

# Competition Regulations and Governance with the Legal Perspective

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**Abstract:** This paper presents an overview on competition regulations and governance with the legal perspective.

**Keywords:** Competition regulations, Governance

## 1. Introduction

Discourse on Corporate Governance in India is stressed towards the relationship between the management of the company and its shareholders. Important external factors, which significantly affect the corporate governance, are rarely emphasized. The most significant external factor is the 'economic environment' in which the corporation operates. A healthy economic environment fosters a healthy corporate governance culture, whereas a slacking & stagnant economic environment leads to retarded corporate growth.

The economic environment is sought to be infused with constant incentives for corporations, so as to sustain robust economic activity. This infusion is achieved through perfect competition in the market. However, perfect combination is a utopian dream, it has been rightly regarded that, perfect competition is as much a mirage as a perfect spouse. Therefore, conscious efforts are to be made to achieve competitiveness in the market which is as near as perfect competition. Regulatory bodies such as the Competition Commission of India, Securities Exchange Board of India, etc. undertake these conscious efforts.

The scope of this paper is circumscribed around the regulatory functions of the Competition Commission of India. Compliance to the regulatory requirements of the Commission ensures competitiveness in the market as far as combinations such as mergers and acquisitions are concerned. Consequently, it ensures the objective of sustained healthy economic activity and protects the symbiotic relationship between healthy economic environment and good corporate governance.

Through the analysis of recent cases & legal issues regarding the competition regulations, the authors trace the relationship between competition regulation and corporate governance, thereon endorsing their views pertaining to future course of action.

## 2. The concept of corporate governance

The corporate form has existed for centuries, East India Company, the first historically regarded Multi-National

Corporation for example, was chartered by the queen in 1600. One might imagine, given this long history, that the issue of how corporations should be governed would have been settled. Yet, for nearly as long as corporations have existed, there have been complaints about corporate governance and agitation to improve it. It is often believed that Corporate Governance is a relationship between the management of a corporation and its shareholders. This is however a very myopic understanding of the concept of corporate governance.

It ignores the whole gamut of external factors which influence the direction and control of business corporations. Understanding of corporate governance as a mere intra-firm concept would be a fallacious approach. It is imperative to consider external factors, particularly the economic environment in which the corporation functions.

"Corporate Governance' has been defined in many ways, securities and Exchange Board of India, in its Narayan Murthy Committee on Corporate governance observed that, "Corporate Governance is the acceptance by management of the inalienable rights of shareholders as the true owners of the corporation and of their own role as trustees on behalf of the shareholders. It is about commitment to values, about ethical business conduct and about making a distinction between personal and corporate funds in the management of a company. International bodies, such as Organization for Economic Cooperation & Development (OECD) defines Corporate Governance as Company. "The system by which business corporations are directed and controlled.

However, in a broader perspective, corporate governance is defined as "The application of best Management practices, compliance of law in true letter and spirit and adherence to ethical standards for effective Management and distribution of wealth and discharge of social responsibility for sustainable development of all stakeholders".

In the modern scenario Corporate Governance needs to be understood in its broader perspective. Majority of the attention under the study of corporate governance is focused on the firms and the regulations that protect shareholder rights and govern the conduct of managers and directors.

However, attention needs to be also given to the environment in which business is conducted, including the degree of competition among firms, entry and exit rules, and the openness of the economy. This type of business environment has a major

impact on firms' incentives to seek out and implement competitive practices and strategies. The narrative of corporate culture needs to be shifted. It cannot be merely considered under the domain of intra-firm practices. Rather, corporate governance needs to be gauged under the lens of the external factors which are affecting and influencing it.

### 3. Relationship between corporate governance and competition regulation

Corporate governance is directly related to the competitive environment, since corporate governance practices do not change unless the Competitive environment in the country is strengthened. One of the most important factors of good management and corporate governance is competition. Competition encourages technological innovation, managerial efficiency and sows the seeds for new development in the economy. Where competition is intense and global in scope, more firms realize that corporate governance makes good business sense. The disclosures and compliance to all regulatory requirements are positively taken by all stakeholders. By applying good governance, a firm can earn a good reputation and efficient access to finance, which in turn enhances their ability to compete. In effect, good governance becomes an instrument of Competitive strategies.

Where Competition is inadequate or sub-optimal, Corporate Governance tends to become loose or slack, with decision making being delayed or postponed. Quite clearly, Competition policies and corporate governance share a symbiotic relationship amongst themselves. Without effective competition, it is not possible to build a culture of good corporate governance. restricted competition generally lack the incentives to use financial and operational resources efficiently. Sound competition policy helps firms focus on efficiency, reduces price distortions, lowers risk of misguided investments, promotes greater accountability and transparency business decisions and promotes better corporate governance.

Presently corporate governance in India suffers from weak culture of competition & inadequate business awareness about competition compliance effects. Competition, the process of rivalry between business enterprises for customers, is a fundamental characteristic of a flexible and dynamic market economy. By responding to the demand for goods and services at lower prices and improved quality, competing businesses are spurred to innovate and reduce costs.

The 'process of competition' needs to be consciously developed and moulded according to the dynamic economic environment. This exercise would sustain the health of economic environment, and result in accrual of various benefits. Competition Act's primary motive, like that of other anti-trust legislations across the globe, is to sustain the competition process." Competition Commission of India (CCI) ensures that the competition process is sustained through its various activates. Although, CCI prohibits Anti-competitive agreements and Abuse of Dominance" these prohibitions are

not regulatory in nature. These provisions are attracted when an instance of their violation is alleged. Since they aren't regulatory, they do not affect the corporate governance aspect to a very significant degree. It is the Combination Regulations which are truly regulatory in nature and mandates compliance by the corporations. It is under these provisions, that the Commission maintains a continuous parallel relationship with the corporation. These provisions are not attracted only when there is a violation, but mandates prescribed notifications by the corporations whilst they are transacting their business relating to combinations such as takeover of control, mergers or acquisitions.

### 4. Competition Regulations: The legal perspective

Some sections of economic jurisprudential thought consider that law is always an impediment to growth. However, we disagree with this proposition. It needs to be understood that rules and regulations are for the better and efficient working of the economic market, instead than of being an impediment to the growth of an enterprise.

The corporation might incur short term costs to imbibe a corporate governance structure. Nevertheless, in the long run it leads to accrual of benefits to the compliance program in its corporation, as it continues to function in a competitive environment.

The Combination regulations were enacted to regulate mergers and acquisitions which affects the market economy and creates appreciable adverse effect on competition. The regulations underwent changes in 2008, 2009 and 2011 and took final shape only in 2013. The Commission has been mindful of the concerns raised by various stakeholders, both national and international, and incorporated suggestions proposed by them as a response to a draft version of the Combination Regulations".

Combination is defined as acquisition of control, shares, voting rights or assets of one or more enterprise by one or more person or the acquisition of control by a person over an enterprise where such person has direct or indirect control over another enterprise engaged in competing business." Further, competition act makes any combination void which causes or is likely to cause an appreciable adverse effect on competition within India. It requires every acquirer to notify the CCI of the combination and seek its approval prior to effectuating the same. The combination regulation came into effect from June 1, 2011 along with provision 5 and 6 of the competition act.

In addition to this, the act provides that 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 the execution of any agreement or other document in relation to the acquisition.

No combination shall come into effect for a period of 210 days from the date it notifies the commission or till the

commission passes the order. If the commission does not pass the order within it the combination shall be deemed to be approved.<sup>20</sup> Once the notice is received it should be dealt in accordance with Section 29, 30, 31. Section 20(4) of the Competition Act, 2002 provides the substantive test whether the combination has or is likely to have appreciable adverse effect on combination<sup>||</sup> in the relevant market in India. The substantive test encompasses examination of the factors provided in the said Section. The section provides an expansive list of 14 factors which the Commission could undertake while inquiring into combinations.

Penalty for Contravention of Orders of Commission is enshrined under Section 42, if any person, without reasonable clause, fails to comply with the orders or directions of the Commission issued under sections 27, 28, 31, 32, 33, 42A and 43A of the Act, he shall be punishable with fine which may extend to Rs. 1,00,000/- per day, during which such non-compliance occurs, subject to a maximum of Rs. 10,03,00,000/- (Rs. Ten Crores), as the Commission may determine, or in case if such person fails to pay fine imposed above, or fails to comply the direction, then there is a provision of imprisonment up to three years or fine up to Rs. 25,00,00,000/- (Rupees twenty-five crore), or with both, as the Chief Metropolitan Magistrate, Delhi may deem fit.

Section 43A empowers the commission to impose penalty for non-furnishing of information on combinations. This section provides that if any person or enterprise has failed to give notice to the Commission u/s 6(2) of the Act then such person or enterprise is liable to pay penalty imposed by the Commission subject to a maximum of 1% of total turnover or assets, whichever is higher of a combination. Without prejudicing the provisions of the Act, the CCI may admit belated notice but subject to penalty under Section 43A of the Act, when under regulation 5(2), 5(3) a notice is filed in Form I and II and received by the commission beyond time limit of 30 days in Section 6(2).

Regulation 28(6) provides that the CCI shall endeavour to make its final determination on the combination notice within 180 days of filing of details of combination in Form I or Form II. Regulation 19(1) of the Combination Regulation also provides that the Commission shall form its prima facie opinion for the purpose of Section 29(1) of the Act.

Stopping of clock provisions are imbibed under Regulation 5 and Regulation 19, which provide that the time taken by the parties providing information on direction of CCI is excluded from the relevant review period. These cases will be removing defects in notice, or Furnishing additional information by the parties.

### 5. Competition compliance and Corporate governance

Competition Compliance involves the active efforts on the part of an enterprise to comply with the provisions of the Act. When the enterprise takes certain necessary and concrete steps to ensure that knowingly or unknowingly it does not infringe

the provisions of the Act, it can be stated to maintain a Competition Compliance Programme" (CCP).

At the level of the enterprises, compliance with competition law is akin to good corporate governance. Corporate governance, as normally understood, is ethical conduct within the internal environment of the company. Similarly, compliance with competition law is akin to ethical conduct in the external environment of the company, principally in the market place." Competition Compliance Programme (CCP) is a multipronged tool to ensure compliance with Competition law and rapid detection in case of any unintended violation. It works on the principle that 'prevention is better than cure'.

An effective CCP is also a proof of the bona fide of the entity. It shows that the entity is genuinely concerned about complying with the Competition law and any violation was unintentional and without any mala fide. Moreover, global experience shows that Competition authorities show leniency towards entities which have a CCP. It is developed keeping in mind the specific requirements of an enterprise.

The compliances of combination under the Competition Commission Act 2002 has been enshrined in Section 5, 6, 20, 29, 30 and 31. Non-compliance of Section 6(2) will lead to penalty imposition in Section 43A and penalty for making false statement under Section 44. The Act contains structured and deterrent provision which are expected to deter corporate entities, their boards and key executives, if found, to have contravened and violated the Act and disrespected the orders of Commission.

Compliance is wholly under the domain of the functioning of the managerial staff of a corporation. Once the shareholders and investors take the important decisions regarding mergers and acquisitions, it is the job of the management to execute the same in compliance with the regulatory provisions of law.

### 6. Recent case studies on regulatory compliance

Effective competition is the prerequisite to build a culture of good corporate governance. Firms under restricted competition generally lack the incentives to use financial and operational resources efficiently. Sound competition policy helps firms focus on efficiency, reduces price distortions, lowers risk of investments, promotes greater accountability and transparency in business decisions and promotes better corporate governance. CCI needs to play a pivotal role in promoting good corporate governance practices. The recent competition compliance programs, along with its orders on regulatory legal issues have been encouraging, perusal of the same has been done in the subsequent case studies and analysis;

### 7. Instances of Compliance

#### A. Case Study 1

Acquisition of "Mahindra Group Companies" by "CIE Group Companies"

*Factual Matrix:* CCI received a notice on 12th July 2013 under

section 6(2) of the Competition Act, 2002 by CIE and M&M in terms of Regulation 14 of Competition Commission of India (Procedure in regard to 4 transaction of business relating to combinations) Regulations, 2011. The transaction involved multiple agreement and stages but the execution triggers that is pre-merger notification requirement under Section 6(2) was executed within 30 days on July 15th, 2013.

CCI examined the combination in the light of the criteria under Section 20(4) and made the following observations; CIE had no presence or investment in India, and was not engaged in any activity that was competed with or vertically related to the business proposed to be acquired by combination, the proposed combination is not between two existing players in the market, post combination M&M would still hold 20% of the equity in Mahindra CIE and technologies used by Mahindra would continue to be used by Mahindra-CIE post combination.

#### *Order of CCI*

The CCI accordingly held that the proposed combination will not make any appreciable adverse effect on Competition in the relevant market in India and approved the combination under Section 31(1) of the Act.

*Remarks:* In the above case, as the notice of the merger was given within 30 days required under Section 6(2). The pre-merger notification is the compliance which needs to be met for a valid combination. If the compliances were not met it would lead to violation of Section 6(2) and imposition of penalty under Section 43A. Compliances or regulations are the driving force of Corporate Governance which will further lead to better economy, environment of fair competition.

#### *B. Case Study 2*

Acquisition of "Sterling Holiday Resorts(India)Limited" by "Thomas Cook(India) Limited" CCI received a notice on 14th February 2014 under section 6(2) the Competition Act, 2002 by the acquirers in terms of regulation 14 the Competition Commission of India (Procedure in regard to saction of business relating to combinations) Regulations, 2011 ide letter dated 20th February, 2014. The notice u/s 6(2) of the Act was given to the Commission in respect of the composite scheme of arrangement and amalgamation.

#### *Order of CCI*

In the proposed combination the Parties are not engaged in similar business. The business of acquirer offering holiday package and travel services and the business of acquired party providing resort and hotel services, there are no vertical arrangements between the Parties. Therefore, the proposed combination is not likely to raise any competition concern. The CCI accordingly held that the proposed combination will not make any appreciable adverse effect on Competition and approved the combination under Section 31(1) of the Act. This approval, however, shall have no bearing on the proceedings relating to Section 43A of the Act.

*Remarks:* This is an instance of partial compliance. The

parties in this case combined and although the combination will not have adverse effect in India, the companies can still be penalized under Section 43A for not notifying their combination in time. This case gives a blatant example of corporate mis governance, the parties have done everything under the boundaries of law, however due to managerial inefficiency they delayed the filing of the notification.

#### *C. Instances of Non-Compliance*

##### *Case Study 3*

Acquisition of "DBS Group holding Limited" by "Temasek holding Private Limited"<sup>3</sup>

*Factual matrix:* Order u/s 43A of the Competition Act, 2002 in the matter of notice u/s 6(2) of the Competition Act, 2002. CCI received a notice on 6th June 2013 under section 6(2) of the Competition Act, 2002 by the acquirers. It was delayed by 399 days.

Commission issued a show cause notice dated 20th June, 2013. under Section 43A of the Act and Regulation 48 of the General Regulations, to the Acquirers to show cause, in writing, within 15 days of the receipt of the notice, as to why penalty in terms of Section 43A of the Act should not be imposed on them for not having filed the notice within the time prescribed in sub-section (2) of Section 6 of the Act. They defended by stating being misled by the advocate about the legal advice.

#### *Order of CCI*

CCI observed that no urgency was showed by the acquirer after being notified delay was of 5 months etc. However, considering the response of the Acquirers to the show cause notice, submission made by their legal counsel and the step taken by the subsidiary to file a notice of condone delay the proposed combination was pursuant to an acquisition of the shareholding of one foreign enterprise by another foreign enterprise, the Commission considers it appropriate to impose a penalty of INR 50,00,000/- (INR Fifty Lakhs only) on the Acquirers pay the penalty within sixty (60) days from the date of receipt of this order.

*Remarks:* In this case CCI penalized the non-compliance by the corporation, according to the reply of the parties, they were not informed by their legal counsel, whatever may be the reason, this was another example wherein the prospect of the company, and shareholders/investors' money was wasted due to inefficient corporate administration.

## **8. Conclusion**

In 2010, India's ranking in the slid from third to seventh in 34 This was a call to all the stakeholders involved in fostering Asia. Corporate governance culture to take effective action. In the follow up analysis by the same body in the year 2012, India improved its score by 3 percentage points, however its rank remained the same. Significant changes have been brought about in the legal sphere of industrial policy of India since that time.

It is clear from the aforementioned legal trends and case studies that corporate governance exists at a complex intersection of law, morality, and economic efficiency, it is a continuous process influenced by the corporate culture of a country.

Legislative intent to foster a culture of Corporate Governance is reflected in The Companies Act, 2013. However, the companies act cannot work in a vacuum, and it needs to be harmoniously assisted by regulatory bodies, such as the CCI. In its future course of action CCI should consider this broad goal

and appreciate the exigencies of our time, whilst fulfilling its role as an essential partner in facilitating corporate governance and sustaining a strong competitive economic environment. It needs to act as a catalyst. and facilitate corporate governance.

### **References**

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