories of combinations[1] mentioned in Schedule I of the Combination Regulations are ordinarily not likely to cause an appreciable adverse effect on competition ("**AAEC**") in India and so notice under Section 6(2) of the Competition Act need not normally be filed..

- Notice is not required if the value of the assets acquired, taken control of, merged or amalgamated is not more than INR 3,50,00,00,000 (Indian Rupees Three Hundred and Fifty Crores) in India or their turnover is not more than INR 10,00,00,00,000 (Indian Rupees One Thousand Crores) in India ("***de minimis* exemption**"). This de minimis exemption was initially given for a period of 5 (five) years vide a notification issued by the Ministry of

[1] One of the categories of combinations mentioned in Schedule I of the Combination Regulations is the acquisition of less than 25% (twenty five percent) shareholding/voting rights, not leading to acquisition of control of the enterprise whose shares or voting rights are being acquired. The provisio to this exception requires that the acquirer should only acquire the rights of any other ordinary shareholder of the company being acquired and should not have the power to nominate any director to the acquired company's board. The explanation to this exemption states that the acquisition of less than 10% (ten per cent) of the total shares or voting rights of an enterprise shall be treated as solely as an investment. Therefore, the caveat in Regulation 4 of the Combination Regulations that combination be one which ordinarily is not likely to cause AAEC in India, would not apply to the acquisition of less than 10% (ten per cent) of shares/voting rights, provided it does not involve the acquisition of any form of control.

Corporate Affairs' *("***MCA**") dated March 27, 2017[2]. The de minimis exemption has now been extended for a further period of 5 (five) years, until March 27, 2027 *vide* MCA's notification dated March 16, 2022.

- As per Section 6(4) of the Competition Act, the provisions of the Section 6 are not applicable to share subscription or financing facility or any acquisition by a public financial institution, foreign institutional investor, bank or venture capital fund, pursuant to any covenant of a loan agreement or investment agreement. For the purpose of this exemption, the definition of a 'venture capital fund' is as per Clause (b) of the Explanation to clause (23 FB) of Section 10 of the Income Tax Act, 1961. This definition requires the Venture Capital Fund to be operating under a trust deed (i) which has been granted a certificate of registration before May 21, 2012 as a venture capital fund and is regulated under the Securities and Exchange Board of India (Venture Capital Funds) Regulation, 1996[3] or (ii) has been granted a certificate of registration as venture capital fund as a sub-category of Category I AIF under the AIF Regulations and which fulfils certain additional conditions[4]. Consequently, Category II and III AIFs are excluded as are Category I AIFs such as angel funds, infrastructure funds, SME Funds and social venture funds. As per Section 6(5) of the Competition Act read with the Combination Regulations, acquisition by entities mentioned in Section 6(4) of the Competition Act are to be reported, by way of Form III, within 7 (seven) days from the date of transaction.

Definition and Scope of 'Control'

As mentioned above, a combination includes an acquisition of assets, shares, voting rights or control. Of the aforesaid four parameters, three parameters, namely assets, shares and voting rights are tangible, while "control" is not, which is problematic. The term 'control' is defined by the Competition Act to include controlling the affairs or management by one or more enterprises (or groups), either jointly or singly over another enterprise or group. Therefore, if a fund invests in a company and receives, in addition to equity or preference shares with voting rights, rights such as veto rights or the right to nominate directors to the board of directors of such company, the fund may be construed to have control over such company, depending on the nature and extent of the influence which the fund would wield over such company on account of its contractual rights.

The abovementioned list of rights is only based on CCI precedents. There is a lack of clarity on which affirmative rights, or other contractual rights would fall under investor protection rights, and which ones would constitute control, thereby triggering the notification requirement under Section 6(2) of the Competition Act.
As mentioned above, the exception provided by the Schedule I of the Combination Regulations (wherein less than 25% (twenty five percent) shareholding/voting right is acquired) do not apply to

[2] The notification may be found at https://www.cci.gov.in/sites/default/files/notification/S.O.%20988%20%28E%29%20and%20S.O.%20989%28E%29.pdf.

[3] Though the AIF Regulations repealed the Securities and Exchange Board of India (Venture Capital Funds) Regulation, 1996, Regulation 39(2)(b) of the AIF Regulations provide that all venture capital funds or schemes launched by such venture capital funds prior to date of notification of the AIF Regulations shall continue to be governed by provisions of Securities and Exchange Board of India (Venture Capital Funds) Regulations, 1996 till the fund or scheme is wound up.

[4] These conditions are that the Venture Capital Fund (i) has invested not less than two-thirds of its investible funds in unlisted equity shares or equity linked instruments of venture capital undertaking; (ii) has not invested in any venture capital undertaking in which its trustee or the settler holds, either individually or collectively, equity shares in excess of fifteen per cent. of the paid-up equity share capital of such venture capital undertaking; and (iii) issued not issued units which are listed in any recognised stock exchange.

the acquisition of control.[5] Therefore, even if a fund acquires a minority stake in a company, which is less than 25% of such company's total share capital, the fund may be construed to 'control' that company if it crosses the 'control' threshold.

Consequences of Acquiring 'Control'

If the acquisition of control of an enterprise meets thresholds prescribed under the Competition Act, it would amount to a combination under the Competition Act and the acquirer should notify the CCI, irrespective of the actual shareholding acquired. Further, such combination would be subject to certain tests to ensure that it doesn't hamper market competition in India.[6] The process for notifying the CCI is provided in the Annexure to this note.

Recent Case Law

Recently, the Competition Commission of India ("**CCI**"), in an order against an investment management company ("Investment Manager"), imposed a penalty of INR 20,00,000 (Indian Rupees Twenty Lakhs Only) on account of the Investment Manager's failure to notify an acquisition.[7]

Facts

The impugned transaction entailed the acquisition of real estate and private equity fund management businesses of one investment manager by the Investment Manager on a slump sale basis for a lump sum consideration. It appears that through this acquisition, the Investment Manager became the investment manager of a number of venture capital funds ("**VCFs**") and alternative investment funds ("**AIFs**") registered with SEBI. It may be presumed that the aforesaid VCFs and AIFs had invested in a number of Indian companies, holding a minority stake in each Indian company, coupled with certain contractual rights.

The transaction was consummated, and the Investment Manager did not notify the CCI under Section 6(2) of the Competition Act. The CCI inquired into the transaction and assessed whether proceedings under Section 20(1) and/or Section 43A were required. Post its enquiry, the CCI was of the *prima facie* view that the Investment Manager should have notified the CCI of the aforesaid transaction under Section 6(2) of the Competition Act.

Issues and decision

A. Does the investment manager of a VCF or AIF control the portfolio companies of such VCF or AIF?

The Investment Manager argued that the acquired funds' assets are under the legal and beneficial ownership of the trustee and the beneficial interest over the said assets lie with the unitholders of the funds. Since the assets of the funds are separate from the assets of the fund manager, the Investment Manager does not enjoy ownership over the assets or any controlling rights over the assets of any of the funds. Additionally, it would be inappropriate to consider that the funds' assets, namely, the acquired portfolio entities of the fund are owned by the Investment Manager by virtue of its ownership of the fund management businesses. In this regard, the CCI noted that by virtue of the acquisition of the fund management business, the Investment Manager became the

5 See Clause 1-3, Schedule I, Competition Commission of India (Procedure in regard to the transaction of business related to combination) Regulations, 2011.

6 *See* Section 20, Competition Act, 2002.

7 Proceedings against Investcorp India Asset Managers Private Limited under Section 43A of the Competition Act, 2002.

manager of the concerned funds. Since the fund-based investment structures give authority to the fund manager to conduct the operation of the fund, though the beneficial ownership over the assets of the fund lies with the unitholders, the control over the operations and management of the fund is entrusted to the Investment Manager.

Further, the CCI added that funds have a varying degree of interest over the portfolio entities and the same depends upon the shareholding and contractual rights of the fund with respect to each portfolio entity. The Investment Manager of the fund, being the authority to exercise the operations of the fund, invariably enjoys control over the portfolio entities, provided the shareholding and/or contractual rights of the fund is such as to enable material influence or higher degree of control over the given portfolio entity. In the given case, acquisition of a fund management business was held to have led to acquisition of control over the underlying portfolio entities of the fund.

B. If an entity acquires a minority stake in a company, coupled with some veto rights and other management rights, can it be said that the acquirer has 100% control of such company and consequently the entire turnover/assets of such company should be taken into account for the purpose of ascertaining if the acquisition has crossed the threshold prescribed under Section 6 of the Competition Act?

The Investment Manager argued that the impugned transaction is eligible for the *de minimis* exemption provided by the CCI notification dated March 27, 2017. In response to this contention, the CCI held that in case of acquisition of an asset management business, the value of assets and turnover of controlled portfolio entities would also be relevant for the purpose of computation of threshold under Section 5 of the Act.

Furthermore, the Investment Manager argued that even if assets and turnover of the portfolio companies are to be taken into consideration, they should only be considered in proportion to the extent of shareholding of the underlying funds of the acquired entity. In relation to the same, the CCI held that when an enterprise acquired material influence over another entity, the whole of the financials of the target entity are to be taken into consideration for the purpose of Section 5 of the Act. Therefore, if control is established, the complete financials of the fund/target would be attributed to the fund manager for the purpose of Section 5 of the Act.

Conclusion

The abovementioned case laws show that while it is arguable that funds make investments in their ordinary course of business and any additional rights acquired by them should be construed as minority protection rights, the CCI may treat the acquisition of a minority stake in a company, coupled with control, to be 100% control over such company. Consequently, the entire turnover/assets of such company is taken into account for the purpose of ascertaining if the acquisition has crossed the threshold prescribed under Section 6 of the Competition Act. This has resulted in a situation wherein the CCI expects every transaction by an AIF (other than venture capital funds) resulting in the acquisition of control to be notified (even if such transaction is very unlikely to result in AAEC), following which the CCI formally assesses whether the nature of rights conferring control results in AAEC or not.

This view has far-reaching consequences for the Funds industry. Every fund, apart from a venture capital fund as discussed above, making an acquisition would have to consider if the rights acquired by them amount to control. Funds may wish to play it safe and notify the CCI of an acquisition, but notifying the CCI of an acquisition on the basis that it involves acquisition of control is tantamount to taking a position that the Fund has acquired control over the target company. In many instances, an investee company would have multiple investors, each with a minority stake and some management rights and every investor in such investee company may be construed to be in ‘control’ of such investee company, thereby triggering the notification requirement on each

investor. As indicated in the Annexure below, the fee payable for each notification is substantial and would add to the cost of making investments for funds.

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ANNEXURE
Notification Process

Filing the notice

1. The notice to be filed for a proposed combination should be in Form I as specified in Schedule II to the Combination Regulations, and should be accompanied by the requisite fee payable by the parties to the combination;
2. In case the parties to a combination have any horizontal or vertical overlap in their provision of goods and services and hold a cumulative market share of more than 15% (fifteen percent) horizontally and 25% (twenty-five percent) vertically, the notice may be given in Form II (instead of Form I). On March 31, 2022 the CCI introduced a new Form II which collects substantially less information regarding the combination, as compared to the earlier version of Form II. Venture capital funds[8] may file details of the proposed combination in Form III. Forms I, II and III are provided in Schedule II of the Combination Regulations;
3. **Fee**: the fee payable for filing Form I is INR 20,00,000 (Indian Rupees Twenty Lakh Only); where the notice is in Form II, the fee payable is INR 65,00,000 (Indian Rupees Sixty Lakh Only). No fee is required to be paid where the notice is in Form III**;**
4. The duly filled notice along with one copy and electronic version thereof shall be delivered to the CCI at the address published on its official website. Confidentiality requests, if any, may be filed in accordance with the Competition Commission of India (General) Regulations, 2009 with a duly filled in public version of the notice and an electronic version thereof;
5. A summary of the combination, without containing any confidential information, in not more than 1000 (one thousand) words should be filed with the notice, containing (i) name of the parties to the combinations, (ii) the nature and purpose of the combination, (iii) the products, services and business(es) of the parties to the combination; and (d) the respective markets in which the parties to the combination operate. The summary is for publication on the CCI website;
6. There is also a provision for e-filing with the CCI, the details of which may be found on the filing section of the CCI website.

Pre-filing consultation

The Competition Commission of India also allows for informal and verbal consultation with its staff/case team prior to filing of a combination notice. Therefore, it is advisable to consult the staff of the commission as soon as possible regarding a proposed transaction, if there is any ambiguity regarding the need for the filing of a combination notice.

A party seeking consultation can file a request for the same along with details regarding the proposed transaction including – (a) scope and structure of the transaction proposed, (b) relevant market sector of the parties to the transaction, (c) key issues for consideration in the consultation and (d) any other details relevant for the purpose of the consultation.

The email seeking consultation may be sent to the details provided in the pre-filing guidance note.

Green Channel Notification

If the parties, on a self-assessment observe that there are no overlaps in products and services offered – horizontal, vertical or complimentary, and that the combination does not result in any AAEC, though it crosses the prescribed threshold, then the parties may fill and submit Form I (the

[8] as defined in the Explanation (b) to Section 6 of the Competition Act.

amended version with a Green Channel section) along with a declaration that the resultant combination is not likely to cause any AAECs. The filing fees as prescribed above shall be filed and the CCI shall issue a deemed approval upon assessment of the combination's green channel assessment.