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Telecom mergers redefined

By **Sugandha Kapur**

Mergers and amalgamations are an important tool for corporate strategy and structuring. On this subject, the division bench of the Delhi High Court ruled (13 July 2012) inter alia, in the case of *Idea Cellular Limited v. Union of India* (Company Appeal Nos. 42 & 67 of 2011) that amalgamation of companies and licenses held by the merging companies are entirely independent and the former need not necessarily lead to the latter.

Facts

On 5th February 2010, the Delhi High Court sanctioned the scheme of amalgamation for Spice Communications Limited ("Spice"), a public listed company providing telecom services in Punjab and Karnataka to merge with Idea Cellular Limited ("Idea"). Idea contended that the Unified Access Service Licenses ("UASL") issued by the Department of Telecom ("DoT") under Section 4 of the Indian Telegraph Act, 1885 to Spice for the service areas of Punjab and Karnataka also stood transferred to it, accordingly, casting an obligation on DoT to merge existing licenses of Spice and Idea. DoT disagreed and stated that its prior approval was required, which was not obtained and hence sought an unwinding of the scheme of amalgamation order.

On 4th July 2011, the Hon'ble Judge modified the earlier order of sanction on grounds of non-disclosure and suppression of material facts by Idea at the time of filing of application for sanction of amalgamation scheme and held that the same amounted to playing a fraud upon the Court[1]. It was held as held that sanction was in contravention of License Condition and Inter Service Area Merger Guidelines, 2008 ("Merger Guidelines") but the recall of the entire order not being feasible, modified the earlier order to state that the licenses and spectrum owned by Spice for Punjab and Karnataka shall not stand transferred to Idea until prior permission of DoT is obtained. Both DoT and Idea, being aggrieved with different parts of the order filed appeals before the division bench of the Delhi High Court and the order passed therein sets out certain important principles governing the rights and limits of the authority of the court and the government in certain cases, as summarized in the following paragraphs.

Key Issues

Merger of a company distinct from merger of licenses

Sections 391-394 of the Companies Act, 1956 (the Act) sets out the procedure and requirements for amalgamation of companies through the courts, whereas terms and conditions of UASL issued to companies are governed by the License Agreement and Merger Guidelines, accordingly, prior approval of DoT is necessary for the same. The court will sanction a scheme that is just, fair, reasonable and beneficial for the class affected by such commercial decisions. If approvals are required under separate statutes for completing the merger, the same needs to be obtained independently and cannot be assumed as automatic pursuant to a sanctioned scheme of amalgamation by a court. Any dispute between the DoT (Government) and a business entity regarding a license would be decided on the basis of the license agreement and the government policy and not by the order of the court sanctioning the merger.

Consequently, sanction of a scheme of amalgamation

[1] The Company Judge held *"non- disclosure of information was not an innocent act and rather it was part of the design to mislead the Court and, therefore, amounted to fraud".*

is only for merging the company and not the licenses for which separate approval has to be obtained from the DoT.

Jurisdiction of TDSAT regarding transfer of licenses

The appropriate forum for deciding disputes as to whether overlapping licenses of Spice shall vest with Idea pursuant to amalgamation or stand transferred to the licensor, is an issue for the Telecom Disputes Settlement and Appellate Tribunal ("TDSAT") to decide.

Effect of suppression of material facts

As per the License Agreement and Merger Guidelines, prior permission of DoT is a requirement for transfer/ merger of licenses. Idea did not seek the approval of DoT for acquiring 41.09% in Spice and did not disclose this material information to the court, as required under the proviso to Section 391(2) of the Act, which mandates that the company or any other person, by whom an application for sanctioning is made, must disclose to the court *"all material facts relating to the company"*. The expression "such as" used before the examples given in the proviso show that the information is not exhaustive and other material facts are also to be supplied with an application seeking sanction of amalgamation scheme. This is further supported by the fact that the specific information is also suffixed by the words *"and the like"*. Thus, all material facts relating to the affairs of the company are to be disclosed.

The aforesaid suppression of material facts would have a bearing on the sanctioning of the scheme subject to certain conditions if the same had been disclosed, but it cannot be said that suppression amounts to playing a fraud requiring a revocation of the entire order sanctioning the scheme. The order of the company judge on fraud for suppression of facts was not upheld by the Division Bench of the Delhi High Court.

Conclusion

A merger of business entities does not necessarily imply an automatic/ consequent merger of all legal approvals/licenses held by the merging individual entities. Separate approvals would have to be obtained under the appropriate statute for successful completion of the merger as envisaged by the entities.

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NOTIFICATIONS & CIRCULARS

Powers of Registrar of Companies and the Regional Directors under the Companies Act: The Ministry of Corporate Affairs has vide Notifications dated 10th July, 2012 delegated the powers vested in the Central Government under Sections 21, 25, 31(1), 108(1D) and 572 of the Companies Act, 1956 to the Registrar of Companies of the State where the registered office of the company is situated or where the applicant ordinarily resides. Furthermore, The Central Government has also delegated its powers and functions vested under Sections 17, 18, 19, 22, 224(3), 224(4), 224(7), clause (a) of 224(8), 141, 188, 297(1), 394A, 400, 439(5) and 439(6), clause (a) of 496(1), clause (a) of 508(1), 551(1), clause (b) of 555(7), clause (a) of 555(9), 610(1) and 627 to the Regional Directors of Mumbai, Kolkata, Chennai, Noida, Ahmedabad and Hyderabad. Both these notifications shall come in force with effect from 12th August, 2012 when certain provisions of the Companies (Second Amendment) Act, 2002 (11 of 2003) will also come into effect (brought in force by another Notification dated 10th July, 2012) whereby reference to the "Company Law Board" is being substituted by the words "Central Government".

Fee payment required for filing certain e-forms: With effect from 22nd July, 2012, prescribed fees will be payable towards filing of certain forms electronically with the Registrar of Companies, Regional Directors or with the Ministry of Corporate Affairs Headquarters. MCA General Circular No. 14/2012, dated 21st June, 2012 imposes fees as per Schedule X of the Companies Act, 1956 for Forms 23B, 36, 62 and for Form 1 of Investor Education Protection Fund Rule. Fees for Forms 24A, 61 and 65 will be as payable per Companies (Fee on Application) Rules, 1999. The said circular however exempts Form 65 providing information and explanation on reservations and qualification contained in the cost audit report by a company, from any fees.

LLPs – Time for filing annual return extended: Time limit for filing annual returns under Form 11 by the Limited Liability Partnerships (LLPs) has been extended till 31-7-2012. Ministry of Corporate Affairs Circular No. 15/2012, dated 29-6-2012 which is effective from 30-6-2012, states that the time limit of 60 days shall be read as 122 days for the financial year ending 31-3-2012.

Specified companies to file Balance Sheet and Profit and Loss Account in XBRL mode: Companies listed with stock exchanges in India and their Indian subsidiaries, companies having paid up capital upto Rs. 5 Crore or more or having turnover of Rs. 100 crore or more or companies who are required to file their financial statements for FY 2010-11 using XBRL mode (Extensible Business Reporting Language) are now mandatorily required to file their Balance Sheet and Profit & Loss Account in XBRL mode for the financial year commencing on or after 1-4-2011. Such companies can file statements without any additional penalty/fees till 15-11-2012 or within 30 days of AGM, whichever is later. General Circular No. 16/2012, dated 6-7-2012 issued in this regard however also states that banking companies, insurance companies, power companies and NBFCs are exempted from XBRL filing.

Registration of transfer of equity shares and debt securities – Time-limit reduced: To expedite transfer of equity shares and debt securities, SEBI has reduced the time from 30 days to 15 days for such transfer. It has directed stock exchanges, registrars to an issue and share transfer agents to adhere to the revised time-limit of 15 days from the date of lodgment of transfer by the parties. By Circular No. 8/2012, dated 5th July, 2012, all concerned have been directed to incorporate provision for compensation for the delay in transfer of debt securities as presently available in case of transfer of equity shares.

Forex retention limit not applicable for resident foreign currency accounts: Reserve Bank of India has advised that the provisions limiting retention of foreign exchange in the EEFC account with any Authorised Dealer in India as prescribed by RBI Circular No. 128, dated 16-5-2012 will not apply for Resident Foreign Currency Accounts. The circular issued in May had allowed exchange earners to retain only 50% of the amount in foreign exchange and surrender balance 50% for conversion to rupees. As per the earlier circular, the EEFC account holder was permitted to access the forex market only after fully utilizing the balance available in his account. A.P. (DIR Series) Circular No. 8, dated 18-7-2012 has been issued in this regard.

RATIO DECIDENDI

Cartelization by certain cement manufacturers – CCI imposes penalty

The Competition Commission of India ("CCI") has imposed penalty of Rs. 6300 crores on 10 cement manufacturers for cartelization. It was noted that member companies, in addition to sharing their price and production related data on the platform of manufacturers' association, were also discussing the price and production related data of competing companies, indicative of coordinated and anti competitive behavior in violation of Section 3(3)(a) of the Competition Act. It was observed that even when the cost structure of the companies was different, there was similarity in price movement. The Commission also considered the non-utilization of production capacity to be a *'plus' factor* along with price parallelism to suggest collusive behavior between the companies. It was held that the companies were indulging in limiting and controlling the production and supplies in the market in violation of Section 3(3)(b) of the Act and that there was an inverse relation between prices and capacity utilization. No single firm was in a dominant position within the meaning of Section 4 of the Competition Act, 2002, hence penalty of 0.5 times of net profit for 2009-10 and 2010-11 was imposed on the cement manufacturers while penalty of 10% of total receipts of two years was imposed on the Cement Manufacturers Association [*Builders Association of India* v. *Cement Manufacturers Association* – CCI Order dated 20-6-2012 in Case No. 29/2010].

Cable operators denying access to particular channel – Penalty imposed by CCI

The CCI, in a recent order, has partly upheld the findings of the Director General for denial of market access to some broadcasters and other stakeholders in contravention of Section 4(2)(c) of the Competition Act, 2002 by certain cable operators working as a group. There was evidence of disruption in the telecast of a particular channel by the cable operators. The Commission observed that the subscriber base of the operators was large and every broadcaster was dependent on them; the group was in a position to affect the market in its favour and had denied the opportunity of transmission of channel of the informant. It noted that the argument of shortage of spectrum should have been considered at the time of entering into the agreement and the excuse of low TRP was an afterthought. The Commission however reversed the findings of the DG in regard to violation of Sections 4(2)(a)(i), 4(2)(b)(i) and 3 ibid. Contention of formation of cartel by the cable operators was overruled by the Commission stating that the operators were under the same group and there cannot be a case of anti-competitive agreement among entities of the same group. Penalty amounting to 6% of the average turnover of last three years was imposed [*Kansan News Pvt. Ltd.* v. *Fast Way Transmission Pvt. Ltd.* – Order dated 3-7-2012 in Case No. 36/2011].

Software companies are 'factories' and hence covered under ESI Act

The Bombay High Court in its recent judgment held that software companies are covered under the definition of 'factory' in the Employees' State Insurance Act, 1948. The definition of 'factory' in the ESI Act has wider meaning than the definition in the Factories Act as the meaning of the said term for the purpose of E.S.I. Act is not to be understood in the context of Explanation II of Section 2(m) of the Factories Act. It was also held that creation or development of software is a manufacturing process for such purposes. The single Judge Bench disagreed with the Division Bench order of the Madras High Court in the case of Seelan Raj R. on the point of Explanation-II of Section 2(m) of the Factories Act. It was noted by the court that application of the ESI Act is not a regressive but a progressive step and to think that its application would affect IT industry adversely is a futile fear [*Asstt. Director, ESIC* v. *Western Outdoor Interactive* – Order dated 11-7-2012 in First Appeal Nos. 143 and 307 of 2012].

NEWS NUGGETS

Priority sector lending – Foreign banks to comply with norms applicable to domestic banks

The Reserve Bank of India has issued revised guidelines in respect of priority sector lending, taking inputs from the Nair Committee which reviewed existing norms in priority sector lending. The recommendation that on principles of reciprocity, foreign banks should comply with priority target and sub-targets applicable to domestic banks has been accepted. Foreign banks with 20 and above branches will have to lend upto 40% of Adjusted Net Bank Credit or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher to the priority sector. These banks have been given a period of five years starting from April 2013 to achieve the target and sub-targets in respect of agriculture, exports, micro and small enterprises and advances to weaker sections.