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CCI's Sun-Ranbaxy master stroke

CCI has balanced the economy's hunger for growth and sound anti-trust policies in its Sun-Ranbaxy merger review

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Sun Pharmaceutical's $4 billion acquisition of rival drug company, Ranbaxy Laboratories, recently became the first transaction to be conditionally approved by the Competition Commission of India (CCI), after a detailed 'Phase II' inquiry. CCI's approval is conditional on the parties divesting some seven brands, within the next six months—before the merger can be consummated to make Sun the largest Indian drug-maker and the world's fifth-largest generic drug company.

CCI's mandate to review transactions, which breach certain statutory asset/turnover thresholds, comes with the concomitant power to block or place conditions on the consummation of transactions which could substantially restrict competition in Indian markets. However, CCI has been reluctant to exercise such powers and has unconditionally approved close to 200 transactions in the first three years of existence of the Indian merger control regime. However, with the recovery of the global and Indian economies and with M&A activity becoming bigger and more complex, CCI seems to be shedding its regulatory inhibitions.

It has already been reported that CCI intends to prescribe structural remedies as a condition for clearing the Holcim-Lafarge merger, which proposes to create the world's biggest cement-maker. CCI had earlier expressed serious reservations about setting of a joint venture of three state-owned oil firms and the Mumbai International Airport Pvt Ltd, for an integrated aviation fuel facility in Mumbai.

As reported by this newspaper ('CCI clears $4-bn Sun Pharmaceutical, Ranbaxy Laboratories merger deal, but adds riders', December 8, goo.gl/N4gU6W), CCI has determined that the proposed Sun-Ranbaxy merger would reduce competition in seven overlapping medicinal formulation markets in India, where Sun-Ranbaxy's combined market share well exceeds the 50% mark and the proposed merger would create a dominant entity, without any significant competitor. CCI has held that until the brands containing such formulations are divested, in a manner which creates a "viable, effective, independent and long-term" competitor in such markets, the Sun-Ranbaxy merger cannot be consummated. CCI has given the merging parties six months to complete the divestiture process and will appoint one of the big four accounting firms to oversee the compliance of its directions.

Given the renewed interest of global businesses in the Indian economy, it would be useful to chronicle certain important takeaways from CCI's approval of the Sun-Ranbaxy merger for domestic and international companies, which may have to notify their proposed transactions under the Indian regime.

The technical maturity of CCI's maiden 'Phase II' investigation, the reasonability of the choice of remedies, the designing of a business-friendly divestiture process and a 56 page non-Delphic order, suggests an alignment of CCI's merger review processes/procedures with those of mature anti-trust jurisdictions. In this regard, CCI's early involvement with the International Competition Network's (ICN) capacity building programmes seems to have borne fruit—helping CCI to create a state-of-the-art merger control regime.

Further, in-spite of the fact that the Sun-Ranbaxy merger deals with the Indian generic drug industry—an industry ripe for public policy politics in India—CCI ensured that the anti-trust scrutiny of the merger did not get influenced by factors irrelevant to competition law. CCI's order asserts that Indian anti-trust norms remain uninfluenced by protectionism, populism, and politics, which should inspire greater confidence among domestic and foreign industry observers.

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The merger was approved by the respective boards of Sun and Ranbaxy back on April 6, 2014 and given that the parties will now have to seek a buyer for the divested brands, who is acceptable to the CCI, the deal could well remain unconsummated till mid 2015. The merger review itself took nearly 7 months, which included several requests for additional information or correction of defects in the merger notification forms.

M&A lawyers should take a rough estimate of the review time-frame for large complex deals and accordingly schedule their transactional milestones, assessing how the length of the review process could potentially affect the commercials of a deal. Parties should start planning for notifying their transactions, early in the deal process, collecting enough market/business data to ensure that the information they provide to CCI is sufficiently comprehensive to maximise the prospect of an expedited clearance. Early identification of issues where CCI could have concerns and prompt information-gathering, could reduce the risk of supplemental information requests delaying the review process.

The review process for the Sun-Ranbaxy merger was further delayed by the fact that it was the first merger where CCI consulted widely with interested parties, including industry peers, customers, public health bodies and other key stakeholders. For big-ticket deals, it will be prudent for the parties to conduct advance discussions with relevant customers and industry associations, briefing them on the efficiencies of the deal and factoring their reservations/comments into the transactional structure. This will increase the prospect of regulatory consultation with such stakeholders, proceeding promptly and smoothly. To that extent, if practical, it could be useful to try and obtain statements from such stakeholder groups supporting the deal to include in the merger notifications to the CCI.

Given that CCI has not published official 'merger guidelines', transactional parties would have to pick up signs from CCI's decisional practice, like those of the Sun-Ranbaxy order, to factor Indian anti-trust policy into their M&A strategies. One such sign is CCI's overt emphasis on 'market shares' of the merging parties to assess a merger's competitive effects on Indian markets. Both in Sun-Ranbaxy and the Jet-Etihad approval orders, CCI choose a market-share based anti-trust analysis, giving inferior attention to factors like 'entry barriers'. Legal commentators have already alleged that given the absence of any IP roadblocks and the ease of entry into the generic markets, CCI's fears that the Sun-Ranbaxy merger would create a dominant entity in the seven identified formulation markets, is exaggerated. Nevertheless, it would be prudent for M&A lawyers, while structuring future mergers, to identify products or sectors where the merging parties have large market shares and factor possible anti-trust roadblocks into the commercials of the merger itself.

Sun and Ranbaxy has been lucky that the brands identified by CCI for divestment account for less than 1% of sales of both the companies, and will have negligible effect on valuation. However, in other cases, CCI may ask for divestment of products which make meaningful contribution to the company's revenues and M&A lawyers should factor such contingencies, into the transaction documents to avoid potential deal-breakers. In such situations, it could be worth exploring if certain behavioural remedies can be offered to offset any structural modifications that could be sought by CCI.

India's finance minister, Arun Jaitley, while inaugurating an ICN merger workshop at New Delhi, recently stated that mergers and acquisitions have to be encouraged to promote the size of Indian companies but there is also a need to understand when to draw the red line while implementing the competition law. As CCI's merger review epoch enters its mature phase, augurs of Indian anti-trust should be happy to observe that in approving the Sun-Ranbaxy merger, CCI seems to have kept Jaitley's advice in mind, balancing the economy's hunger for growth and sound policies countering anti-trust.

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