Changes in Secretarial Audit, Compliance Management and Due Diligence Module relevant for June 2017 examination

Dear Student,

Please incorporate the following updates in your study material which is updated till June 2016. The soft copy of the study (Updated till June, 2016) is available on the ICSI Website.

1. Page 34: for the words:

(3) A copy of order of the competent authority approving the alteration, shall be filed with the Registrar in Form No. INC.27 with fee together with the printed copy of the altered articles within fifteen days of the receipt of the order from the Central Government.

The following shall be substituted namely:-

(3) Subject to the provision of sub-rule (1), for effecting the conversion of a public company into a private company, a copy of order of the Tribunal approving the alteration, shall be filled with the Registrar in Form No. INC -27 with fee together with the printed copy of altered articles within fifteen days from the date of receipt of the order from the Tribunal.

2. Page 36:

The words Section 115 read with [Rule 23 (3)] should be read as **Section 115 read with [Rule 23 (4)]**

3. Page 40 –In point (8),The words -

"If convertible securities are offered on a preferential basis with an option to apply for and get equity shares allotted, the price of the resultant shares shall be determined beforehand on the basis of a valuation report of a registered valuer"

shall be substituted as under:

"where convertible securities are offered on a preferential basis with an option to apply for and get equity shares allotted, the price of the resultant shares pursuant to conversion shall be determined-

(i). either upfront at the time when the offer of convertible securities is made, on the basis of valuation report of the registered valuer given at the stage of such offer, or

(ii). at the time, which shall not be earlier than thirty days to the date when the holder of convertible security becomes entitled to

apply for shares, on the basis of valuation report of the registered valuer given not earlier than sixty days of the date when the holder of convertible security becomes entitled to apply for shares:

Provided that the company shall take a decision on point (i) or (ii) at the time of offer of convertible security itself and make such disclosure in the explanatory statement.

4. Page 49- In point 2 of Issue of Certificates for Shares and other Securities (Section 46), the words **SA-2 shall be read as SH-2**.

5. Page 53- In point No. 12, the words **DIV-5 shall be read as IEPF-1**.

6. Page 68– In the points wherein the special resolution is required, reference to section 262,304,319,321 shall be omitted by Insolvency and Bankruptcy code,2016.

7. Page 69 – Point (f) shall be omitted.

8. Page 104 - Point (c) shall be omitted.

9. Page 125 – In regulation 73, after point (g), the following point shall be inserted:

(h) disclosures, similar to disclosures specified in Part G of Schedule VIII, if the issuer or any of its promoters or directors is a wilful defaulter indicating the following:

1.

(a) Name of the bank declaring the entity as a wilful defaulter;
(b) The year in which the entity is declared as a wilful defaulter;
(c) Outstanding amount when the entity is declared as a wilful defaulter;
(d) Name of the party declared as a wilful defaulter;
(e) Steps taken, if any, for the removal from the list of wilful defaulters;
(f) Other disclosures, as deemed fit by the issuer in order to enable investors to take informed decisions;
(g) Any other disclosure as specified by the Board.

2. The fact that the issuer or any of its promoters or directors is a wilful defaulter shall be disclosed prominently on the cover page with suitable cross-referencing to the pages.

3. Disclosures specified herein shall be made in a separate chapter or section distinctly identifiable in the Index / Table of Contents.

10. Page 127 – In point (c) of part (b), if listed for less than twenty six weeks, **the words "closing prices" shall be read as "volume weighted average prices".**

11. Page 130 – In Rule 13(1), the following proviso to be added after first para of point 1–

Provided that in case of any preferential offer made by a company to one or more existing members only, the provisions of sub-rule (1) and proviso to sub-rule (3) of rule 14 of Companies (Prospectus and Allotment of Securities) Rules, 2014 shall not apply.

12. Page 130 –

(i) Point 2(c) shall be omitted, which is as under:

(c) The securities allotted by way of preferential offer shall be made fully paid up at the time of their allotment.

(ii) Point (h) shall be read as follows:

"(h) where convertible securities are offered on a preferential basis with an option to apply for and get equity shares allotted, the price of the resultant shares pursuant to conversion shall be determined-
(i) either upfront at the time when the offer of convertible securities is made, on the basis of valuation report of the registered valuer given at the stage of such offer, or
(ii) at the time, which shall not be earlier than thirty days to the date

when the holder of convertible security becomes entitled to apply for shares, on the basis of valuation report of the registered valuer given not earlier than sixty days of the date when the holder of convertible security becomes entitled to apply for shares:

Provided that the company shall take a decision on sub-clauses (i) or (ii) at the time of offer of convertible security itself and make such disclosure under the explanatory statement to be annexed to the notice of the general meeting.

13. The revised Lesson 6- Due Diligence – Mergers and Amalgamations is attached at the end of this supplements.

14. The revised Lesson 7- Competition Law Due Diligence is attached at the end of this supplements.

15. Page 320: the paragraph shall be read as under

ISO standards for Environment

The ISO 14000 family addresses various aspects of environmental management. It provides practical tools for companies and organizations looking to identify and control their environmental impact and constantly improve their environmental performance. It helps organizations improve their environmental performance through more efficient use of resources and reduction of waste, gaining a competitive advantage and the trust of stakeholders. ISO 14001:2015 and ISO 14004:2016 focus on environmental management systems.

ISO 14001:2015 helps an organization achieve the intended outcomes of its environmental management system, which provide value for theenvironment, the organization itself and interested parties. Consistent with the organization's environmental policy, the intended outcomes of an environmental management system include:

- enhancement of environmental performance;
- fulfilment of compliance obligations;
- achievement of environmental objectives.

ISO 14004:2016 provides guidance for an organization on the establishment, implementation, maintenance and improvement of a robust, credible and reliable environmental management system. The guidance provided is intended for an organization seeking to manage its environmental responsibilities in a systematic manner that contributes to the environmental pillar of sustainability. The other standards in the family focus on specific environmental aspects such as life cycle analysis, communication and auditing.

Elements of the ISO 14001 standard

- ISO 14001 contains the core elements for an effective environmental management system. It can be applied to both service and manufacturing sectors. The main elements of the standard are:
- Environmental policy
- Planning
- Implementation and operation
- Checking and corrective action
- Management review
- Continuous improvement

16. Page 329-The words form CHG 10 **shall be read as CHG-1.**

17. Page 330 - In last para, the words "under the seal of the company", **shall be read as "under the seal, if any, of the company**".

Lesson 6
Due Diligence –Mergers and Amalgamations

LESSON OUTLINE

- Introduction
- Due diligence process in M&A strategy
- Business Financial and Legal Due diligence
- Data Room Management
- Cultural Due diligence
- Corporate Governance Due diligence
- Due diligence on takeovers
- Impact of Due diligence on valuation

LEARNING OBJECTIVES

The decision to merge or amalgamate has to be based on rational analysis, which can be formed only after evaluation of information and records available. Due Dilligence is the assessment process to judge the benefits vis-à-vis the threats that are likely in post merger scenario. In fact there are several factors financial/non financial/open/hidden factors that influence the ultimate choice of strategy. The process of analysis of strategic choices on various aspects for merger is done through due diligence process. This involves analysis of business, financial, legal, cultural, governance aspects. This lesson is based on Companies Act, 2013, as the provisions relating to Mergers and Acquisitions came into effect from 15-12-2016.

On 7th November, 2016 Central Government issued a notification for enforcement of section 230-233, 235-240, 270-288 etc. pertaining to proceedings relating to arbitration, compromise, arrangements and reconstruction of companies which came into effect from 15th December, 2016.

INTRODUCTION

A company may decide to accelerate its growth by developing into new business areas, which may or may not be connected with its traditional business areas, or by exploiting some competitive advantage that it may have. Once a company has decided to enter into a new business area, it has to explore various alternatives to achieve its aims.

Basically, there can be three alternatives available to it:

(i) the formation of a new company;

(ii) the acquisition of an existing company;

(iii) merger with an existing company.

The decision as to which of these three options are to be accepted, will depend on the company's assessment of various factors including in particular:

(i) the cost that it is prepared to incur;

(ii) the likelihood of success that is expected;

(iii) the degree of managerial control that it requires to retain.

For a firm desiring immediate growth and quick returns, mergers can offer an attractive opportunity as they obviate the need to start from 'scratch' and reduce the cost of entry into an existing business. However, this will need to be weighed against the fact that unless the shareholders of the transferor company (merging company) are paid the consideration in cash, part of the ownership of the existing business remains with the former owners.

Merger with an existing company will, generally, have the same features as an acquisition of an existing company. However, identifying the right candidate for a merger or acquisition is an art, which requires sufficient care and calibre.

Once an organization has identified the various strategic possibilities, it has to make a selection amongst them. There are several factors financial/non financial/ open/hidden factors that influence the ultimate choice of strategy. The process of analysis of strategic choices on various aspects for merger is done through due diligence process.

Due Diligence Process in the M&A Strategy

Stages	For Buyer	For seller
Preparation Stage	➢ M&A Strategy formulation ➢ Preparation of List of potential targets ➢ Appoint external advisor for evaluation of targets ➢ Short list targets ➢ Create Due diligence team	➢ Structure a Business plan ➢ Preparation of list of potential buyers ➢ Appoint external advisor ➢ Shortlist buyers

Pre diligence	➢ Approach targets ➢ Negotiation of initial terms ➢ Execute Non Disclosure Agreement ➢ Compilation of list of data required	➢ Approach buyers ➢ Negotiate initial terms ➢ Execution of Non-Disclosure agreement ➢ Creation of Data room
Due diligence	➢ Inspection of Data room ➢ Analysis of private documents ➢ Evaluation of risk and return ➢ Structure the terms and conditions	➢ Assistance in data room ➢ Setting deadlines for offer
Negotiations	➢ Make final offer ➢ Negotiate and agree on terms	➢ Compile final offers ➢ select best offer ➢ negotiations
Post diligence	➢ Post merger integration and cultural adjustments	➢ Termination of data room and ownership exchange

ACTIVITY SCHEDULE FOR PLANNING A MERGER

As there are two steps of process of M&A filing of 1stmotion application (Take permission/ instruction for holding of Meetings) with NCLT and filing of 2nd motion petition (Scheme of M&A) with NCLT. Each step includes number of activities and processes as defined as under:

Sl.	***Activity***	***Action to be taken for completion of activity***
(1)	***(2)***	***(3)***
1.	Objects clause to be examined	Check the object clause of Memorandum of Association of all the Companies with regard to the power of amalgamation.
		Check the object clause of the transferee company regarding power to carry on the business of the transferor company; if it is not then it is necessary to amend the Objects Clause to add objects of transferor Companies.
		Check if authorized share capital of the transferee company is sufficient; if not then it is necessary to amend the capital clause of the Company.
2.	Preparation of Draft Scheme of Amalgamation	Aspects of Business Valuation, calculation of Swap ratio etc. are being carried out during this process.

3.	Board meeting of the transferor and transferee companies to be held.	Notice, Agenda, notes to Agenda and draft resolution of the Board Meeting to be sent. Board Meeting to be held. Agenda for Board Meeting will include the following items: • Effective date to be announced: • Approval of the scheme of amalgamation • Approval of Ratio • Directors/Officers to be empowered to make application to appropriate Tribunal and to take necessary action.
4.	Stock Exchange	Immediately after the board meeting approving the scheme/ exchange ratio, both companies will have to inform the respective stock exchanges.
5.	Press Release	The news may be released to the press for information and others.
6.	Financial Institutions/ Banks/Trustees to Debenture holders, if any, to be formally advised their consent sought.	Financial institutions/trustees to Debenture holders, if any to be formally advised and their consent sought.
7.	Application to the Tribunal . If there are any calls in arrears of transferor company, the Tribunal direction to be sought specifically. In case of a merger of a potentially sick company with a healthy company, the possibility of reducing the share capital of the sick company to the extent of losses to be considered and procedure for reduction to be undertaken. This would have an effect on the EPS of the merged company.	An application to the Tribunal concerned both to the transferor and transferee companies will have to be made under Companies (Compromises, Arrangements and Amalgamations) Rules, 2016. It shall be made in Form NCLT-1 along with a notice of admission in Form NCLT-2, for direction to convene the meeting. Affidavit in support of application will be in Form NCLT-6 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016. After considering the application in NCLT-1, tribunal can give the following instructions regarding holding and concluding of Meeting. Fixing the time and place of the meeting or meetings, appointing a Chairperson, the procedure to be followed at the meeting, including voting in person or by proxy or by postal ballot or by voting through electronic means, The time within which the chairperson of the meeting is required to report the result of the meeting to the Tribunal and Such other matters as the Tribunal may deem necessary. The Tribunal may dispense with calling of a meeting of creditor or class of creditors where such creditors or class of creditors, having at least ninety per cent. value, agree and confirm, by way of affidavit, to the scheme of compromise or arrangement,

<table>
<tr><td>8.</td><td>Notices of Extra Ordinary General Meeting.</td><td><u>Person entitled to receive the notice:</u> The notice shall be sent individually to each of the Creditors or Members and the debenture-holders at the address registered with the company.

<u>Person authorized to send the notice:</u>

• Chairman of the Company, or
• If tribunal so direct- by the Company or its liquidator or by any other person

<u>Modes of Sending of notice:</u>

• By Registered post, or by Speed post, or by courier, or
• By e-mail, or by hand delivery, or by any other mode as directed by the tribunal

Notice should be accompanied with:
— The statement.
— a copy of the scheme
— form of proxy
The Notice of the meeting shall be advertised in Form No. CAA-2 at least in one English Newspaper and in at least one vernacular language newspaper. It shall indicate the time within which copies of the compromise or arrangement shall be made available to the concerned persons free of charge from the registered office of the company.
• Such Newspaper advertisement shall be published on the website of the company at least 30 days before the date fixed for meeting, as directed by tribunal. (Section 230(3))
• In case of Listed Company, such notice and other documents shall also be published on the website of SEBI and stock exchange where securities of the Company are listed.</td></tr>
<tr><td>9.</td><td>• Notice to Statutory Authorities</td><td>A notice in Form No CAA-3 along with Copy of Scheme of C&A, the explanatory statement and Disclosures mentioned in Annexure A, shall also be sent to followings:

• The Central Government, The Registrar of Companies and The income-tax authorities, in all cases
• The Reserve Bank of India, the Securities and Exchange Board of India, the Competition Commission of India, and the stock exchanges, as may be applicable.

Other Sectoral Regulators or authorities, as required by Tribunal

Notice shall be sent to the office of the authority after sending of notice to members or creditors of the Company by Registered post, or by Speed post, or by courier, or by hand delivery</td></tr>
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<tr><td>10.</td><td>Meetings of Members</td><td>The meetings will be held as scheduled. The management will answer the queries of the members, permitted by the Chair.

The voting at the meeting or meetings held in pursuance of the directions of the Tribunal on all resolutions shall take place by poll or by voting through electronic means. Approval is required of a majority in number of persons present and voting representing three-fourths in value of the members.

The Chairperson of the meeting shall, within the time fixed by the Tribunal, or where no time has been fixed, within 3 (Three) days after the conclusion of the meeting, submit a report to the Tribunal on the result of the meeting in Form No. CAA.4.</td></tr>
<tr><td>11</td><td>Petition to Tribunal</td><td>The Company shall, within 7 (seven) days of the filing of the report by the Chairperson, present a petition to the Tribunal in Form No. CAA.5 for sanction of the scheme of compromise or arrangement.</td></tr>
<tr><td>12</td><td>Directions on the Petition by tribunal</td><td>The Tribunal shall fix a date for the hearing of the petition. The notice of the hearing of the petition shall also be served by the Tribunal;
▪ To the Objectors or
▪ To Their Representatives under sub-section (4) of section 230 of the Act and
▪ To the Central Government and
▪ Other Authorities who have made representation under rule 8 and have desired to be heard in their representation.</td></tr>
<tr><td>13</td><td>Publication of notice of the hearing</td><td>The notice of the hearing shall be advertised in the same newspaper in which the notice of the meeting was advertised or in such other newspaper as the Tribunal may direct, at least 10 (ten) days before the date fixed for the hearing.</td></tr>
<tr><td>14.</td><td>Hearing and Order.</td><td>Any person interested including creditors and employees may appear before the tribunal and make submissions.

Where the Tribunal sanctions the Merger & Amalgamation, An order made under section 232 read with section 230 of the Act shall be in Form No.CAA.6 & CAA 7 with such variation as the circumstances may require.

The order may include an order for dissolution of the transferor company, if the Official Liquidator has submitted the report.

The Court may make any provision for any person who dissents from the scheme.

The order will not have any effect till a certified copy is filed with the Registrar.</td></tr>
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15.	Filing/Annexing	The order of the Tribunal shall be filed with the Registrar by the company in Form INC-28 within a period of thirty days of the receipt of the copy of order, or such other time as may be fixed by the Tribunal. In computing the period of 30 days the time taken in obtaining certified copy has to be excluded. A copy of the Tribunal order will be annexed to every copy of the memorandum and articles of association of the transferee company.
16	FEMA	Approval of Reserve Bank of India will be obtained for allotment of shares to non-residents under FEMA, wherever required.
17	Effective Date	As soon as the scheme has become effective, particulars will be intimated through press and to the government authorities, banks, creditors, customers and others. Certified copy of the Court order will be given where necessary.
18	Compliance until completion of scheme	Every company in relation to which the order is made shall, until the completion of the scheme, file a statement in Form No. CAA.8 within two hundred and ten days from the end of each financial year with the Registrar every year, duly certified by a chartered accountant or a cost accountant or a company secretary in practice indicating whether the scheme is being complied with in accordance with the orders of the Tribunal or not.

Annexure- A:

INFORMATION REQUIRED TO BE CIRCULATED ALONG WITH THE NOTICE

a. Details of the order of the Tribunal directing the calling, convening and conducting of the meeting:-
   - Date of the Order;
   - Date, time and venue of the meeting.
b. Details of the company including:
   - Corporate Identification Number (CIN) or Global Location Number (GLN) of the company;
   - Permanent Account Number (PAN);
   - Name of the company;
   - Date of incorporation;
   - Type of the company (whether public or private or one person company);
   - Registered office address and email address;
   - Summary of main object as per the memorandum of association; and main business carried on by the company;
   - Details of change of name, registered office and objects of the company during the last five years;
   - Name of the stock exchange (s) where securities of the company are listed, if applicable;
   - Details of the capital structure of the company including authorised, issued, subscribed and paid up share capital; and
   - Names of the promoters and directors along with their addresses.

c. Relationship in case of Combined Application: if the scheme of compromise or arrangement relates to more than one company, then the fact and details of any relationship subsisting between such companies who are parties to such scheme of compromise or arrangement, including holding, subsidiary or of associate companies.

d. Disclosure about effect of M&A on material interests of directors, Key Managerial Personnel (KMP) and debenture trustee

e. Details of Board Meeting:
   - The date of the board meeting at which the scheme was approved by the board of directors
   - The name of the directors who voted in favour of the resolution,
   - The name of the directors who voted against the resolution and
   - The name of the directors who did not vote or participate on such resolution

f. Explanatory Statement disclosing details of the scheme of compromise or arrangement including:
   - Parties involved in such compromise or arrangement;
   - Appointed date, effective date, share exchange ratio (if applicable) and other considerations, if any;
   - Summary of valuation report (if applicable) including basis of valuation and fairness opinion of the registered valuer, if any, and the declaration that the valuation report is available for inspection at the registered office of the company;
   - Details of capital or debt restructuring, if any;
   - Rationale for the compromise or arrangement;
   - Benefits of the compromise or arrangement as perceived by the Board of directors to the company, members, creditors and others (as applicable);
   - Amount due to unsecured creditors.

g. Disclosure about the effect of the Merger & Amalgamation (C&A) on: Section 230(3)
   - Key Managerial Personnel;
   - Directors;
   - Promoters;
   - Non-Promoter Members;
   - Depositors;
   - Creditors;
   - Debenture holders;
   - Deposit trustee and debenture trustee;
   - Employees of the company:
   - Shareholders of the Company

h. A report adopted by the directors of the merging companies explaining effect of compromise on each class of shareholders, key managerial personnel, promoters and non-promoter shareholders laying out in particular the share exchange ratio, specifying any special valuation difficulties;

i. Below Mentioned Details: Following below mentioned details

- Investigation or proceedings, if any, pending against the company under the Act.
- Details of approvals, sanctions or no-objection(s), if any, from regulatory or any other governmental authorities required, received or pending for the proposed scheme of compromise or arrangement
- A statement to the effect that the persons to whom the notice is sent may vote in the meeting either in person or by proxies, or where applicable, by voting through electronic means
- A copy of the valuation report, if any Section 230(3)

j. Details of availability of documents: Details of the availability of the following documents for obtaining extract from or for making or obtaining copies of or for inspection by the members and creditors, namely

- Latest audited financial statements of the company including consolidated financial statements;
- Copy of the order of Tribunal in pursuance of which the meeting is to be convened or has been dispensed with;
- Copy of scheme of Merger & Amalgamation (C&A);
- Contracts or agreements material to the Merger & Amalgamation (C&A);
- The certificate issued by Auditor of the company to the effect of the accounting treatment, if any,
- Proposed scheme of Merger & Amalgamation (C&A) is in conformity with the Accounting Standards prescribed under Section 133 of the Companies Act, 2013; and
- Such other information or documents as the Board or Management believes necessary and relevant for making decision for or against the scheme;

k. Some Other documents: Where an order has been made by the Tribunal under section 232(1), merging companies or the companies in respect of which a division is proposed, shall also be required to circulate the following:

- The draft of the proposed terms of the scheme drawn up and adopted by the directors of the merging company;
- Confirmation that a copy of the draft scheme has been filed with the Registrar;
- The report of the expert with regard to valuation, if any;
- Supplementary accounting statement if the last annual accounts of any of the merging company relate to a financial year ending more than six months before the first meeting of the company summoned for the purposes of approving the scheme

Explanation- For the purposes of above disclosure required to be made by a company, these shall be made in respect of all the companies which are part of the compromise or arrangement.

PREPARATION OF SCHEME OF AMALGAMATION

The scheme of amalgamation to be prepared by the company should contain *inter-alia* the following information:

1. Definitions of transferor and transferee as well as the definition of the undertaking of the transferor company.
2. Authorised, issued and subscribed capital of transferor and transferee companies.

3. Basis of scheme should be explained briefly on the recommendation of valuation report, covering transfer of assets/liabilities, specified date, reduction or consolidation of capital, application to financial institutions as lead institution for permission, etc.
4. Change of name, object and accounting year.
5. Protection of employment.
6. Dividend position and prospects.
7. Management structure, indicating the number of directors of the transferee company and the transferor company.
8. Applications under Sections 230 and 230 of the Companies Act, 2013 to obtain approval from the Tribunal.
9. Expenses of amalgamation.
10. Conditions of the scheme to become effective and operative and the effective date of amalgamation.

The basis of the scheme should be framed on the reports of valuers, auditors and chartered accountants of assets of both the merger partner companies. The underlying idea is to ensure that the scheme is just and equitable to the shareholders and employees of each of the amalgamating companies and to the public at large. It should be ensured that common yardstick is adopted for valuation of shares of each of the amalgamating company for fixing rate of exchange of shares on merger.

A. Information Required by the Professional Generally

Cross holding of the Directors of the Transferee and Transferor Companies.

1. Relationship between the directors of the transferee and transferor companies under the Companies Act, 2013.
2. Names of the officers of both the transferee and transferor companies who are to be authorised to sign the Application, Affidavit and Petition. (The companies concerned can authorise any one person to act on behalf of them, who may be from either of the companies).
3. Names of the English and regional language newspapers in which notices are to be published.
4. Names in preferential order as to the chairmen of the meetings of the transferee and transferor companies. (The chairman in this case need not be a director on the board of directors of the company concerned or even a member of the company).
5. List of creditors and their dues. List of individual cases to be given, as well as categorisation in various slabs.

B. Information/Documents that may be required by the Regional Director, Ministry of Corporate Affairs, in Connection With Amalgamation.

1. Balance sheets for last five years of the transferee company.
2. Balance sheets for last five years of the transferor company.
3. Two copies of the valuation report of the chartered accountants.
4. List of top shareholders of the transferee company.

5. List of top shareholders of the transferor company.
6. List of directors of the transferor company and their other directorships.
7. List of directors of the transferee company and their other directorships.
8. Number and percentage of NRI and foreign holding in the transferee and transferor companies.
9. Rights/Bonus/Debentures Issues made by the transferee and the transferor companies in the last five years.

C. The Following Information is required to be furnished to the Auditors Appointed by the Official Liquidator.

From the transferor company

1. Certified true copy of the scheme of amalgamation alongwith the petition.
2. Certified true copy of the Memorandum and Articles of Association of the company.
3. List of shareholders of the company with their shareholding. Any changes during the last five years to be indicated.
4. Accounts of the company made upto the appointed day of amalgamation.
5. Address of the registered office of the company.
6. Present authorised and paid-up share capital of the company.
7. Changes in the Board of directors during the last five years alongwith list of present Board of directors.
8. List of associated concern in which directors are interested.
9. List of various appeals pending under Income-tax, Sale Tax, Excise Duty, Custom Duty, FEMA, etc.
10. Details of loans and advances given to the associated concern/companies under the same management during the last five years.
11. Details of revaluation of assets.
12. Details of any allegations and/or complaints against the company.
13. Details of amount paid to the managing director, directors or any relative of the directors during the last five years.
14. Comparative statement of profit and loss account and balance sheet for the last five years.
15. Details of bad debts written off during the last five years.
16. List of all charges registered with the Registrar of Companies and the amount secured against the same.
17. Copy of the latest annual return filed with the Registrar of Companies alongwith Annexures.
18. Details of all the subsidiary companies as under:
    (a) Authorised and paid-up share capital of the company.

(b) List of present shareholders alongwith details of changes in the shareholding patterns during the last five years.

The following information of the transferee company is required by the auditor:

1. Names of the existing directors of the company.
2. List of common shareholders of the companies involved in the amalgamation with individual shareholding.
3. Authorised and paid up capital of the company.
4. Copy of latest audited balance sheet.

The auditors may also require the following records of the transferor company for examination:

1. Books of accounts and relevant records for the last five years.
2. Minutes book of Board and General Meetings.

IMPACT OF DUE DILIGENCE ON VALUATION

To arrive at a value of the target company we need to analyze aspects viz. how much should we pay for the target company, how much is the target worth, how does this compare to the current market value of the target company, etc.

Senior management at the acquiring company will delegate the M&A process to a special team of experts responsible for assessing the value of the target company. The composition of the buyer's team is likely different from that of the seller's team because of the buyer's motivation, depending on whether the buyer is strategic or financial. After inspecting the relevant documents, the functional due diligence team provides a summary of findings regarding his or her area of expertise. These summaries are then collected and incorporated into a diligence synthesis and a technical and financial analysis of the target. Expert recommendations are then summarized into an integration recommendation.

As we are aware that the due diligence process helps in identifying the hidden risks/ litigations etc, it helps in arriving at a right price after valuation process by discounting for the risks identified and vice versa. The techniques of valuations are dealt in Corporate Restructuring, Valuations and Insolvency study material.

DATA ROOM MANAGEMENT IN STRATEGIC DECISIONS

As regards data room management, security is a critical issue in managing the data room, as sensitive information should not be leaked to the people not covered by non-disclosure or confidentiality agreements executed between the parties. Such information leaks can have detrimental effects on the entire transaction process, and may adversely affect the consideration being paid by a buyer, or the consideration being exchanged in a merger, if either party senses a process damaged or tainted by leaks. A person is generally employed as a coordinator for this purpose and is assigned to manage the operation of the data room by minimizing security and information leaks, recording data room attendance, and searching briefcases and other bags as attendees leave the data room.

The process of collecting the necessary data room documents and information is extensive and time consuming. Data must be compiled, indexed and properly organized and this process takes up valuable resources. Function-wise contact persons are assigned to manage the data room information from their areas. They ensure that their operational area provides the information needed, indexes the relevant documents and information, coordinates with management regarding documents that may be copied, and

verifies that information that cannot be copied. Similarly under virtual data room copying or printing of documents may be delayed.

HR AND CULTURAL DUE DILIGENCE IN BUSINESS TRANSACTIONS

Culture is a complex system with a multitude of interrelated processes and mechanisms based on which the organisation functions. It includes vision/mission of the organisation, work flow process, communication mechanism, formal procedures, informal practices, strategy setting mechanism and so on.

Corporate Culture is embedded deeply in the organization and in the behavior of the people there. It is not necessarily equal to the image the company gives itself in brochures and on the website. Therefore, it is difficult to determine an organization's culture from the outside. Especially in pre-merger negotiations – when time and confidentiality are critical factors while trust still needs to be established – it can be a challenging task to find out if the cultures of the potential partners fit together.

The issues of cultural integration and the issues of human behaviour need to be addressed simultaneously if not well before the issues of financial and legal integration are considered. Implementation of structural nature may be financially and legally successful. But if cultural issues are ignored, the success may only be transient.

According to KPMG Study 83% of all mergers and acquisitions failed to produce any benefit for the shareholders and over half actually destroyed value. It revealed that the overwhelming cause for failure is the people and cultural difference. Difficulties encountered in M & As are amplified in cross-cultural situations, when the companies involved are from two or more countries.

Culture of an organization means the sum total of things the people do and the things the people do not do. Behavioral patterns get set because of the culture. These patterns create mental blocks for the people in the organization. Pre-merger survey and summarization of varying cultures of different companies merging, needs to be carried out. People belonging to each defined culture need to be acquainted with other cultures of other merging companies. They need to be mentally prepared to adopt the good points of other cultures and shed the blockades of their own cultures. Such an open approach will make the fusion of cultures and ethos easy and effective.

The successful merger demands that strategic planners are sensitive to the human issues of the organisations. For the purpose, following checks have to be made constantly to ensure that:

— sensitive areas of the company are pinpointed and personnel in these sections carefully monitored;

— serious efforts are made to retain key people;

— a replacement policy is ready to cope with inevitable personnel loss;

— records are kept of everyone who leaves, when, why and to where;

— employees are informed of what is going on, even bad news is systematically delivered. Uncertainty is more dangerous than the clear, logical presentation of unpleasant facts;

— training department is fully geared to provide short, medium and long term training strategy for both production and managerial staff;

— likely union reaction be assessed in advance;

— estimate cost of redundancy payments, early pensions and the like assets;

— comprehensive policies and procedures be maintained up for employee related issues such as office procedures, new reporting, compensation, recruitment and selection, performance, termination, disciplinary action etc.;

— new policies to be clearly communicated to the employees specially employees at the level of managers, supervisors and line manager to be briefed about the new responsibilities of those reporting to them;

— family gatherings and picnics be organised for the employees and their families of merging companies during the transition period to allow them to get off their inhibitions and breed familiarity.

Why is corporate culture that important?

Corporate culture influences the performance of an organization, since it determines

- Style of tackling problems
- Method or style of communication
- Adaptability of employees
- Organization commitment to strategies and ultimately to vision and mission etc

A perfect integration would develop a new culture form both former cultures of the partners. Ideally, this new culture should include the best elements from both organizations.

Corporate culture influences the performance of an organization, since it determines:

1. Style of organizational functioning
2. Adaptability of people to changes
3. The way people interact with each other
4. The way the organization interacts with stakeholders
5. Level of commitment

Types of Cultural differences

There are three types of cultural differences:

1. Cross-national differences (especially in cross-boarder mergers),
2. Cross-organizational differences,
3. Cross-functional differences.

Areas of differences in cultural aspects:

- Organizational values
- Management culture and leadership styles
- Organizational myths and stories
- Organizational taboos, rituals
- Cultural symbols

Ideally, this new culture should include the best elements from both organizations.

Survey by Accenture and Economist Intelligence Unit

Accenture and the Economist Intelligence Unit in the first half of 2006, surveyed senior executives in North America, Europe and Asia on their mergers and acquisitions (M&A) activities and their experience in integrating companies. Similar survey was also administered to 156 executives based in India during the

fourth quarter of 2006.

Of the total respondents in India, 40% were senior-level. About 64% were from companies that had global annual revenues of US$100m or more and 36% had revenues of US$1bn or more. 45% executive mainly played roles in strategy and business development and 42% in general management. Their companies were from a wide range of industries, including financial services (25%), IT and technology (21%) and professional services (13%).

The Key findings of the Survey

Human and Cultural Factors

Accenture Survey points out that for integrating a cross border company, 43%, respondents found addressing cultural issues as critical. The real challenge, after an acquisition is, therefore, the integration of the two companies. That is why the integration should be given a focused attention. There should be a focus on aligning the acquired company's processes through the business excellence model.

Human Factor

Studies on post-acquisition performance have primarily been a centre of interest of researchers in strategy, economics and finance. The identified factors of performance variations have usually ranged from the industry match (complementary of assets, similarities of markets and products, synergies in production, strategic orientation, etc.), pricing policy, financing and size of the operation and type of the transaction, bidding conditions, etc.

By contrast to quantitative measurements from finance and economics, the research, which has focused on the organizational and human side of M & As, has mostly dealt with identifying factors that might have played a role in the integration process of the merging entities and led to successful outcomes. Despite the absence of a direct causal correlation, several dimensions have been identified as having an important impact on M&A performance, these include psychological, cultural and managerial factors, knowing that the human factor covers at the same time employees and managers of the companies.

Psychological Factors

A large part of the existing research has looked at the psychological effects of M&A on employees. Scholars have pointed out that strong impact that the operations could have on employees, in particular the resulting increase in stress and anxiety due to changes in work practices and tasks, managerial routines, colleagues environment, the hierarchy, etc. Further, merger and acquisitions often introduce an environment of uncertainty among employees about job losses and future career development. It has been pointed out that stress and insecurity may lead to employee resistance to change, absenteeism and lack of commitment to work and the organisation. Employee resistance prevents the building up of a well functioning organisation and constructive cooperative environment. Lock of work commitments have a negative impact on individual and organizational performance measured in terms of productivity, quality, and service. Moreover, a relationship between organizational and financial performance has also been identified which may have consequences for the market value of company.

On the other hand, it has been argued that satisfied employees are presumed to work harder, better, and longer with higher productivity records. Even though a direct relationship between job satisfaction and corporate performance remains to be established with certainty, it appears that lower job satisfaction is a cause of higher absenteeism, which, in turn is shown to have a negative influence on organizational performance.

Cultural factors

Cultural differences look like playing both ways. Although distant cultural environments make the integration process harder, the lack of culture-fit or cultural compatibility has often been used to explain M&A failure. Cultural differences have also been considered a source of lower commitment to work, making co-operation more difficult, particularly from employees of the acquired company. In this regard, scholars have largely given account of the lack of co-operation momentum stemming from a “we” versus “them” attitude, resulting in hostility among employees.

It is, therefore, no surprise that strong cultural differences are usually associated with a negative impact on M&A performance, since the integration process is less easy and deals with higher employee resistance, communication problems, and lower interest in co-operation. Noticeably, cultural clashes are likely to be more prominent in cross-national than domestic acquisitions, since such mergers bring together not only two companies that have different organizational cultures but also organizational cultures rooted in national diversity. The scholars have identified building up of a common culture as essential for the success of merger and acquisitions. Researchers have found that high levels of employees’ social identification with the organization’s identity results in increased work effort, higher performance, reduced staff turnover and more frequent involvement in positive organizational citizenship.

Cultural Due Diligence

Cultural Due Diligence (CDD) is the process of identifying, assessing, investigating, evaluating and defining the cultures of two or more distinct corporates through a cultural analysis so that the similarities and differences that impact the merged organization are identified and remedial actions are taken well in advance. It should be carried along with M&A due diligence stage itself. The findings of cultural due diligence would be the base for post integration strategies.

Scope of Cultural Due diligence

The Cultural Due Diligence process covers

1. Leadership, Strategies and Governing principles: It covers vision, mission, values, business strategy development, leadership effectiveness, ethics, board room practices, role of independent directors etc.,
2. Relationships and behaviors: It covers trust, inter/intra group relationships, community and customers
3. Communication: feedback, information sharing, employee trust in information
4. Infrastructure: formal procedures, processes, systems, policies, structure and teams
5. Involvement & Decision Making: authority levels, accountability, expectations and the decision making process
6. Change Management: creativity, innovation, recognition, continuous learning and diversity
7. Communication platforms
8. Finance: perception of financial health and the role of the employee and the level of financial comprehension and impact on the business

Cultural Due Diligence is the process which analyzes the cultural aspects which includes:

- leadership vision
- management practices,
- governing principles,

- policies and procedures
- informal practices,
- relationship management,
- employee satisfaction,
- customer satisfaction,
- key business drivers,
- organizational characteristics,
- organizational perceptions
- communication mechanism etc.

Questions being analysed in Cultural Due Diligence

The following questions are being analysed for determining the different corporate culture.

1. What are the primary issues driving the business strategy?
2. What are the levels of relations ship with the board and the senior management?
3. What is the nature of the relationship between groups and units in the organization?
4. What formal and informal systems are in place and what part do they play in the daily life of doing the work?
5. How do people dress and address each other?
6. How do the office ambience differ?
7. What are the working hours?
8. What are the variation in utilization of technology in daily routine?
9. How actual work is performed?
10. How authority and responsibility is allocated?
11. How the performance evaluation is done and reward is granted?
12. What are the reporting relationship in the organization?
13. What are the supervisory practices in the organization?

The above questions indicate that the corporate culture is basically focused on:

1. Leadership style and management practices.
2. Manner of organizational functioning.
3. Employees.

How to address Cultural Differences during merger?

1. Formation of strategies for cultural integration.
2. Analyzing the existing cultures.
3. Identifying common aspects and differences.
4. Decide if you want to go on with one of the existing cultures or if you prefer an integration culture.
5. Establish ‘bridges’ between both companies.
6. Establish a basis and mechanisms for the new culture.

7. Extensive interaction with people.

The following mechanism may help in resolving cultural differences:

1. Newsletters and hotlines.
2. Workshops.
3. Surveys, questionnaires and feedback analysis.
4. Synergy teams.
5. Continuous interactions.

CORPORATE GOVERNANCE DUE DILIGENCE

FACTORS INFLUENCING QUALITY OF CORPORATE GOVERNANCE

Quality of governance primarily depends on following factors:

(*i*) Integrity of the management;

(*ii*) Ability of the Board;

(*iii*) Adequacy of the processes;

(*iv*) Commitment level of individual Board members;

(*v*) Quality of corporate reporting;

(*vi*) Participation of stakeholders in the management.

While corporate governance is an important element affecting the long-term financial health of companies, it is only part of the larger economic context in which companies operate. The corporate governance framework depends on the legal, regulatory and institutional environment, business ethics and awareness of the environmental and societal interests of the constituencies in which it operates.

The degree to which corporations observe basic principles of good corporate governance is an increasingly important factor for taking key investment decisions. International flow of capital enables companies to seek financing from a larger pool of investors. If companies are to reap the full benefits of the global capital market, capture efficiency gains, benefit by the economies of scale and attract long term capital, adoption of corporate governance standards must be credible, consistent, coherent and inspiring.

As the final analysis the factors which add greater value through Good Governance, may be summarized as follows:

- Adoption of good governance practices provides stability and growth to the enterprise.
- Good governance system, demonstrated by adoption of good corporate governance practices, builds confidence amongst stakeholders as well as prospective stakeholders.
- Investors pay higher price to the corporates demonstrating strict adherence to internationally accepted norms of corporate governance.
- Effective governance reduces perceived risks, consequently reduces cost of capital and enables Board of directors to take quick and better decisions which ultimately improves bottom line of the corporates.

- Adoption of good corporate governance practices provides long-term sustainability and strengthens stakeholders' relationship.
- A good corporate citizen becomes an icon and enjoys a position of respect.
- Potential stakeholders aspire to enter into relationships with enterprises whose governance credentials are exemplary.

The following compliances can be checked in this regard.

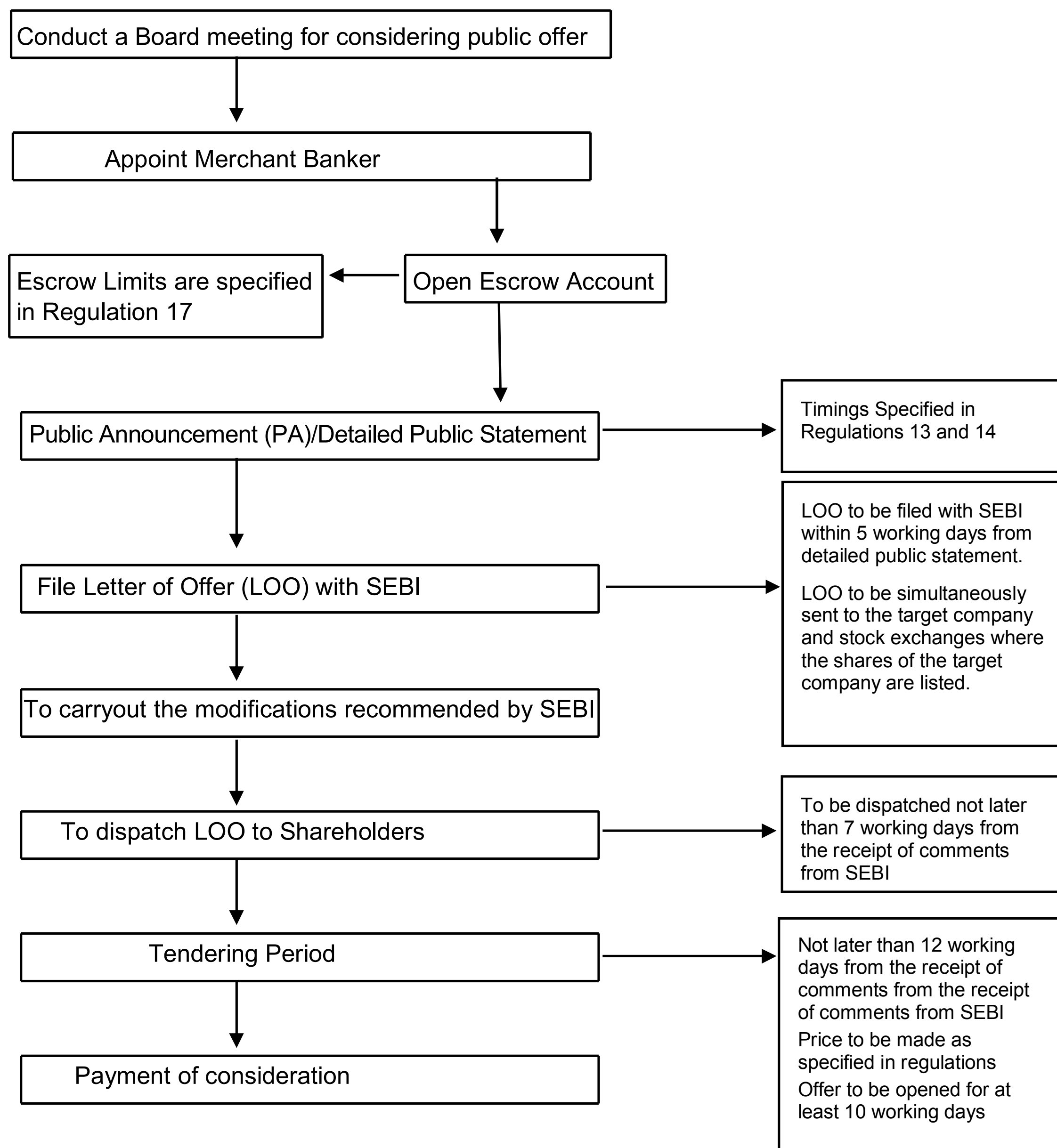
1. Board structure and composition
2. Board committees
3. Annual Report disclosures
4. Board Processes
5. Corporate social responsibilities

TAKEOVERS DUE DILIGENCE

Takeover process under SEBI (SAST) Regulation 2011 – An Overview

SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011

Takeover of companies whose securities are listed on one or more recognized stock exchanges in India is regulated by the provisions of the Listing Agreements with various stock exchanges and the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011. The compliances under the regulations include event based/continual disclosures, open offer requirements including public announcement, escrow account, obligations of acquirer/target company/merchant banker, undertaking/authorization, offer price etc.



Note:

Exception from the applicability

The regulations shall not apply to direct and indirect acquisition of shares or voting rights in, or control over a company listed without making a public issue, on the institutional trading platform of a recognised stock exchange.

CHECKLISTS ON TAKEOVERS

Checklist for Compliances under SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011

1. Whether any acquisition/transfer has triggered open offer?
2. Ensure that a merchant banker of Category I has been appointed who is not an associate of or group of acquirer or the target company.
3. Ensure that an escrow account has been opened with the required deposit.
4. the consideration payable under the open offer shall be calculated at the offer price, assuming full acceptance of the open offer, and in the event the open offer is subject to differential pricing, shall be computed at the highest offer price, irrespective of manner of payment of the consideration (computed as per sub regulation (2) of regulation 16)
5. A letter duly authorizing target company to realize the value of escrow account as specified in these regulations.
6. An undertaking from the target company that none of the Acquirer/Persons Acting in Concert have been prohibited by SEBI from dealing in securities, in terms of direction issued under Section 11B of SEBI Act.
7. An undertaking from the sellers, promoters, directors of the target company that they have not been prohibited by SEBI from dealing in securities, in terms if direction issued under section 11B of SEBI Act.
8. An undertaking from the target company that it has complied with the provisions of Listing Agreement, and that any non-compliance or delayed compliance has been brought to the notice of Target Company.
9. An undertaking from the target company that it has complied with the provisions of these regulations, and that any non-compliance or delayed compliance has been brought to the notice of Target Company.
10. A public announcement of an open offer to the shareholder of the target company has been given and detailed public statement has been published as per the prescribed timeline in case of Acquirer acquires the shares or voting rights of the target company in excess of the limits prescribed under Regulation 3 and 4 of these regulations.
11. The public announcement has been sent to all the stock exchanges on which the shares of the target company are listed, to SEBI and to the target company at its registered office within one working day of the date of the public announcement. The time within which the public announcement is required to be made to the Stock Exchanges under different circumstances is tabulated below. It is to be checked that following compliances have been made by the company.

12. A detailed public statement has been published by the acquirer through the Manager to the Open Offer within maximum 5 working days from the date of public announcement as provided in regulation 13(4).

13. In case of indirect acquisition where none of condition specified in regulation 5(2) are satisfied, the detailed public statement has been published not later than five working days of the completion of the primary acquisition of shares or voting rights in or control over the company or entity holding shares or voting rights in, or control over the target company.

14. The compliances relating to publication of public announcement and detailed public statement by the acquirer has been complied under regulation 14.

15. The public announcement contains the information as provided in regulation 15.

16. The acquirer through the manager to the offer has filed a draft letter of offer along with the fee as prescribed in regulation 16, with SEBI for its observations within 5 working days of publication Detailed Public Statement.

17. The offer price is not less than the price as calculated under regulation 8 for frequently or infrequently traded shares.

18. The minimum of 26% of voting capital of the company is being offered subject to minimum public holding requirements.

19. The acquirer has made complete payment of consideration whether in the form of cash, or as the case may be, by issue, exchange or transfer of securities, to all shareholders who have tendered shares in acceptance of the open offer, within ten working days of the expiry of the tendering period.

20. The unclaimed balances, if any, lying to the credit of the special escrow account at the end of seven years from the date of deposit thereof, has been transferred to the Investor Protection and Education Fund established under the Securities and Exchange Board of India (Investor Protection and Education Fund) Regulations, 2009.

21. Ensure that:

    (a) any person, who along with PACs crosses the threshold limit of 5% of shares or voting rights, has disclosed his aggregate shareholding and voting rights to the Target Company at its registered office and to every Stock Exchange where the shares of the Target Company are listed within 2 working days of acquisition as per the format specified by SEBI. (Regulation 29(1) read with Regulation 29(3))

    (b) any person, who together with persons acting in concert with him, holds shares or voting rights entitling them to five per cent or more of the shares or voting rights in a target company, has disclosed the number of shares or voting rights held and change in shareholding or voting rights, even if such change results in shareholding falling below five per cent, if there has been change in such holdings from the last disclosure made under sub-regulation (1) or under this sub regulation; and such change exceeds two per cent of total shareholding or voting rights in the target company, in such form as may be specified. (Regulation 29(2) read with Regulation 29(3))

22. Continual disclosures of aggregate shareholding has been made within 7 days of financial year ending on March 31 to the target company at its registered office and every stock exchange where the shares of the Target Company are listed by:

    (a) Shareholders (along with PACs, if any) holding shares or voting rights entitling them to exercise

25% or more of the voting rights in the target company.

(b) Promoter (along with PACs, if any) of the target company irrespective of their percentage of holding.

23. The promoter (along with PACs) of the target company has disclosed details of shares encumbered by them or any invocation or release of encumbrance of shares held by them to the target company at its registered office and every stock exchange where shares of the target company are listed, within 7 working days of such event.

A. Checklist for Acquirer

Preliminary Examination of a target company:

The acquirer has to undertake a preliminary study on the target company, before taking any action for taking over a company. He may consider the following points.

It may be noted that this list is not an exhaustive checklist and it varies depends on size of the company nature of industry

(a) Information has to be collected on Target Company and to be analysed on financial and legal angle.

(b) Register of members to be examined to verify the profile of the shareholders.

(c) Title of the target company with respect to immovable properties may be verified.

(d) Financial statements of Target Company have to be examined.

(e) Examination of Articles and Memorandum of Association of the Company.

(f) Examination of charges created by the Company

(g) Applicability of FEMA provisions if any relating to FDI has to be looked into.

(h) Import and Export of technology if any

(i) Business prospects etc.

A merchant Banker of Category I have to be appointed. It has to be ensured that the merchant banker is not an associate of or group of acquirer or the target company

Escrow Account:

(1) (i) An escrow account has to be opened and the following sum has to be deposited.

(ii) The escrow amount shall be calculated in the following manner, as specified in regulation 17,—

For consideration payable under the public offer,—

On the first 500 crores	25 per cent; of the consideration
On the balance consideration	An additional amount equal to 10% of balance consideration.

If, an open offer is made conditional upon minimum level of acceptance, hundred percent of the consideration payable in respect of minimum level of acceptance or fifty per cent of the consideration payable under the open offer, whichever is higher, shall be deposited in cash in the escrow account.

(2) The consideration payable under the open offer shall be computed as provided for in sub-regulation (2) of regulation 16 and in the event of an upward revision of the offer price or of the offer size, the value of the escrow amount shall be computed on the revised consideration calculated at such revised offer price, and the additional amount shall be brought into the escrow account prior to effecting such revision.

(3) The escrow account referred to in sub-regulation (1) may be in the form of,—

(a) cash deposited with any scheduled commercial bank;

(b) bank guarantee issued in favour of the manager to the open offer by any scheduled commercial bank; or

(c) deposit of frequently traded and freely transferable equity shares or other freely transferable securities with appropriate margin:

Provided that securities sought to be provided towards escrow account under clause (c) shall be required to conform to the requirements set out in sub-regulation (2) of regulation 9.

Regulation 9(2) specifies the following requirements.

(a) such class of shares are listed on a stock exchange and frequently traded at the time of the public announcement;

(b) such class of shares have been listed for a period of at least two years preceding the date of the public announcement;

(c) the issuer of such class of shares has redressed at least ninety five per cent. of the complaints received from investors by the end of the calendar quarter immediately preceding the calendar month in which the public announcement is made;

(d) the issuer of such class of shares has been in material compliance with the listing agreement for a period of at least two years immediately preceding the date of the public announcement:

Provided that in case where the Board is of the view that a company has not been materially compliant with the provisions of the listing agreement, the offer price shall be paid in cash only;

(e) the impact of auditors' qualifications, if any, on the audited accounts of the issuer of such shares for three immediately preceding financial years does not exceed five per cent. of the net profit or loss after tax of such issuer for the respective years; and

(f) the Board has not issued any direction against the issuer of such shares not to access the capital market or to issue fresh shares.

(4) In the event of the escrow account being created by way of a bank guarantee or by deposit of securities, the acquirer shall also ensure that at least one per cent of the total consideration payable is deposited in cash with a scheduled commercial bank as a part of the escrow account.

(5) For such part of the escrow account as is in the form of a cash deposit with a scheduled commercial bank, the acquirer shall while opening the account, empower the manager to the open offer to instruct the bank to issue a banker's cheque or demand draft or to make payment of the amounts lying to the credit of the escrow account, in accordance with requirements under these regulations.

(6) For such part of the escrow account as is in the form of a bank guarantee, such bank guarantee shall be in favour of the manager to the open offer and shall be kept valid throughout the offer period and for an additional period of thirty days after completion of payment of consideration to shareholders who have tendered their shares in acceptance of the open offer.

(7) For such part of the escrow account as is in the form of securities, the acquirer shall empower the manager to the open offer to realise the value of such escrow account by sale or otherwise, and in the event there is any shortfall in the amount required to be maintained in the escrow account, the manager to the open offer shall be liable to make good such shortfall.

(8) The manager to the open offer shall not release the escrow account until the expiry of thirty days from the completion of payment of consideration to shareholders who have tendered their shares in acceptance of the open offer, save and except for transfer of funds to the special escrow account as required under regulation 21.

(9) In the event of non-fulfillment of obligations under these regulations by the acquirer the Board may direct the manager to the open offer to forfeit the escrow account or any amounts lying in the special escrow account, either in full or in part.

(10) The escrow account deposited with the bank in cash shall be released only in the following manner,—

(a) the entire amount to the acquirer upon withdrawal of offer in terms of regulation 23 as certified by the manager to the open offer:

Provided that in the event the withdrawal is pursuant to clause (c) of sub-regulation (1) of regulation 23, the manager to the open offer shall release the escrow account upon receipt of confirmation of such release from the Board;

(b) for transfer of an amount not exceeding ninety per cent of the escrow account, to the special escrow account in accordance with regulation 21;

(c) to the acquirer, the balance of the escrow account after transfer of cash to the special escrow account, on the expiry of thirty days from the completion of payment of consideration to shareholders who have tendered their shares in acceptance of the open offer, as certified by the manager to the open offer;

(d) the entire amount to the acquirer upon the expiry of thirty days from the completion of payment of consideration to shareholders who have tendered their shares in acceptance of the open offer, upon certification by the manager to the open offer, where the open offer is for exchange of shares or other secured instruments;

(e) the entire amount to the manager to the open offer, in the event of forfeiture for non-fulfillment of any of the obligations under these regulations, for distribution in the following manner, after deduction of expenses, if any, of registered market intermediaries associated with the open offer,—

(i) one third of the escrow account to the target company;

(ii) one third of the escrow account to the Investor Protection and Education Fund established under the Securities and Exchange Board of India (Investor Protection and Education Fund) Regulations, 2009; and

(iii) one third of the escrow account to be distributed pro-rata among the shareholders who have accepted the open offer.

Undertakings/Authorisation:

Ensure to obtain following undertakings/authorization.

1. A letter duly authorizing Target Company to realize the value of escrow account in terms of Takeover Regulations.

2. An undertaking to Target Company that none of the Acquirer/Persons Acting in Concert have been

prohibited by SEBI from dealing in securities, in terms of direction issued under Section 11B of SEBI Act.

3. An undertaking from the sellers, promoters, directors of the Target Company that they have not been prohibited by SEBI from dealing in securities, in terms if direction issued under Section 11B of SEBI Act.
4. An undertaking from the Target Company that it has complied with the provisions of Listing Agreement, and that any non-compliance or delayed compliance has been brought to the notice of Target Company.

Public announcement (PA):

1. Public announcement.

SEBI (SAST) Regulation, 2011 provides that whenever Acquirer acquires the shares or voting rights of the Target Company in excess of the limits prescribed under Regulation 3 and 4, than Acquirer is required to give a Public Announcement of an Open Offer to the shareholder of the Target Company. During the process of making the Public Announcement of an Open Offer, the Acquirer is required to give Public Announcement and publish Detailed Public Statement. The regulations have prescribed the separate timeline for Public Announcement as well as for Detailed Public Statement.

(i) Public Announcement
(ii) Detailed Public Statement

Timing of Pubic Announcement

The Public Announcement shall be sent to all the stock exchanges on which the shares of the target company are listed. Further, a copy of the same shall also be sent to the Board and to the target company at its registered office within one working day of the date of the public announcement. The time within which the Public Announcement is required to be made to the Stock Exchanges under different circumstances is tabulated below:

Applicable Regulation	Particulars	Time of making Public Announcement to Stock Exchange
13(1)	Agreement to Acquirer Shares or Voting Rights or Control Over The Target Company	On the same day of entering into agreement to acquire share, voting rights or control over the Target Company.
13(2)(a)	Market Purchase of shares	Prior to the placement of purchase order with the stock broker.
13(2)(b)	Acquisition pursuant to conversion of Convertible Securities without a fixed date of conversion or upon conversion of depository receipts for the underlying shares	On the same day when the option to convert such securities into shares is exercised.
13(2)(c)	Acquiring shares or voting rights or control pursuant to conversion of Convertible Securities with a fixed date	On the second working day preceding the scheduled date of conversion of such securities into

	of conversion	shares.
13(2)(d)	In case of disinvestment	On the date of execution of agreement for acquisition of shares or voting rights or control over the Target Company.
13(2)(e)	In case of Indirect Acquisition where the parameters mentioned in Regulation 5(2) are not met	Within four working days of the following dates, whichever is earlier: a. When the primary acquisition is contracted; And b. Date on which the intention or decision to make the primary acquisition is announced in the public domain.
13(2)(f)	In case of Indirect Acquisition where the parameters mentioned in Regulation 5(2) are met	On the same day of the following dates, whichever is earlier: a. When the primary acquisition is contracted; And b. Date on which the intention or decision to make the primary acquisition is announced in the public domain.
13(2)(g)	Acquisition of shares, voting rights or control over the Target Company pursuant to Preferential Issue	On the date on which the board of directors of the target company authorizes such preferential issue.
13(2)(h)	Increase in voting rights pursuant to a buy-back not qualifying for exemption under Regulation 10	Not later than 90th day from the date of closure of the buyback offer by the target company.
13(2)(i)	Acquisition of shares, voting rights or control over the Target Company where the such acquisition is beyond the control of acquirer	Not later than two working days from the date of receipt of such intimation.
13(3)	Voluntary Offer	On the same day when the Acquirer decides to make Voluntary Offer.

Timing of Detailed Public Statement

In terms of Regulation 13(4) of SEBI (SAST) Regulations, 2011, a Detailed Public Statement shall be published by the acquirer through the Manager to the Open Offer within maximum 5 working days from the date of Public Announcement.

However in case of Indirect Acquisition where none of condition specified in Regulation 5(2) are satisfied, the Detailed Public Statement shall be published not later than five working days of the completion of the primary acquisition of shares or voting rights in or control over the company or entity holding shares or voting rights in, or control over the target company.

Publication of Public Announcement and Detailed Public Statement

Regulation 14 of SEBI (SAST) Regulation, 2011 provides the requirements relating to publication of Public Announcement and Detailed Public Statement which are tabulated below:

Regulation	***Particulars***	***Time***	***To whom***
14(1)	Public Announcement	On the same day	All the stock exchanges on which the shares of the target company are listed. The stock exchanges shall forthwith disseminate such information to the public.
14(2)	Public Announcement	One working day of the date of the public announcement	Board and to the target company at its registered office
14(3)	Detailed Public Statement	5 working days from the date of Public Announcement.	Publication in the following newspaper: (a) One Hindi national language daily with wide circulation (b) One English national language daily with wide circulation (c) One regional national language daily with wide circulation language at a place where registered office of the company is situated. (d) One regional language daily with wide circulation at the place of the stock exchange where the maximum volume of trading in the shares of the target company is recorded during the sixty trading days preceding the date of the public announcement.
14(4)	Detailed Public Statement	Simultaneously with publication of such detailed public statement in the	A copy of 'Detailed Public Statement shall be sent to followings: (a) Board

		newspapers.	(b) All the stock exchanges in which the shares of the target company are listed (c) The target company at its registered office

Contents of Public announcement (Regulation 15)

The public announcement shall contain such information as may be specified, including the following,—

(a) name and identity of the acquirer and persons acting in concert with him;

(b) name and identity of the sellers, if any;

(c) nature of the proposed acquisition such as purchase of shares or allotment of shares, or any other means of acquisition of shares or voting rights in, or control over the target company;

(d) the consideration for the proposed acquisition that attracted the obligation to make an open offer for acquiring shares, and the price per share, if any;

(e) the offer price, and mode of payment of consideration; and

(f) offer size, and conditions as to minimum level of acceptances, if any.

(2) The detailed public statement pursuant to the public announcement shall contain such information as may be specified in order to enable shareholders to make an informed decision with reference to the open offer.

(3) The public announcement of the open offer, the detailed public statement, and any other statement, advertisement, circular, brochure, publicity material or letter of offer issued in relation to the acquisition of shares under these regulations shall not omit any relevant information, or contain any misleading information.

Filing Draft Letter of offer (Regulation 16)

Within 5 working days of publication Detailed Public Statement, the acquirer through the manager to the offer is required to file a draft letter of offer with SEBI for its observations.

The Board shall give its comments on the draft letter of offer as expeditiously as possible but not later than fifteen working days of the receipt of the draft letter of offer and in the event of no comments being issued by the Board within such period, it shall be deemed that the Board does not have comments to offer:

Provided that in the event the Board has sought clarifications or additional information from the manager to the open offer, the period for issuance of comments shall be extended to the fifth working day from the date of receipt of satisfactory reply to the clarification or additional information sought.

Provided further that in the event the Board specifies any changes, the manager to the open offer and the acquirer shall carry out such changes in the letter of offer before it is dispatched to the shareholders.

Offer price

Offer price is the price at which the acquirer announces to acquire shares from the public shareholders under the open offer. The offer price shall not be less than the price as calculated under regulation 8 of the SAST Regulations, 2011 for frequently or infrequently traded shares.

If the target company’s shares are frequently traded then the open offer price for acquisition of shares under

the minimum open offer shall be highest of the following:

- Highest negotiated price per share under the share purchase agreement (“SPA”) triggering the offer;
- Volume weighted average price of shares acquired by the acquirer during 52 weeks preceding the public announcement (“PA”);
- Highest price paid for any acquisition by the acquirer during 26 weeks immediately preceding the PA;
- Volume weighted average market price for sixty trading days preceding the PA.

If the target company’s shares are infrequently traded then the open offer price for acquisition of shares under the minimum open offer shall be highest of the following:

- Highest negotiated price per share under the share purchase agreement (“SPA”) triggering the offer;
- Volume weighted average price of shares acquired by the acquirer during 52 weeks preceding the public announcement (“PA”);
- Highest price paid for any acquisition by the acquirer during 26 weeks immediately preceding the PA;
- The price determined by the acquirer and the manager to the open offer after taking into account valuation parameters including book value, comparable trading multiples, and such other parameters that are customary for valuation of shares of such companies.

It may be noted that the Board may at the expense of the acquirer, require valuation of shares by an independent merchant banker other than the manager to the offer or any independent chartered accountant in practice having a minimum experience of 10 years.

The shares of the target company will be deemed to be frequently traded if the traded turnover on any stock exchange during the 12 calendar months preceding the calendar month, in which the PA is made, is at least 10% of the total number of shares of the target company. If the said turnover is less than 10%, it will be deemed to be infrequently traded.

Minimum size:

It has to be ensured that minimum of 26% of voting capital of the company is being offered subject to minimum public holding requirements.

Date of opening of offer:

The date of opening of offer has to be not later than the 12 working days from the date of receipt of recommendation from SEBI.

Period of offer:

The offer to acquire should remain open for a period of minimum 10 days.

Competitive Bid and Revision:

Ensure to revise the offer price in consultation with merchant bankers in case of competitive bid if any.

Payment of consideration (Regulation 21)

For the amount of consideration payable in cash, the acquirer shall open a special escrow account with a banker to an issue registered with the Board and deposit therein, such sum as would, together with cash transferred under clause (b) of sub-regulation (10) of regulation 17, make up the entire sum due and payable to the shareholders as consideration payable under the open offer, and empower the manager to the offer to operate the special escrow account on behalf of the acquirer for the purposes under these regulations.

(2) Subject to provisos to sub-regulation (11) of regulation 18, the acquirer shall complete payment of consideration whether in the form of cash, or as the case may be, by issue, exchange or transfer of securities, to all shareholders who have tendered shares in acceptance of the open offer, within ten working days of the expiry of the tendering period.

(3) Unclaimed balances, if any, lying to the credit of the special escrow account referred to in sub-regulation (1) at the end of seven years from the date of deposit thereof, shall be transferred to the Investor Protection and Education Fund established under the Securities and Exchange Board of India (Investor Protection and Education Fund) Regulations, 2009.

Completion of acquisition (Regulation 22)

The acquirer shall not complete the acquisition of shares or voting rights in, or control over, the target company, whether by way of subscription to shares or a purchase of shares attracting the obligation to make an open offer for acquiring shares, until the expiry of the offer period:

Provided that in case of an offer made under sub-regulation (1) of regulation 20, pursuant to a preferential allotment, the offer shall be completed within the period as provided under sub-regulation (1) of regulation 74 of Securities and Exchange Board of India (Issue of Capital and Disclosure) Regulations, 2009.

Provided further that in case of a delisting offer made under regulation 5A, the acquirer shall complete the acquisition of shares attracting the obligation to make an offer for acquiring shares in terms of regulations 3, 4 or 5, only after making the public announcement regarding the success of the delisting proposal made in terms of sub-regulation (1) regulation 18 of Securities and Exchange Board of India (Delisting of Equity Shares) Regulations, 2009.

(2) Notwithstanding anything contained in sub-regulation (1), subject to the acquirer depositing in the escrow account under regulation 17, cash of an amount equal to one hundred per cent of the consideration payable under the open offer assuming full acceptance of the open offer, the parties to such agreement may after the expiry of twenty-one working days from the date of detailed public statement, act upon the agreement and the acquirer may complete the acquisition of shares or voting rights in, or control over the target company as contemplated.

(2A) Notwithstanding anything contained in sub-regulation (1), an acquirer may acquire shares of the target company through preferential issue or through the stock exchange settlement process, other than through bulk deals or block deals, subject to ,-

(i) such shares being kept in an escrow account,

(ii) the acquirer not exercising any voting rights over such shares kept in the escrow account:

Provided that such shares may be transferred to the account of the acquirer, subject to the acquirer complying with requirements specified in sub-regulation (2).

(3) The acquirer shall complete the acquisitions contracted under any agreement attracting the obligation to make an open offer not later than twenty-six weeks from the expiry of the offer period:

Provided that in the event of any extraordinary and supervening circumstances rendering it impossible to complete such acquisition within such period, the Board may for reasons to be published, may grant an extension of time by such period as it may deem fit in the interests of investors in securities and the securities market.

Withdrawal of open offer (Regulation 23)

23.(1) An open offer for acquiring shares once made shall not be withdrawn except under any of the following circumstances,—

(a) statutory approvals required for the open offer or for effecting the acquisitions attracting the obligation to make an open offer under these regulations having been finally refused, subject to such requirements for approval having been specifically disclosed in the detailed public statement and the letter of offer;

(b) the acquirer, being a natural person, has died;

(c) any condition stipulated in the agreement for acquisition attracting the obligation to make the open offer is not met for reasons outside the reasonable control of the acquirer, and such agreement is rescinded, subject to such conditions having been specifically disclosed in the detailed public statement and the letter of offer; or

(d) such circumstances as in the opinion of the Board, merit withdrawal.

Explanation.— For the purposes of clause (d) of sub-regulation (1), the Board shall pass a reasoned order permitting withdrawal, and such order shall be hosted by the Board on its official website.

Provided that an acquirer shall not withdraw an open offer pursuant to a public announcement made under clause (g) of sub-regulation (2) of regulation 13, even if the proposed acquisition through the preferential issue is not successful.

(2) In the event of withdrawal of the open offer, the acquirer shall through the manager to the open offer, within two working days,—

(a) make an announcement in the same newspapers in which the public announcement of the open offer was published, providing the grounds and reasons for withdrawal of the open offer; and

(b) simultaneously with the announcement, inform in writing to,—

(i) the Board;

(ii) all the stock exchanges on which the shares of the target company are listed, and the stock exchanges shall forthwith disseminate such information to the public; and

(iii) the target company at its registered office.

Directors of the target company (Regulation 24)

(1) During the offer period, no person representing the acquirer or any person acting in concert with him shall be appointed as director on the board of directors of the target company, whether as an additional director or in a casual vacancy:

Provided that after an initial period of fifteen working days from the date of detailed public statement, appointment of persons representing the acquirer or persons acting in concert with him on the board of directors may be effected in the event the acquirer deposits in cash in the escrow account referred to in regulation 17, one hundred per cent of the consideration payable under the open offer:

Provided further that where the acquirer has specified conditions to which the open offer is subject in terms of clause (c) of sub-regulation (1) of regulation 23, no director representing the acquirer may be appointed to the board of directors of the target company during the offer period unless the acquirer has waived or attained such conditions and complies with the requirement of depositing cash in the escrow account.

(2) Where an open offer is made conditional upon minimum level of acceptances, the acquirer and persons acting in concert shall, notwithstanding anything contained in these regulations, and regardless of the size of the cash deposited in the escrow account referred to regulation 17, not be entitled to appoint any director representing the acquirer or any person acting in concert with him on the board of directors of the target company during the offer period.

(3) During the pendency of competing offers, notwithstanding anything contained in these regulations, and regardless of the size of the cash deposited in the escrow account referred to in regulation 17, by any acquirer or person acting in concert with him, there shall be no induction of any new director to the board of directors of the target company:

Provided that in the event of death or incapacitation of any director, the vacancy arising therefrom may be filled by any person subject to approval of such appointment by shareholders of the target company by way of a postal ballot.

(4) In the event the acquirer or any person acting in concert is already represented by a director on the board of the target company, such director shall be participate in any deliberations of the board of directors of the target company or vote on any matter in relation to the open offer.

Obligation of Target Company (Regulation 26)

Once a Public Announcement is made, the board of directors of the Target Company is expected to ensure that the business of the target company is conducted in the ordinary course. Alienation of material assets, material borrowings, issue of any authorized securities, announcement of a buyback offer etc. is not permitted, unless authorized by shareholders by way of a special resolution by postal ballot.

- The target company shall furnish to the acquirer within two working days from the identified date, a list of shareholders and a list of persons whose applications, if any, for registration of transfer of shares, in case of physical shares, are pending with the target company.

- After closure of the open offer, the target company is required to provide assistance to the acquirer in verification of the shares tendered for acceptance under the open offer, in case of physical shares.

- Upon receipt of the detailed public statement, the board of directors of the target company shall constitute a committee of independent directors to provide reasoned recommendations on such open offer, and the target company shall publish such recommendations and such committee shall be entitled to seek external professional advice at the expense of the target company. The recommendations of the Independent Directors are published in the same newspaper where the Detailed Public Statement is published by the acquirer and are published at least 2 working days before opening of the offer. The recommendation will also be sent to SEBI, Stock Exchanges and

the Manager to the offer.

Obligations of the Acquirer (Regulation 25)

(1) Prior to making the public announcement of an open offer for acquiring shares under these regulations, the acquirer shall ensure that firm financial arrangements have been made for fulfilling the payment obligations under the open offer and that the acquirer is able to implement the open offer, subject to any statutory approvals for the open offer that may be necessary.

(2) In the event the acquirer has not declared an intention in the detailed public statement and the letter of offer to alienate any material assets of the target company or of any of its subsidiaries whether by way of sale, lease, encumbrance or otherwise outside the ordinary course of business, the acquirer, where he has acquired control over the target company, shall be debarred from causing such alienation for a period of two years after the offer period:

Provided that in the event the target company or any of its subsidiaries is required to so alienate assets despite the intention to alienate not having been expressed by the acquirer, such alienation shall require a special resolution passed by shareholders of the target company, by way of a postal ballot and the notice for such postal ballot shall inter alia contain reasons as to why such alienation is necessary.

(3) The acquirer shall ensure that the contents of the public announcement, the detailed public statement, the letter of offer and the post-offer advertisement are true, fair and adequate in all material aspects and not misleading in any material particular, and are based on reliable sources, and state the source wherever necessary.

(4) The acquirer and persons acting in concert with him shall not sell shares of the target company held by them, during the offer period.

(5) The acquirer and persons acting in concert with him shall be jointly and severally responsible for fulfillment of applicable obligations under these regulations

Obligations of the manager to the open offer (Regulation 27)

(1) Prior to public announcement being made, the manager to the open offer shall ensure that,—

- (a) the acquirer is able to implement the open offer; and
- (b) firm arrangements for funds through verifiable means have been made by the acquirer to meet the payment obligations under the open offer.

(2) The manager to the open offer shall ensure that the contents of the public announcement, the detailed public statement and the letter of offer and the post offer advertisement are true, fair and adequate in all material aspects, not misleading in any material particular, are based on reliable sources, state the source wherever necessary, and are in compliance with the requirements under these regulations.

(3) The manager to the open offer shall furnish to the Board a due diligence certificate along with the draft letter of offer filed under Regulation 16.

(4) The manager to the open offer shall ensure that market intermediaries engaged for the purposes of the open offer are registered with the Board.

(5) The manager to the open offer shall exercise diligence, care and professional judgment to ensure compliance with these regulations.

(6) The manager to the open offer shall not deal on his own account in the shares of the target company during the offer period.

(7) The manager to the open offer shall file a report with the Board within fifteen working days from the expiry of the tendering period, in such form as may be specified, confirming status of completion of various open offer requirements.

Consequences of Violation of obligations SEBI (SAST) Regulations, 2011 (Regulation 32)

SAST Regulations, 2011 have laid down the general obligations of acquirer, Target Company and the manager to the open offer. For failure to carry out these obligations as well as for failure / non-compliance of other provisions of these Regulations, penalties have been laid down there under. These consequences include:

- directing the divestment of shares acquired;
- directing the transfer of the shares / proceeds of a directed sale of shares to the investor protection fund;
- directing the target company / any depository not to give effect to any transfer of shares;
- directing the acquirer not to exercise any voting or other rights attached to shares acquired;
- debarring person(s) from accessing the capital market or dealing in securities;
- directing the acquirer to make an open offer at an offer price determined by SEBI in accordance with the Regulations;
- directing the acquirer not to cause, and the target company not to effect, any disposal of assets of the target company or any of its subsidiaries unless mentioned in the letter of offer;
- directing the acquirer to make an offer and pay interest on the offer price for having failed to make an offer or has delayed an open offer;
- directing the acquirer not to make an open offer or enter into a transaction that would trigger an open offer, if the acquirer has failed to make payment of the open offer consideration;
- directing the acquirer to pay interest of for delayed payment of the open offer consideration;
- directing any person to cease and desist from exercising control acquired over any target company;
- directing divestiture of such number of shares as would result in the shareholding of an acquirer and persons acting in concert with him being limited to the maximum permissible non-public shareholding limit or below.

LESSON ROUND UP

- M&A Due Diligence involves preparation stage, Pre diligence, diligence, negotiations, post diligence.
- Due diligence impacts valuation in Mergers
- Business, legal, financial, HR/Cultural and corporate governance aspects are analysed in M&A due diligence process.
- Data room management is an important function in due diligence process.
- Data security is crucial in data room management.
- Many mergers and acquisitions fail due to cultural mismatch.

- SEBI (SAST) Regulations, 2011 regulate takeovers covering open offer requirements, disclosure mandates etc.

SELF TEST QUESTIONS

1. What are the stages of M&A due diligence?
2. Prepare a check list for M&A due diligence
3. How does due diligence impact valuations?
4. Describe corporate governance due diligence?
5. How HR/Cultural issues are addressed in mergers?
6. What is the process involved in takeover?

Lesson 7
Competition Law Due Diligence

LESSON OUTLINE

- Introduction
- Competition Act, 2002- An overview
- Need to comply with competition law
- Due diligence of competition law relating to:
  - various agreements (both existing and proposed)
  - dominance and its likely abuse if any, (existing)
  - Combinations (i.e. effect of proposed mergers & Acquisition)
- Competition Compliance Programme

LEARNING OBJECTIVES

Ensuring compliance with competition law, rules etc. is crucial, during strategic business decisions, as the consequences of non-compliance may be serious for concerned companies in terms of investigation by Competition Commission of India (CCI), hefty financial penalties, agreements being unenforceable and void, adverse publicity, damages, possibility of being sued for damages by those harmed by unlawful behaviour and what not.

Due diligence of competition law involves examination of the current/proposed operations and practices of an enterprise to determine the extent of its compliance with the competition law and to identify potential risks and liabilities, and assessment of the adherence to and effectiveness of the company's competition law compliance programme. This process includes examination of business/trade agreements, analysis of proposed mergers/ combination, check into the dominance of an organization so that the same is not abused etc.,

After reading this chapter you will be able to understand the broad aspects of due diligence relating to competition law including anti-competitive agreement, abuse of dominance, regulation of combinations, and the relevant checklists, importance of competition compliance programme etc.

I. INTRODUCTION

In the light of international economic development, there was a need felt to shift the focus from curbing monopolies to promoting competition. Further, in the wake of economic reforms in 1991 in tune with international environment, a high level committee on competition law and policy was constituted under the chairmanship of Shri S.V.S. Raghavan to examine the provisions of MRTP Act, and to propose modern competition law in view of liberalization of economy. The Committee brought out its report on 22nd May, 2000 and the Central Government after a detailed consultative process with Chamber of Commerce, trade associations, professional bodies and general public, enacted the Competition Act, 2002 which received the president's assent on January 13, 2003.

The Competition Act seeks to ensure fair competition by providing for

(a) Prohibition of Anti-Competitive Agreements;

(b) Prohibition of Abuse of Dominance;

(c) Regulation of combinations, acquisitions, mergers etc;

(d) Competition Advocacy.

To fulfill the objectives of the Act, government established Competition Commission of India with effect from October 14, 2003. This has replaced the MRTP Commission, which has been dissolved with effect from October 14, 2009.

Need for compliance of Competition Law

The basic purpose of the competition law is to ensure that markets remain competitive, to the benefit of both business and consumers. The compliance by the market participants of competition law, rules and directions issued by competition authorities, is a precondition in achieving the purpose of law.

Why Comply?

Business community needs to be fully aware that while anti competitive business practices may bring about short-term profits to individual corporations, in the long run they in fact become less competitive. Genuine business competitiveness is demonstrated through fierce competition in individual markets, and only competitiveness that survives market competition can sustain itself in the long term.

All businesses have a duty to act lawfully, but there are more practical reasons why compliance with competition law is particularly important. On a broad level, the main aim of competition law is to ensure that markets remain competitive. Compliance ensures that this aim is achieved to the benefit of both business and consumers. At an individual level, businesses that comply with the law could avoid the various consequences of non-compliance.

Further, compliance with competition law is more than just good corporate governance, as it reduces the risk of the company being subject to an investigation by the Competition authorities. In the event of violation of competition law, business can face significant financial penalties, third party actions and loss of reputation and goodwill.

In an era of global competition, voluntary compliance with competition law is becoming a global standard led by the world's most prominent international corporations. This is due to the growing recognition that breach of competition law brings about managerial burdens rather than market benefits to individual companies.

Corporations are thus obliged to firmly build up a business philosophy of abiding by established rules of fair market competition. In recognition of these facts, it becomes essential that all companies strive for voluntary observance of fair market discipline, and in the process help lay a cornerstone for a mature culture of corporate compliance.

COMPETITION ACT, 2002 – A BIRD'S EYE VIEW

Anti-competitive agreements (Section 3)

What are Anti Competitive Agreements?

These are agreements between enterprises or association of enterprises in respect of production, supply, distribution, storage, acquisition or control of goods or provisions of services, which cause or likely to cause an appreciable adverse effect on competition within India.

How to determine appreciable adverse effect?

The Commission has been put under obligation, while determining whether an agreement has an appreciable adverse effect on competition under section 3, to have due regard to all or any of the following factors, namely:—

(a) creation of barriers to new entrants in the market;

(b) driving existing competitors out of the market;

(c) foreclosure of competition by hindering entry into the market;

(d) accrual of benefits to consumers

(e) improvements in production or distribution of goods or provision of services;

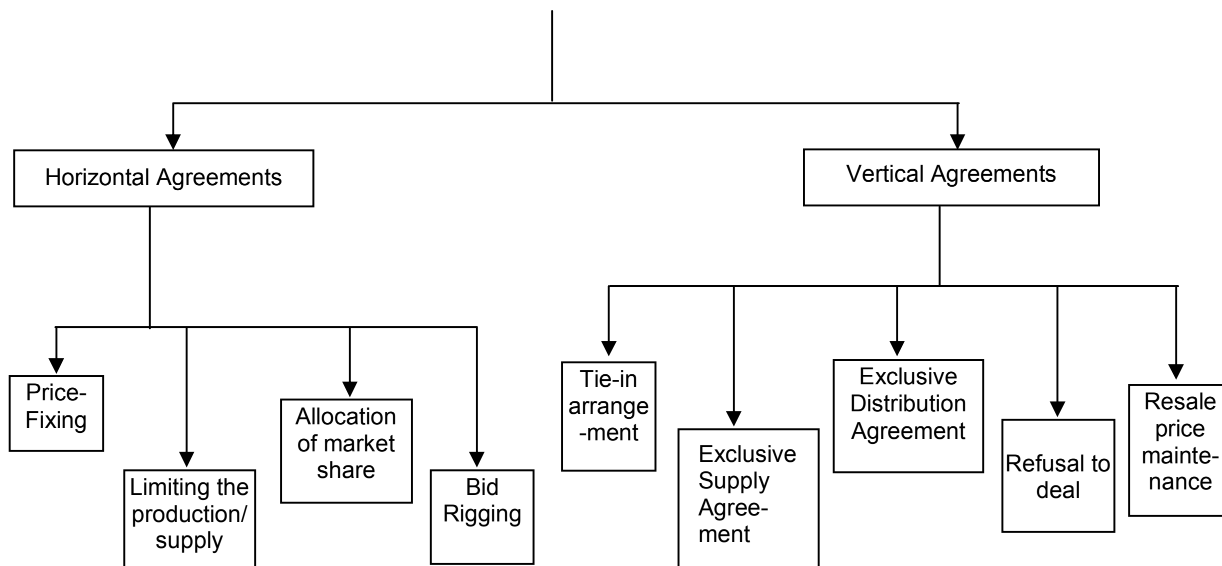
(f) promotion of technical, scientific and economic development by means of production or distribution of goods or provision of services.

What is an Enterprise?

"Enterprise" means a person or a department of the Government, who or which is, or has been, engaged in any activity, relating to the production, storage, supply, distribution, acquisition or control of articles or goods, or the provision of services, of any kind, or in investment, or in the business of acquiring, holding, underwriting or dealing with shares, debentures or other securities of any other body corporate, either directly or through one or more of its units or divisions or subsidiaries, whether such unit or division or subsidiary is located at the same place where the enterprise is located or at a different place or at different places, but does not include any activity of the Government relatable to the sovereign functions of the Government including all activities carried on by the departments of the Central Government dealing with atomic energy, currency, defence and space.

Anti Competitive Agreements are void (Section 3(2)

Anti Competitive Agreements



Horizontal Agreements (Section 3(3))

Price Fixing (Section 3(3)(a))

Price fixing occurs when two or more firms agree to raise or fix the prices in order to increase their profits by reducing competition. It is an attempt at forming a collective monopoly.

Limiting the Production or supply (Section 3(3)(b))

The object of these agreements or arrangements is to eliminate the competition by limiting the quantity.

Allocation of Market Share (Section 3(3)(c))

It means agreement among enterprises that will have exclusive or preferential rights in a designated area for sale, production or provision of services or otherwise.

Bid Rigging (Section (3(3)(d))

An agreement, between enterprises or persons engaged in identical or similar production or trading of goods or provision of services, which has the effect of eliminating or reducing competition for bids or adversely affecting or manipulating the process for bidding. Bid rigging is a particular form of collusive price-fixing behaviour by which firms coordinate their bids.

Vertical Agreements (Section 3(4))

These are agreement between enterprises that are at different stages or levels of production chain and there fore in different markets. These agreements are not considered anti-competitive per se as in the case of horizontal agreements and have to be judged by the rule of reason.

Tie in arrangement (Section 3(4)(a))

It an agreement requiring a purchaser of goods as a condition of such purchase, to purchase some other goods.

Exclusive Supply agreement (Section 3(4)(b)

Exclusive supply agreement or exclusive dealings means an arrangement pr practice whereby a manufacturer or supplier requires his dealers to deal exclusively in his products and not in the products of his competitors.

Exclusive Distribution Agreement (Section 3(4)(c)

Exclusive distribution agreement or exclusive territory includes agreement between enterprises that will have exclusive or preferential rights in a designated area for sales production, performance of services.

Refusal to Deal (Section 3(4)(d)

The practice of restricting persons or class of persons to whom the goods are sold or from whom the goods are bought.

Resale price Maintenance (Section 3(4)(e))

It is a situation in which the supplier forces the distributor/retail seller to sell the good to the customer at prices stipulated by the supplier.

Case Studies on Anti-Competitive Agreement

Case Studies- I

Competition Commission of India (CCI) finds cement companies guilty of anti-competitive agreements-cartelization, collusive price, dispatch and supplies parallelism, creating artificial scarcity by limiting output to raise prices

Facts

Information was filed under section 19 of the Competition Act, 2002 by the Builders' Association of India ('the informant') against the Cement Manufacturers' Association (CMA) 11 cement manufacturing companies for alleged violation of section 3 (Anti-competitive agreements) and section 4 (Abuse of dominant position) of the Competition Act, 2002.

Held

• Mere examination of data belonging to period prior to 20-5-2009 cannot be construed to mean that provisions of the Act have been applied retrospectively. Moreover, if the effects of an act/conduct, prior to 20-5-2009 continue post notification of the date of coming into force of provisions relating to anti-competitive agreements, the CCI has the necessary jurisdiction to look into such conduct.

• Section 3(3)(a) deals with any agreement which directly or indirectly determines the purchase or sale prices, section 3(3)(b) deals with any agreement which limits or controls production, supply, markets, technical development, investment or provision of services.

• The word 'agreement' used in section 3(3) has been defined in section 2(b). The definition is inclusive and inter-alia includes any arrangement, understanding or action in concert irrespective of whether it is written/formal or otherwise or intended to be legally enforceable. Thus, there is no need for an explicit agreement. The same can be inferred from the intention or conduct of the parties.

• Parties to an anti-competitive agreement will not come out in open and reveal their identity to be punished by the competition agencies. This is also the reason why the legislature in its wisdom has made the definition of 'agreement' wide and inclusive and not restricted it to a documented written agreement between parties.

• In cases of conspiracy or existence of any anti-competitive agreement, proof of formal agreement may not be available and may be established by circumstantial evidence alone.

• In addition to the exchange of information on prices and production using CMA as platform, there were other 'plus' or 'facilitating' factors over and above the existence of price parallelism which indicated collusive behaviour among the cement companies. One of the 'plus' factors that suggested a concerted action among the cement companies is the finding by the Director General (DG) as regards the overall low capacity utilisation and lower supply of cement. The overall capacity utilisation of cement companies dropped from 83% in 2009-10 to 73% during 2011-12. The companies were not able to substantiate their low capacity utilisation even during the period as per their version.

• The act of these Cement Companies in limiting and controlling supplies in the market and determining prices through an anti-competitive agreement is not only detrimental to the cause of the consumers but also to the whole economy since cement is a crucial input in construction and infrastructure industry vital for economic development of the country.

• The Cement Manufacturers were directed to deposit the penalty of `6,300 crores (Approx) within 90 days. They were also directed to 'cease and desist' from indulging in any activity relating to agreement, understanding or arrangement on prices, production and supply of cement in the market.

• CMA was directed to disengage and disassociate itself from collecting wholesale and retail prices through the member cement companies and also from circulating the details on production and dispatches of cement companies to its members.

- Aggrieved by CCI's orders, the Respondents appealed before the Competition Appellate Tribunal ("COMPAT"), on the grounds of violation of principles of natural justice.
- COMPAT noted that thorough consideration was not given to the report of the Director General ("DG"), parties' submissions and interlocutory orders. COMPAT observed that procedural defect in nature of non-observance of principles of natural justice cannot be cured in appeal, because if natural justice is violated in the first stage, the same cannot be given as true right in an appeal.
- Accordingly, the COMPAT set aside the impugned orders and remitted the matter to the CCI for fresh adjudication of the issues relating to the alleged violation of Section 3(3)(a) and 3(3)(b) read with Section 3(1) of the Act.
- CCI pursuant to the directions issued by COMPAT, has imposed penalties of Rs. 1147.59 crores (ACC), Rs. 1163.91 crores (ACL), Rs. 167.32 crores (Binani), Rs. 274.02 crores (Century), Rs. 187.48 crores (India Cements), Rs. 128.54 crores (J K Cements), Rs. 490.01 crores (Lafarge), Rs. 258.63 crores (Ramco), Rs. 1175.49 crores (UltraTech) and Rs. 1323.60 crores (Jaiprakash Associates Limited) have been imposed by CCI. In addition, a penalty of Rs. 0.73 crore has also been imposed on CMA. While imposing penalties, the Commission noted the action of the cement companies and CMA as being not only detrimental to the interests of consumers but also as detrimental to the whole economy, as cement is a critical input in construction and infrastructure industry – and thus vital for the economic development of the country. CCI has also imposed a penalty of Rs. 397.51 crore upon Shree Cement Limited vide a separate order.

Case Study- II

The Competition Commission of India imposed a penalty on public sector insurance companies - National Insurance Co. Ltd, New India Assurance Co. Ltd, Oriental Insurance Co. Ltd and United India Insurance Co. Ltd at the rate of 2% of their average turnover of the last three financial years based on the financial statements filed by them for the impugned conduct in contravention of the provisions of section 3(1) read with section 3(3)(d) of the Act by engaging in Anti-Competitive practices and bid rigging in public procurement for social welfare schemes.

Facts:

The case was taken up by the Commission *suo moto* pursuant to an anonymous information alleging cartelization by four public sector insurance companies in relation to a tender issued by the Government of Kerala for the implementation of RSBY (Rashtriya Swasthya Bima Yojna) and CHIS (Comprehensive Health Insurance Scheme) schemes.

A copy of the minutes of the ICCC meeting dated 07.12.2009 attended by the company officials of the above-named public sector insurance companies was enclosed with the anonymous information. These minutes reveal that the 'winner' of said tender was pre-decided by the public sector insurance companies. The Commission directed the DG to conduct an investigation into the allegations. The DG conducted a detailed investigation and found cartelization by these companies during the periods between 2010-11 and 2012-13.

Held:

The Commission directed these public sector insurance companies to cease and desist from indulging in the practices which have been found to be anti-competitive under the provisions of section 3(1) read with section 3(3)(d) of the Act.

The Commission imposed a sum of Rs. 162.80 crore on OP- 1, Rs. 251.07 crore on OP-2, Rs. 100.56 crore on OP-3 and Rs. 156.62 crore on OP-4 as penalties for the impugned conduct in contravention of the provisions of section 3(1) read with section 3(3)(d) of the Act and ordered them to deposit the penalty amount within 60 days of receipt of the order.

Abuse of Dominance (Section 4)

As regards Competition Act, 2002, the following points are significant to understand the concept of 'Abuse of Dominance'

1. What is Dominance?

Explanation to Section 4(2) of the Competition Act, 2002 defines dominant position (dominance) in terms of a position of strength enjoyed by an enterprise, in the relevant market in India, which enables it to:

(a) operate independently of the competitive forces prevailing in the relevant market; or

(b) affect its competitors or consumers or the relevant market in its favour.

2. What is relevant market?

The definition of the term 'Dominant Position' contains the term 'Relevant Market' which is very significant to identify whether an enterprise is in a dominant position or not.

The Competition Act, 2002 defines the term ‘Relevant Market’ also.

"relevant market" means the market which may be determined by the Commission with reference to the relevant product market or the relevant geographic market or with reference to both the markets;

"relevant geographic market" means a market comprising the area in which the conditions of competition for supply of goods or provision of services or demand of goods or services are distinctly homogenous and can be distinguished from the conditions prevailing in the neighbouring areas;

"**relevant product market"** means a market comprising all those products or services which are regarded as interchangeable or substitutable by the consumer, by reason of characteristics of the products or services, their prices and intended use;

Dominance as such is not bad

Dominance of market as such is not bad under Competition Act, but its’ abuse is prohibited under the Act.

The Act gives an exhaustive list of practices that constitute abuse of dominant position and, therefore, are prohibited. Such practices shall constitute abuse only when adopted by an enterprise enjoying dominant position in the relevant market in India.

When Dominance gets abused?

Abuse of dominance is judged in terms of the specified types of acts committed by a dominant enterprise alone or in concert. Such acts are prohibited under the law. Section 4 (2) of the Act specifies the following practices by a dominant enterprises or group of enterprises as abuse of dominant position:

- directly or indirectly imposing unfair or discriminatory condition in purchase or sale of goods or service;
- directly or indirectly imposing unfair or discriminatory price in purchase or sale (including predatory price) of goods or service;
- limiting or restricting production of goods or provision of services or market;
- limiting or restricting technical or scientific development to the prejudice of consumers;
- denying market access in any manner;
- making conclusion of contracts subject to acceptance by other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts;
- Using its dominant position in one relevant market to enter into, or protect, other relevant market.

The Commission shall, while inquiring whether an enterprise enjoys a dominant position or not under section 4, have due regard to all or any of the following factors, namely:—

(a) market share of the enterprise;

(b) size and resources of the enterprise;

(c) size and importance of the competitors;

(d) economic power of the enterprise including commercial advantages over competitors;

(e) vertical integration of the enterprises or sale or service network of such enterprises;

(f) dependence of consumers on the enterprise;

(g) monopoly or dominant position whether acquired as a result of any statute or by virtue of being a Government company or a public sector undertaking or otherwise;

(h) entry barriers including barriers such as regulatory barriers, financial risk, high capital cost of entry, marketing entry barriers, technical entry barriers, economies of scale, high cost of substitutable goods or service for consumers;

(i) countervailing buying power;

(j) market structure and size of market;

(k) social obligations and social costs;

(l) relative advantage, by way of the contribution to the economic development, by the enterprise enjoying a dominant position having or likely to have an appreciable adverse effect on competition;

(m) Any other factor which the Commission may consider relevant for the inquiry.

A Case Study - Intel

The European Commission imposed a fine of €1.06 Billion on Intel Corporation for violating EC Treaty antitrust rules on the abuse of a dominant market position by engaging in anti-competitive practices and for excluding competitors from the market for computer chips called x86 central processing units (CPUs).

Facts of the case

Throughout the period October 2002-December 2007, Intel had a dominant position in the worldwide x86 CPU market (at least 70% market share).

The Commission found that Intel engaged in two specific forms of illegal practice.

- First, Intel gave wholly or partially hidden rebates to computer manufacturers on condition that they bought all, or almost all, their x86 CPUs from Intel. Intel also made direct payments to a major retailer on condition to stock only computers with Intel x86 CPUs. Such rebates and payments effectively prevented customers - and ultimately consumers - from choosing alternative products.

- Second, Intel made direct payments to computer manufacturers to halt or delay the launch of specific products containing competitors' x86 CPUs and to limit the sales channels available to these products.

The Commission found that these practices constituted abuse by Intel of its' dominant position on the x86 CPU market that harmed consumers throughout the European Economic Area. By undermining its competitors' ability to compete on the merits of their products, Intel's actions undermined competition and innovation.

The Commission has also ordered Intel to cease ongoing abusive practices immediately.

A brief Analysis of Intel case under Competition Act, 2002

- In the above mentioned case the relevant market is 'Relevant Product Market", and to be more specific, 'Computer Chip Market'

- The dominance is abused on the grounds of 'Denial of Market Access' which is listed as one of the grounds of abuse of dominance, under Section 4(2)(c) of Competition Act, 2002

A Case Study - DLF

Facts:

DLF launched a Group Housing Complex (The Belaire) in Gurgaon, planned to construct 5 multistoried residential buildings. The informant filed an instant case under Section 19(1) (a) of the Competition Act, 2002 and alleged that DLF, by abusing its dominant position, imposed highly arbitrary, unfair and unreasonable conditions on the informant through its agreements. As a matter of fact, the rights of the informant in this agreement were affected by the DLF.

The Informant further, alleged that the various clauses of the house agreement had imposed unilateral and one sided clauses and the action of DLF pursuant thereto was prima facie unfair and discriminatory, thus attracting the provisions of Section 4 (2) (a) of the Act.

The CCI asked Director General (DG) to investigate the allegations on DLF, as a dominant player in market and whether there exist a relevant market. The DG's investigation report observed that allegations made by the informant were true and the Act was applicable in this respective case. It was observed that DLF in exercise of its market power and dominance violated the Section 19 (4) and also has imposed unfair conditions of sale to consumers, which violated Section 4(2) (a) (i) of the Act.

Held:

CCI held that DLF has contravened the Section 4 (2) (a) (i) and (ii), directly and indirectly, imposing unfair or discriminatory conditions in the sale of services. CCI found DLF guilty of abusing its dominant position in the market and imposed a penalty of Rs. 630 crores on DLF. The CCI further directed DLF to cease and desist from formulating and imposing such unfair conditions in its Agreement with buyers in Gurgaon and to suitably modify unfair conditions imposed on its buyers as referred to above, within 3 months of the date of receipt of the order on DLF.

DLF challenged the CCI order before COMPAT which granted stay order against the CCI order of imposing penalty under section 27 (b) of the Act subject to DLF furnishing an undertaking to pay 9% interest on the amount of penalty to be determined by COMPAT for the period from the date of order by CCI till the date of payment by DLF. Further, COMPAT ordered that the directions of CCI for modifications of terms of the Agreement shall remain in abeyance. However, the direction of CCI to "cease and desist" with the implementation of the Agreement was not stayed.

Regulation of Combinations (Section 5)

Combination under Competition Act, 2002

Combination means acquisition of control, shares, voting rights or assets, acquisition of control by a person over an enterprise where such person has control over another enterprise engaged in competing businesses, and mergers and amalgamations between or amongst enterprises when the combining parties exceed the thresholds set in the Act. The thresholds are unambiguously specified in the Act in terms of assets or turnover in India and abroad. Entering into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India is prohibited and such combination would be void.

Sections 5 and 6 of the Competition Act, 2002 came into force with effect from 1 June 2011

Combinations – Thresholds

The current thresholds for the combined assets/turnover of the combining parties are as follows:

- **Individuals:** Either the combined assets of the enterprises are more than `2,000 crore in India or the combined turnover of the enterprise is more than `6,000 crore in India. In case either or both of the enterprises have assets/turnover outside India also, then the combined assets of the enterprises are more than US $ 1 billion, including at least `1000 crore in India, or turnover is more than US$ 3 billion, including at least `3,000 crore in India.
- **Group:** The group to which the enterprise whose control, shares assets or voting rights are being acquired would belong after the acquisition or the group to which the enterprise remaining the merger or amalgamation would belong has either than `8,000 crore in India or turnover more than `24,000 crore in India. Where the group has presence in India as well as outside India then the group has assets more than US $ 4 billion including at least `1,000 crore in India or turnover more than US$ 12 billion including at least `3,000 crore in India.
- In term Group has been explained in the Act. Two enterprises belong to a "Group" if one is in position to exercise at least 26 percent voting rights or appoint at least 50 per cent of the directors or controls the management or affairs in the other. Vide notification S.O. 481 (E) dated 4 March, 2011, Government has exempted "Group" exercising less than fifty per cent of voting rights in other enterprise from the provisions of section 5 of the Act for a period of five years.
- The above thresholds are presented in the form of a table below:

<table>
<tr><td rowspan="3">In India</td><th>Applicable to</th><th colspan="2">Assets</th><th colspan="2">Turnover</th></tr>
<tr><th>Individual</th><td colspan="2">`2,000 Cr.</td><td>`6,000 Cr.</td><td></td></tr>
<tr><th>Group</th><td colspan="2">` 8,000 Cr.</td><td>`24,000 Cr.</td><td></td></tr>
<tr><td rowspan="4">In India an outside</td><th rowspan="2">Applicable to</th><th colspan="2">Assets</th><th colspan="2">Turnover</th></tr>
<tr><td>Total</td><td>Minimum Indian Component</td><td>Total</td><td>Minimum Indian Component out of Total</td></tr>
<tr><th>Individual parties</th><td>$ 1 bn.</td><td>RS 1,000 cr.</td><td>$ 3 bn.</td><td>Rs 3,000 cr.</td></tr>
<tr><th>Group</th><td>$ 4 bn.</td><td>Rs 1,000 cr.</td><td>$ 12 bn.</td><td>Rs 3,000 cr.</td></tr>
</table>

1,000 Crore = 1 billion

The turnover shall be determined by taking into account the values of sale of goods or services. The value of assets shall be determined by taking the book value of the assets as shown in the audited books of account of the enterprise, in the financial year immediately preceding the financial year in which the date of proposed combination falls, as reduced by any depreciation. The value of assets shall also include the brand value, value of goodwill, or intellectual Property Rights etc. referred to in explanation (c) to section 5 of the Act.

Regulation of combinations

Section 6 of the Competition Act, 2002 prohibits any person or enterprise from entering into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and if such a combination is formed, it shall be void.

However, 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—

(a) approval of the proposal relating to merger or amalgamation, referred to in clause (c) of section 5, by the **board of directors** of the enterprises concerned with such merger or amalgamation, as the case may be;

(b) execution of any agreement or other document for acquisition referred to in clause (a) of section 5 or acquiring of control referred to in clause (b) of that section.

As per Regulation 5, sub-regulation 7 of Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011, Board of Directors shall mean and include

(a) the individual himself or herself including a sole proprietor of a proprietorship firm;

(b) the karta in case of a Hindu Undivided Family (HUF);

(c) the board of directors in case of a company registered under the Companies Act, 1956;

(d) in case of a corporation established by or under any Central, State or Provincial Act or a Government company as defined in section 617 of the Companies Act, 1956 or an association of persons or a body of individuals, whether incorporated or not, in India or outside India or anybody corporate incorporated by or under the laws of a country outside India or a cooperative society registered under any law relating to cooperative societies or a local authority, the person or the body so empowered by the legal instrument that created the said bodies;

(e) in the case of a firm, the partner(s) so authorized;

(f) in the case of any other artificial juridical person not falling within any of the preceding sub- clauses, by that person or by some other person competent to act on his behalf.

COMPETITION COMMISSION OF INDIA (PROCEDURE IN REGARD TO THE TRANSACTION OF BUSINESS RELATING TO COMBINATIONS) AMENDMENT REGULATIONS, 2016

Form of notice for the proposed combination.-

Enterprise to give notice

Any enterprise which proposes to enter into a combination shall give notice of such combination to the Commission in accordance with sub-section (2) of section 6 of the Act and these regulations.

Notice to be given in Form I

The notice under sub-section(2) of section 6 of the Act, shall ordinarily be filed in Form I as specified in schedule II to these regulations, duly filled in and accompanied by evidence of payment of requisite fee by the parties to the combination.

COMBINATIONS IN RESPECT OF WHICH NOTICE NEED TO BE NORMALLY FILED IN FORM II

(a) the parties to the combination are engaged in production, supply, distribution, storage, sale or trade of similar or identical or substitutable goods or provision of similar or identical or substitutable services and the combined market share of the parties to the combination after such combination is more than fifteen percent (15%) in the relevant market;

(b) the parties to the combination are engaged at different stages or levels of the production chain in different markets, in respect of production, supply, distribution, storage, sale or trade in goods or provision of services, and their individual or combined market share is more than twenty five percent (25%) in the relevant market.

The parties to the combination shall give notice in Form I or Form II, as the case may be, in accordance with the notes to Form I and Form II issued by the Commission and published on its official website, from time to time.

DUE DILIGENCE OF COMPETITION LAW ASPECTS

Due diligence on competition law aspects is an examination of the actual operations and practices of an enterprise to determine the extent of its compliance with the competition law and to identify potential risks and liabilities, and assess the adherence to and effectiveness of the company's competition law compliance policy and training program.

Primary components of Competition Law due diligence are:

- An examination of selected company documents.
- Interviews with selected company personnel.
- Identify specific business activities that potentially could create antitrust exposure for the company.
- The results of the due diligence may suggest an enterprise to have an effective competition law compliance programme.
- The results of the due diligence may result in variation of deal value, withdrawal of deal and also make suggestions to structure a compliance program.

How to go about the process of due diligence of competition law?

Due diligence of competition law may be made under the following heads:

(a) Due diligence of various agreements (both existing and proposed)

(b) Due diligence on dominance and its likely abuse if any,(existing)

(c) Due diligence on combinations (i.e. effect of proposed mergers & Acquisition)

(d) Competition law compliance programme of an enterprise

Due Diligence of various agreements include

- agreements relating to production, supply and distribution of goods or services.
- agreement if any with competitor relating to production, marketing or bidding, price etc.
- agreements with customers and distributors.
- purchase agreements.

- non-compete covenants.
- technology transfer/technical know-how agreements.
- Concession agreements

Due diligence on abuse of dominance if any includes

- Examination as to the existence of dominance
- Examination of relevant market, whether product or geographical
- Cases of abuse if any.

Due diligence on regulation of combinations

The following aspects are to be analysed during due diligence process:

- What is the nature of combination? Whether it is acquisition of share, voting rights, assets or control or merger/amalgamation etc?
- Examination of total value of Assets or Turnover and the valuation methodology.
- Status of merger notification to be filed with CCI
- Status of dominance after merger.

DUE DILIGENCE CHECKLIST FOR COMPLIANCE WITH COMPETITION ACT, 2002

I CHECKLIST FOR ANTI COMPETITIVE AGREEMENTS

Section 3 of the Competition Act, 2002 dealing with anti-competitive agreements prohibits such agreements or practices, or decision taken which causes or is likely to cause an appreciable adverse effect on competition within India.

An enterprise might enter into horizontal[1] or vertical[2] agreements during the ordinary course of business. However, when agreements are entered to prevent the competition, such agreements are not in accordance with the principles of fair play in the market, hence anti-competitive.

In this context, it is important to note that the term Agreement[3] would include any arrangement or understanding or action in concert whether or not it is formal or in writing; or it is intended to be enforceable by legal proceedings. This definition is an inclusive one and covers not only an agreement as understood in the conventional sense under the Indian Contract Act, but any arrangement or understanding or action in concert. In other words, the form of agreement is of no importance. Not only written agreements are deemed to come within the scope of competition law but also verbal agreements or so-called co-ordinated policies, i.e. deliberate and intended collaboration between individual companies for the purpose of eliminating or restricting competition in a certain market.

Following general checklist may be followed while carrying out assessment of agreements including

1 Horizontal agreements mean agreements between companies acting on the same marketing stage, e.g. agreements with competing manufacturers.

2 Vertical agreements mean agreements between companies acting on different marketing stages, e.g. agreements with distributors and customers, licensees, suppliers or licensors.

3 Section 2 (b) of The Competition Act, 2002

horizontal and vertical agreements such as tie-in arrangements, exclusive supply agreement, exclusive distribution agreement, refusal to deal, resale price maintenance from competition law compliance perspective:

1. The company has not jointly determines selling or purchase prices
2. The company has not jointly agreed on rebates, discounts
3. The company has not granted discounts or special deals on a published list price or ruling price
4. The company has not accepted recommendations of a trade association in relation to price
5. The company has not indulged in collective price-fixing or price co-ordination of any product
6. The company has not fixed /exchanged any price related conditions including discussions related to aspects of pricing with competitors
7. The company has not shared information about prices, discounts, profit margins, cost structures, during meetings of a trade association
8. The company has not mutually agreed not to supply certain customers or not to purchase from certain suppliers
9. The company has not agreed with competitors to make the supply or purchase of goods subject to certain mutually agreed conditions.
10. The company has not shared or allocated markets between competitors in respect of specific territories, products, customers or sources of supply.
11. The company has not fixed production/output, buying and selling quotas between competitors.
12. The company has not brought multiple bids to a bid opening and submits its bid only after coming to know as to who else is bidding.
13. The company has not made a statement indicating advance knowledge of the offers of the competitors.
14. The company has not made a statement that a bid is a ‘complementary’, 'token 'or' cover' bid.
15. The company has not made a statement that the bidders have discussed prices and reached an understanding.
16. The company has not given a false impression that the enterprise is a party to any anticompetitive agreement.
17. The company has not discussed among competitors of such matters as need for changes in price levels, prospective production plans, allocation of markets, action aimed at hindering the prospects of competitors, or the like.
18. The company has not agreed in writing or in any other way on prices or pricing policy.
19. The company has not restricted the liberty of competitors to promote and sell products at independently determined prices and conditions.

20. The company has not restricted the possibilities of competitors to use a common quality label.
21. The company has not entered into standardisation agreements with competitors that might make entry for new entrant in the market more difficult.
22. The company has not restricted import or export or the type of customers.
23. In case of exclusive distribution, the company has not restricted passive sales.
24. In case of selective distribution, the company has not restricted sales inside the system.

WHILE DEALING WITH COMPETITORS (HORIZONTAL AGREEMENTS)

25. The company has not agreed to adopt the same price list.
26. The company has not discussed future prices, price changes, or price formulas.
27. The company has not discussed terms and conditions of business.
28. The company has not discussed marketing programmes or allowances.
29. The company has not shared or partition markets or customers.
30. The company has not agreed to limit output or investment.
31. The company has not discussed or agreed about bids/tendering arrangements.
32. The company has not discussed or exchange confidential business information.

WHILE BIDDING IN A TENDER

33. The company has not agreed to submit identical bids.
34. The company has not agreed as to who shall submit the lowest bid, agreements for the submission of cover bids (voluntarily inflated bids).
35. The company has not agreed not to bid against each other.
36. The company has not agreed on common norms to calculate prices or terms of bids.
37. The company has not agreed to squeeze out outside bidders.
38. The company has not agreed on designating bid winners in advance on a rotational basis, or on a geographical or customer allocation basis.
39. The company has not agreed as to the bids which any of the parties may offer at an auction for the sale of goods or any agreement through which any party agrees to abstain from bidding for any auction for the sale of goods or any agreement through which any party agrees to abstain from bidding for any auction for the sale of goods, which eliminates or distorts competition.

WHILE WRITTEN COMMUNICATIONS

40. The company has not used misleading language.
41. The company has not used ambiguous language that may convey suspicious anti- competitive conduct such as “please destroy or delete after reading”, “no copies to be made”, “the main purpose of this transaction/conduct is oust competitor”.

42. The company has not use phrases that suggest that competitors/distributors will follow price rise, stick to agreed price.

43. The company has not used any expressions which are hyperbole and slangs.

II CHECKLIST FOR ABUSE OF DOMINANT POSITION

Competition Act, 2002 does not prohibit the mere possession of dominant position, but only its abuse, thus recognizing that a dominant position may have been achieved through superior economic performance. Once it is determined that an enterprise is in dominant position, then the next question that arises is whether there has been an abuse of dominant position. In particular Section 4(2) states that there shall be an abuse of dominant position if an enterprise indulges in any of the activities listed in the sub-section, these being unfair or discriminatory condition or price including predatory pricing, limiting or restricting production or technical or scientific development, denying market access, imposing supplementary obligations having no connection with the subject of the contract, or using dominance in one market to enter into or protect another relevant market. Thus, the Act provides for five kinds of abuses and the list of abuses is exhaustive, and not merely illustrative.

Following general checklist may be followed while carrying out assessment of abuse of dominant position from competition law compliance perspective:

1. The company has not imposed unfair or discriminatory condition in purchase or sale; or price in purchase or sale of goods or services (including predatory price) of goods or service.

2. The company has not indulged in practice or practices resulting in denial of market access in any manner.

3. The company has not made conclusion of contracts subject to acceptance by other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

4. The company has not used dominant position in one relevant market to enter into, or protect, other relevant market.

5. The company has not discriminated between different customers.

6. The company has not discriminated prices or rebates between similar customers.

7. The company has not abruptly refused to provide services.

8. The company has not provided Discriminatory differential bonus or discount based on quantity.

9. The company has not operated the pricing mechanism in such manner that as and when there is a rise in cost of production, the sale price should be changed proportionately.

10. The company has not discriminated in relation to prices, terms of sale, or the quality or quantity of what is supplied, and may extend to refusal to sell.

11. The company has not discriminated in terms and conditions in the supply or purchase of goods or services, for example, extension of discriminated credit facilities or ancillary services.

12. The company has not imposed discriminatory or unfair conditions to any category of users, or any other enterprise having contractual relationship with the dominant enterprise.

III CHECKLIST FOR REGULATION OF COMBINATIONS

According to the provisions of the Competition Act, 2002, combinations are discouraged, if they reduce or harm competition. Act does not provide for monitoring all kinds of combinations by the CCI, for the reason that very few Indian companies are of international size and that in the light of continuing economic reforms, opening up of trade and foreign investment, a great deal of corporate restructuring is taking place in the country and that there is a need for mergers, amalgamations etc. as part of the growing economic process before India can be on an equal footing to compete with global giants, as long as the mergers are not prejudicial to consumer interest.

It is in this context, the provisions relating to combinations in the Act are fairly liberal, in the sense that the thresholds are relatively high, and if the Commission fails to complete the investigation and pass an order regarding the combination within the prescribed time period, the combination is deemed to have been approved.

The Competition Act, 2002 regulates those combinations which, in certain circumstances, causes or is likely to cause an appreciable adverse effect on competition within relevant market in India and renders such a combination as void.

Following general checklist may be followed while carrying out assessment of combinations from competition law compliance perspective at the earliest of deal/transaction negotiation process:

- Check whether mergers, acquisitions and amalgamations (as the case may be) qualifies as combination under the Act i.e. whether they are within the foot-print of Section 5 thresholds. These thresholds determine whether the proposed combination would qualify as a "combination" and be then covered by the regulatory and operative provisions of Section 6. The current thresholds appearing in Section 5 of the Act are as follows:

Individual: Either the combined assets of the enterprises are more than Rs. 1,500 crores in India or the combined turnover of the enterprise is more than Rs. 4,500 crores in India. In case either or both of the enterprises have assets/ turnover outside India also, then the combined assets of the enterprises are more than US$ 750 millions, including at least 750 crores in India, or turnover is more than US$ 2250 millions, including at least 2,250 crores in India.

Group : The group, to which the enterprise whose control, shares, assets or voting rights are being acquired would belong after the acquisition or the group to which the enterprise remaining the merger or amalgamation would belong has either assets of more than 6000 crores in India or turnover more than Rs. 18000 crores in India. Where the group has presence in India as well as outside India then the group has assets more than US$ 3 billion including at least 750 crores in India or turnover more than US$ 9 billion including at least 2250 crores in India.

Check whether mergers, acquisitions and amalgamations (as the case may be) fall within any special exemptions provided therein, and unless exempted, the proposed transaction will have to be notified to the CCI.

Subject to certain requirements, a "combination" resulting from a transaction involving share subscription, financing facility or acquisition by a Public Financial Institution, Foreign Institutional Investor, Bank or Venture Capital Fund is exempt from scrutiny by the CCI.

EXEMPTION NOTIFICATIONS

- In exercise of the powers conferred by clause (a) of Section 54 of the Act, the Central Government, in public interest, has exempted enterprises being parties to-

  a) any acquisition referred to in clause (a) of section 5 of the Competition Act;

  b) acquiring of control by a person over an enterprise when such person has already direct or indirect control over another enterprise engaged in production, distribution or trading of a similar or identical or substitutable goods or provision of a similar or identical or substitutable service, referred to in clause (b) of section 5 of the Competition Act; and

  c) any merger or amalgamation, referred to in clause (c) of section 5 of the Competition Act,

  where the value of assets being acquired, taken control of, merged or amalgamated is not more than rupees 350 crores in India or turnover of not more than rupees 1000 crores in India, from the provisions of section 5 of the said Act for a period of five years.

  Where a portion of an enterprise or division or business is being acquired, taken control of, merged or amalgamated with another enterprise, the value of assets of the said portion or division or business and or attributable to it, shall be the relevant assets and turnover to be taken into account for the purpose of calculating the thresholds under section 5 of the Act.

  It may be noted that the value of the said portion or division or business shall be determined by taking the book value of the assets as shown, in the audited books of accounts of the enterprise or as per statutory auditor's report where the financial statement have not yet become due to be filed, in the financial year immediately preceding the financial year in which the date of the proposed combination falls, as reduced by any depreciation. The turnover of the said portion or division or business shall be as certified by the statutory auditor on the basis of the last available audited accounts of the company.

- A banking company in respect of which the Central Government has issued a notification under Section 45 of the Banking Regulation Act, 1949, from the application of the provisions of Sections 5 and 6 of the Act for a period of five years.

COMBINATIONS IN RESPECT OF WHICH NOTICE NEED NOT NORMALLY BE FILED

Regulation 4 of the Procedural Regulations clarify that since the categories of combinations mentioned in Schedule I are ordinarily not likely to cause an appreciable adverse effect on competition in India, notice under sub-section(2) of section 6 of the Act need not normally be filed.

- The Combination Regulations provide that notice in respect of certain combinations, specified under Schedule I, need not normally be filed with the Commission as those transactions are ordinarily not likely to cause appreciable adverse effect on competition in India.

SCHEDULE I TO THE COMBINATION REGULATIONS

(1) An acquisition of shares or voting rights, referred to in sub-clause (i) or sub-clause (ii) of clause (a) of section 5 of the Act, solely as an investment or in the ordinary course of business in so far as the total shares or voting rights held by the acquirer directly or indirectly, does not entitle the acquirer to hold twenty five per cent (25%) or more of the total shares or voting rights of the company, of which shares or voting rights are being acquired, directly or indirectly, or in accordance with the execution of any

document including a share holders' agreement or articles of association, not leading to acquisition of control of the enterprise whose shares or voting rights are being acquired.

The acquisition of less than ten per cent of the total shares or voting rights of an enterprise shall be treated as solely as an investment.

Provided that in relation to the said acquisition,-

(a) the Acquirer has ability to exercise only such rights that are exercisable by the ordinary shareholders of the enterprise whose shares or voting rights are being acquired to the extent of their respective shareholding; and

(b) the Acquirer is not a member of the board of directors of the enterprise whose shares or voting rights are being acquired and does not have a right or intention to nominate a director on the board of directors of the enterprise whose shares or voting rights are being acquired and does not intend to participate in the affairs or management of the enterprise whose shares or voting rights are being acquired.

(1A) An acquisition of additional shares or voting rights of an enterprise by the acquirer or its group, where the acquirer or its group, prior to acquisition, already holds twenty five per cent (25%) or more shares or voting rights of the enterprise, but does not hold fifty per cent (50%) or more of the shares or voting rights of the enterprise, either prior to or after such acquisition:

Provided that such acquisition does not result in acquisition of sole or joint control of such enterprise by the acquirer or its group.

(2) An acquisition of shares or voting rights, referred to in sub-clause (i) or sub-clause (ii) of clause (a) of Section 5 of the Act, where the acquirer, prior to acquisition, has fifty percent (50%) or more shares or voting rights in the enterprise whose shares or voting rights are being acquired, except in the cases where the transaction results in transfer from joint control to sole control.

(3) An acquisition of assets, referred to in sub-clause (i) or sub-clause (ii) of clause (a) of Section 5 of the Act, not directly related to the business activity of the party acquiring the asset or made solely as an investment or in the ordinary course of business, not leading to control of the enterprise whose assets are being acquired except where the assets being acquired represent substantial business operations in a particular location or for a particular product or service of the enterprise, of which assets are being acquired, irrespective of whether such assets are organized as a separate legal entity or not.

(4) An amended or renewed tender offer where a notice to the Commission has been filed by the party making the offer, prior to such amendment or renewal of the offer:

Provided that the compliance with regulation 16 relating to intimation of any change is duly made.

(5) An acquisition of stock-in-trade, raw materials, stores and spares, trade receivables and other similar current assets in the ordinary course of business.

(6) An acquisition of shares or voting rights pursuant to a bonus issue or stock splits or consolidation of face value of shares or buy back of shares or subscription to rights issue of shares, not leading to acquisition of control.

(7) Any acquisition of shares or voting rights by a person acting as a securities underwriter or a registered stock broker of a stock exchange on behalf of its clients, in the ordinary course of its business and in the process of underwriting or stock broking, as the case may be.

(8) An acquisition of shares or voting rights or assets, by one person or enterprise, of another person or enterprise within the same group, except in cases where the acquired enterprise is jointly controlled by enterprises that are not part of the same group.

(9) A merger or amalgamation of two enterprises where one of the enterprises has more than fifty per cent (50%) shares or voting rights of the other enterprise, and/or merger or amalgamation of enterprises in which more than fifty per cent (50%) shares or voting rights in each of such enterprises are held by enterprise(s) within the same group:

Provided that the transaction does not result in transfer from joint control to sole control.

(10) A combination referred to in Section 5 of the Act taking place entirely outside India with insignificant local nexus and effect on markets in India.

COMBINATION NOTICE

The review process for combination under the Act involves mandatory pre-combination notification to the Commission. Any person or enterprise proposing to enter into a combination shall give notice to the Commission in the specified form disclosing the details of the proposed combination within 30 days of the approval of the proposal relating to merger or amalgamation by the board of directors or of the execution of any agreement or other document in relation to the acquisition, as the case may be. In case, a notifiable combination is not notified, the Commission has the power to inquire into it within one year of the taking into effect of the combination.

The Commission also has the power to impose a fine which may extend to one per cent of the total turnover or the assets of the combination, whichever is higher, for failure to give notice to the Commission of the combination.

Any combination for which notice has been filed with the Commission would not take effect for a period of 210 days from the date of notification or till the Commission passes an order, whichever is earlier. If the Commission does not pass an order during the said period of 210 days, the combination shall be deemed to have been approved.

ACQUISITION OR FINANCING FACILITY BY PFIs, VCFs Etc .

In case of share subscription or financing facility or any acquisition, inter alia, by a public financial institution, foreign institutional investor, bank or venture capital fund, pursuant to any covenant of a loan agreement or investment agreement, details of such acquisition are required to be filed with the Commission within seven days from the date of acquisition.

PROCEDURE FOR INVESTIGATION OF COMBINATIONS

As per the Combination Regulations, the Commission shall form its prima facie opinion as to whether the combination is likely to cause or has caused appreciable adverse effect on competition within the relevant market in India within 30 days from the receipt of the notice. If the Commission is prima facie of the opinion that a combination has caused or is likely to cause adverse effect on competition in Indian markets, it shall issue a notice to show cause to the parties as to why investigation in respect of such combination should not be conducted. On receipt of the response, if Commission is of the prima facie opinion that the combination has or is likely to have appreciable adverse effect on competition, the Commission shall deal with the notice as per the provisions of the Act.

CHECKLIST – REGULATION OF COMBINATIONS

1. The transaction qualified as a “combination” under Section 5 of the Act, it will have to mandatorily be notified to the CCI, and the transaction has taken effect only after 210 days of such notification or from the date the CCI passes an order approving the proposed “combination”, whichever is earlier.
2. Mandatory notice to the CCI is filed, in case of merger or amalgamation, within 30 working days of approval of the proposal relating to merger or amalgamation by the board of directors of the enterprises concerned.

3. Mandatory notice to the CCI is filed, in case of acquisition or acquiring of control, within 30 days of execution of any agreement or other document. Such ‘other document’ is defined to include any binding document conveying an agreement or decision to acquire control.
4. Notice was given to CCI is in terms of the Procedural Regulations issued by CCI
5. There is no premature pre-closing activity involving sharing of competitively sensitive information or joint marketing, production.
6. If, the transaction involves any substantive competition/antitrust risk, the risk is allocated amongst the parties to the transaction.

Under the provisions of Competition Act, 2002, no documents, are exempt from disclosure. All documents may be subject to production, including agenda, minutes of the meetings, annual reports, statements relating to corporate information made, discussed at various forums. Hence, it is in the interest of the company to ensure that its employees comply with the Competition Act, 2002.

The above checklist is not to be regarded as covering all competition issues that can arise. Rather, they are intended to educate the officer or employee of the enterprise of some of the common situations in which competition issues may arise. It is pertinent to note that failure to comply with Competition Act, 2002 has serious consequences for the enterprise, its officers, and employees.

EVALUATION OF ‘APPRECIABLE ADVERSE EFFECT ON COMPETITION’

The Act envisages appreciable adverse effect on competition in the relevant market in India as the criterion for regulation of combinations.

In order to evaluate appreciable adverse effect on competition, the Act empowers the Commission to evaluate the effect of Combination on the basis of factors mentioned in sub section (4) of Section 20.

Factors to be considered by the Commission while evaluating appreciable adverse effect of Combinations on competition in the relevant market:

(a) actual and potential level of competition through imports in the market;

(b) extent of barriers to entry into the market;

(c) level of concentration in the market ;

(d) degree of countervailing power in the market;

(e) likelihood that the combination would result in the parties to the combination being able to significantly and sustainably increase prices or profit margins;

(f) extent of effective competition likely to sustain in a market;

(g) extent to which substitutes are available or are likely to be available in the market;

(h) market share, in the relevant market, of the persons or enterprise in a combination, individually and as a combination;

(i) likelihood that the combination would result in the removal of a vigorous and effective competitor or competitors in the market;

(j) nature and extent of vertical integration in the market;

(k) possibility of a failing business;

(l) nature and extent of innovation;

(m) relative advantage, by way of the contribution to the economic development, by any combination having or likely to have appreciable adverse effect on competition;

(n) whether the benefits of the combination outweigh the adverse impact of the combination, if any.

APPEALS

Under the relevant provisions of the Act, an appeal to Competition Appellate Tribunal (COMPAT) may be filed within 60 days of receipt of the order /direction/decision of the Commission.

The Commission also has the power to impose a fine which may extend to one per cent of the total turnover or the assets of the combination, whichever is higher, for failure to give notice to the Commission of the combination.

NEED FOR COMPETITION COMPLIANCE PROGRAMME

It goes without saying that prevention is always better than cure. When businesses fail to have a compliance program, or when it is ineffective, they are essentially relying on others to bring that failure to their attention. It is far better when companies discover a breach first and act to rectify the problem, rather than the competition authorities bringing the breach to the company's attention. Given today's rigorous competitive environment, a robust competition compliance programme is an absolute must for enterprises.

As every business is unique, so each company requires different steps to ensure compliance with competition law. These depend on a range of factors, including the size and nature of the business, and the frequency of contact of employees with their competitors. Businesses which are able to significantly affect the market in which they are operating or which have large market shares, may be more vulnerable to allegations of abuse of their strong position in the market. Their agreements may be more likely to have an appreciable adverse effect on competition in the market. Employees or directors of a business who have regular contact with competitors on a business or social basis may run a higher risk of colluding.

A compliance programme therefore provides a formal internal framework for ensuring that businesses, i.e., the management and individual employees, comply with competition law. It may include such elements as training to raise awareness of law, the use of checklists to ensure compliance by individual staff with company policies, recording systems to document any permitted contacts that employees have with competitors and independent reviews of agreements, behavior and staff to monitor ongoing compliance. It can also help identify actual or potential infringements at an early stage, enabling the company to take appropriate remedial action.

When considering whether it is necessary to implement a compliance programme, companies should bear in mind that if they do commit an infringement, the competition authorities may take a lenient view where they can show that they have taken adequate steps to achieve compliance. The larger the business and the greater the risk of infringement, the more likely it is that adequate steps will include the introduction of a compliance programme. As a starting point it is helpful to assess the extent to which competition law will affect the business and the risk of committing an infringement. In case the risk of infringement is high, more elaborate measures may be required to ensure compliance.

Further, if employees understand competition law, they will also be able to recognize when the business is a victim of anti-competitive agreements or conduct, and be better-placed to protect the business' interests by making a reasoned complaint to the Competition Commission.

Compliance programmes have following three main purposes:

(i) they strive to prevent violation of law,

(ii) promote a culture of compliance, and

(iii) encourage good corporate citizenship.

As the consequences of infringement can be serious a compliance programme must be capable of meeting the changing requirements of business and must make efforts as part of the regular evaluation process to ensure that the compliance programme continues to be relevant.

Competition Compliance programme help reduce legal costs in the short run by enabling the enterprise to avoid violation of competition laws, while in the long run, they increase corporate competitiveness by raising the value of an enterprise. The prescription of behavioral standards under the compliance programme not only prevents officers and employees of an enterprise from unconsciously violating the competition laws, but at the same time, relieve the employees of the fear that accompanies breach of such laws. The enterprises also save time and money by securing the following benefits from compliance programme:

- Corporate officers and employees being well aware of the requirements of competition law may maintain legal transparency.
- Corporate officers have advance perception concerning the activity of employees that might violate competition laws.
- Corporate officers and employees can avoid civil and criminal liability resulting from violation of competition laws.

The costs of legal counseling and litigation incurred from investigation and prosecution of acts of violation, as well as penalties, negative publicity, and disruptions in normal corporate operation, can be reduced.

An effective compliance programme equips the enterprise with the capacity to demonstrate due diligence to the competition authorities. This is a benefit that can make the cost and effort in putting in place a compliance program seem the best possible investment by company. This is because the amount of time the corporate professionals, who have encountered regulatory action, have had to devote in dealing with enforcement action, when they could be better focussed on more constructive activities of the company. This is not to ignore the cost involved in employing lawyers or paying fines or damages, and the negative impact on the business brand if found to be in breach of the law. There is evidence to suggest a strong link between effective compliance programme and maintaining the reputation of an enterprise and its brands.

Compliance embodied by a well-managed and adequately resourced corporate governance system, is aimed at a business enabler. In a paper presented at an Australian compliance forum, the author summarises that the importance of a good governance system, a holistic approach to compliance, can not be over emphasised: in an increasingly responsive stakeholder environment managing regulatory risk and being committed to the principles of good governance is vital to overall strategic management.

One of the greatest potential benefits of a vigorous compliance program is the ability to protect the company from being a victim of waste, fraud and abuse. The very same techniques that help prevent a company from harming others, also helps protect the company from being victimised.

Advantages of Competition Compliance Programme

Competition Compliance programme offers various advantages to the companies during its ordinary course of business. Broadly, the advantages of Competition Compliance programme can be classified as under:

Positive Benefits to Business

An effective compliance programme that embeds a culture of compliance throughout the organisation can be a business enhancer offering positive benefits to business. A superior knowledge of the risks faced by the organisation and of the measures in place to guard against those risks can provide a company with a competitive advantage. When employees are aware of their rights and obligations, customer service

improves and the employees become more alert and better able to deal with unlawful conduct that the company may be subjected to. A company can obtain value from good governance and compliance, develop a better culture, sustain itself for long term and maintain its reputation, and may avoid or reduce the negative effects of litigation and regulatory intervention.

Reputation and Goodwill

Companies that contravene the competition law may suffer damage to their reputation, unraveling years of careful marketing and brand development. In the era of information age it is more difficult to escape events that in the past were consigned to fading memories and dusty library shelves. Information on past misconduct by companies can now be retrieved at the stroke of a keyboard.

Mitigation of penalties

In the event, Competition Commission institutes proceedings, the verifiable presence of a compliance programme and culture, and its successful implementation, can be scrutinised by the competition authorities/courts when the quantum of penalty is determined.

LESSON ROUND-UP

- All businesses have a duty to act lawfully, but there are more practical reasons why compliance with competition law is particularly important. On a broad level, the main aim of competition law is to ensure that markets remain competitive.
- The Competition Act, 2002 was passed to encourage competition in markets in India.
- The Competition Act broadly covers anti-competitive agreements, abuse of dominance and regulation of combinations.
- During combinations, i.e. mergers or takeovers, the businesses of the transferor and transferee are to be studies from the point of view of anti-trust aspects (i.e. Competition aspects). This process is competition law due diligence.
- Competition law due diligence involves examination of various agreements, check into the companies dominace and its' abuse if any, checking combination thresholds, implementing competition compliance programme help reduce legal costs in the short run by enabling the enterprise to avoid violation of competition laws, while in the long run, they increase corporate competitiveness by raising the value of an enterprise.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation)

1. Write briefly about the preamble of Competition Act, 2002.
2. What are the combination thresholds for domestic takeovers?
3. Write short notes on
   (i) Anti competitive agreement
   (ii) Relevant market
   (iii) Abuse of dominance.
4. Why do we need to carry out competition law due diligence during strategic decisions?