

CPI's Asia Column Presents:

CCI'S Guidance on Calculation of Turnover

*By Nandish Vyas and Geet Sawhney (Veritas Legal,
India)¹*



Copyright © 2018

Competition Policy International, Inc. For more information visit CompetitionPolicyInternational.com

January 2019

The Competition Commission of India (CCI) recently amended its FAQ's on combination (**Amended Combination FAQs**), published on its website,² in order to bring them in line with the Ministry of Corporate Affairs, Government of India (MCA) 2017 notifications regarding (i) exemption from notifying a combination within thirty days³ and (ii) revised *de minimis* exemption⁴ as well as clarification on calculation of relevant assets and turnover in case a portion of an enterprise or division or business is being acquired, taken control of, merged or amalgamated. The most notable development in these Amended Combination FAQs includes providing guidance on (i) identification of target (assets/unit/division/enterprise) in variety of merger & acquisitions (M&A) transactions and (ii) calculation of turnover for the purposes of the Competition Act, 2002 (**Competition Act**). Till recently, there was no set guidance provided by the CCI as to how party(ies) to an M&A transaction should calculate its/their turnover. Further, between 2016-17, the CCI imposed penalty ranging from INR 0.2 million (USD 2,867/EUR 2,521)⁵ up to INR 10 million (USD 0.14 million/ EUR 0.12 million) on the acquirers' for their failure to notify transaction involving acquisition of portion of an enterprise/division/business due to incorrect calculation of turnover for *de-minimis/target based exemption*.⁶ However, Amended Combination FAQs now provide much needed guidance and clarity to party(ies), in terms of the Competition Act, while determining notifiability of M&A transactions through CCI's online guidance system '*Do It Yourself (DIY)*'.⁷

The Amended Combination FAQs on calculation of turnover are largely in line with European Commission's (EC) Council Regulation (EEC) No 4064⁸ which contains detailed guidance on calculating turnover. In this article we have discussed the methodology to be adopted by the parties to an M&A transaction in relation to calculation of turnover based on recent guidance from the CCI and the implications for both Indian as well as foreign enterprises engaged in diverse industrial sectors.

Introduction

The concept of turnover is extremely important under the Indian merger control regime as the Competition Act requires mandatory notification⁹ of all proposed M&A transactions to the CCI that breach certain asset and turnover based jurisdictional thresholds and qualify as a combination under Section 5 of the Competition Act. However, this mandatory pre-merger notification requirement is subject to certain exemptions, including the *de-minimis/target based exemption* which stipulates that any transaction involving acquisition¹⁰/merger/amalgamation¹¹ where the target enterprise has either value of turnover in India of less than INR 10 billion (USD 143.34 million/EUR 126.05 million) or value of assets in India of less than INR 3.5 billion (USD 50.17 million/ EUR 44.11 million) is exempt from pre-notification to the CCI (**Target Exemption**).

Therefore, the turnover of the party(ies) becomes the key determining point whether a proposed M&A transaction should be notified or not to the CCI. The CCI's methodology for calculation of turnover of parties to such proposed M&A transactions has been summarized in **Appendix A** of this article. The Competition Act provides an extremely broad and inclusive definition of the term turnover to include 'value of sales of goods and services' i.e. the income or revenue generated from the sale of goods or provision of services.¹² The Amended Combination FAQs attempt to remove the vagueness from the definition of turnover in terms of the geographic limitation as well as the time period for turnover calculation.

Time Period for Turnover Calculation: In relation to the time period for calculation of turnover, it has been clarified that in an M&A transaction, the turnover of a party is taken to be the book value of turnover shown in the audited books of accounts of the party for the financial year immediately preceding the financial year in which the binding document¹³ is executed. This is identical to how a party calculates the

value of assets under Explanation (c) to Section 5 of the Competition Act. However, in case of unavailability of such financial statements, the Amended Combination FAQs now reaffirm the current industry practice of considering the party's turnover as the turnover certified by the statutory auditor based on the last available audited accounts of the party, for the purposes of the Competition Act.

Geographic Limitation on Turnover Calculation: Similarly, in relation to the geographic limitation, Section 5 of the Competition Act provides two distinct and separate turnover thresholds, one for turnover of parties to M&A transaction in India and another for turnover of the parties to the M&A transaction worldwide, including India. For calculating the turnover of the parties in India the Amended Combination FAQs provides that the goods and services "exported from India" would be part of total turnover while computing the threshold limits under section 5 of the Competition Act. This is in line with the recent decisional practice of the CCI where it observed that the statutory definition of turnover under the Competition Act does not mean turnover as reported for a particular geographic segment and therefore, the entire turnover value as provided in the books of accounts of the enterprise concerned should be considered as turnover for the purposes of the Competition Act. In this case¹⁴ the acquirer (*Intellect Design Arena Limited (IDAL)*), in 2014, had failed to notify its acquisition of demerged business of the target entity (*Polaris Financial Technology Limited*) to the CCI. IDAL had generated majority of its turnover from outside India in FY 2012-13¹⁵ and had claimed that it was exempt under the Competition Act since total revenue attributable to India (and Middle East) was INR 576.94 crore (USD 82.70 million/EUR 72.72 million) and below the then target exemption thresholds.¹⁶ However, the CCI rejected the acquirer's (IDAL's) segmentation of revenue based on the location of customers and took the entire turnover of INR 1,853.99 crore (USD 265.76 million/EUR 233.70 million) as provided in the target entity's (Polaris's) book of accounts which breached the then target exemption thresholds and imposed a penalty of INR 1 million (USD 14,335/ EUR 12,605.57) on IDAL in this case. This approach followed by the CCI is however different from the European Commission's (*EC*) practice, which adheres to the community or member state dimension and follows the principle that turnover should be attributed to the place where the customer is located.¹⁷

Intra Group Revenue

Another concept of intra-group revenue becomes relevant while calculating turnover for the purposes of the Competition Act especially in M&A transactions where the Indian turnover of foreign enterprise (being party to the transaction) has to be calculated. In case of enterprises belonging to conglomerates with layers of subsidiaries spanning across different jurisdictions, substantial revenues may be generated by selling goods or providing services to the enterprises belonging to the same group. In one of the M&A transaction,¹⁸ the acquirer (Avago) claimed that the turnover of the target entity (Broadcom) in India was below the Target Exemption thresholds. However, the CCI refused to accept Avago's arguments since the latter had excluded the intra-group revenue generated by Broadcom's Indian subsidiaries¹⁹ from the Indian turnover whereas its Indian subsidiaries (namely BCTPL and BSIPL) books of accounts did not make any distinction between the revenue generated through intra-group sales and sales to the third parties. Therefore, the CCI found a delay of approximately 123 days of filing of the notification form and imposed a penalty of INR 1 million (USD 14,335/ EUR 12,605.57) on Avago. The CCI has now clarified by way of the Amended Combination FAQs, that the 'intra-group' sales are excluded from total turnover for the purposes of section 5 of the Competition Act. This is now in line with EC as they exclude the sale of products or the provision of services between any of the undertakings which have links with the undertaking concerned (essentially parent companies or subsidiaries).²⁰ However, until this position is clarified through the CCI's decisional practice, the parties to an M&A transaction should be cautious and

consider excluding the intra-group revenue while calculating their turnover in India only where such intra-group revenue is recorded separately in the books of accounts of the parties or their subsidiaries or other enterprises belonging to the same group.

Other Income and Indirect Taxes

Previously there seemed to be a debate amongst various industry players as well as their legal advisors in relation to treatment of 'other income' while computing turnover for the purposes of section 5 of the Competition Act. Further, in a scenario, where the combined turnover of the parties was marginally below than Section 5 threshold limits, the parties used to include the other income to the total turnover, out of abundant caution, and notify such combination to the CCI in order to avoid any penalty proceedings under Section 43A of the Competition Act. However, the CCI has explicitly clarified by way of the Amended Combination FAQs that the 'other income' is not to be included while computing turnover for the purpose of Section 5 of the Competition Act. This brings our jurisdiction in line with EC, as the latter only takes into account the revenue generated from the 'ordinary activities' of the undertakings concerned while calculating the turnover.²¹ Further, the Amended Combination FAQs have reiterated that the turnover under the Competition Act is to be "net turnover" i.e. gross turnover minus indirect taxes which corresponds to EC's approach to aggregate turnover which excludes rebates, value-added tax and other taxes directly related to turnover.²² This clarification earlier existed as notes to sample long form (Form II) provided by the CCI on its website.²³

Banking and Insurance Industry

Apart from the general guidance provided above in relation to calculation of turnover applicable across all industrial sectors, the CCI has also issued some industry specific guidance in relation to calculation of turnover of banking and insurance enterprises. In case of the banking enterprise, the turnover shall be sum of the operating income and other income (such as commission, exchange and brokerage; income earned by way of dividends; profit (loss) on sale of investments; leasing income; profit (loss) on exchange transactions). In case of the insurance enterprise, the value of the turnover would be the gross premium without deducting the reinsurance ceded, and other income such as income from investments in shares, securities, real estate or other assets, only where such investments amount to control (as per CCI's decisional practice)²⁴ over the enterprises involved. The CCI's concept of including the other income only from controlling investments in the turnover of insurance enterprise is similar to EC's practice of making a clear distinction between (i) a pure financial investments (with no participation of the insurance undertaking in investee undertaking's management) and (ii) investments giving control and right to exert a decisive influence to insurance undertaking over the subsidiary or affiliated company concerned.

Other Concerns

Calculating income in case of E-Commerce Sector - Although the limited guidance provided by the CCI on calculation of turnover is useful from various stakeholders point of view, however, there are certain areas where additional clarity is expected from the CCI either through formal guidelines, rules, regulations or through its orders. One such area of concern is ambiguity in calculation of turnover in case of e-commerce enterprises in India. India is the fastest growing market for the e-commerce sector and the revenue from this sector is expected to reach USD 120 billion in year 2020.²⁵ In case of e-commerce platforms such as Zomato, Trivago, Airbnb, Amazon, Flipkart etc. which do not own any restaurants, properties, hotels or retailers, respectively, but merely act as online platforms, it may be argued that the term turnover may

be interpreted to include only commission they earn on each sale of airplane, train, bus ticket etc. made through its platform.²⁶

Similarly in the case of radio taxi operators such as ANI Technologies Pvt. Ltd. (Ola) and Uber India Systems Pvt. Ltd. (Uber), which do not only operate as a platform/intermediaries between the drivers but are considered to be radio taxi operators by the CCI, the question that remains to be answered is how to calculate the turnover of these entities, as their drivers do not function as their employees, but are independent third party service providers. The CCI has recognized this in its recent order in *Meru Travel Solutions Pvt. Ltd. vs. M/s ANI Technologies Pvt. Ltd. & Ors.*,²⁷ where it observed that in certain markets, and increasingly in digital markets, the concerns related to common ownership may not be under the scanner of merger control rules if the merging firms or share acquisitions fall under the *de minimis exemption*, thus, giving rise to a statutory lacunae.

Attributing income to Non-revenue generating assets – In one of the M&A transactions²⁸ involving transfer of non-revenue generating Media Convergence Nodes (**MCN**) assets, the parties filed the notification form before the CCI out of abundant caution as the former believed the turnover of the MCN assets to be below Target Exemption thresholds. Further, according to parties, MCN assets on a standalone basis did not perform any revenue generation activities and were merely used to support the provision of telecom business. However, the CCI rejected the parties' arguments and held the entire turnover of the mobile telephony business to be attributable to these target non-revenue generating MCN assets and therefore, the combination was subject to CCI's approval.

Conclusion

In light of these new informal guidance in relation to calculation of the Target Exemption as well as Section 5 thresholds, penalties for belated notification form filing and/or gun jumping due to incorrect calculation of turnover thresholds can no longer be viewed as unwarranted by the parties.²⁹ It is possible that the CCI will now consider any omission to file notification form due to incorrect calculation of value of turnover of the parties as a substantive violation (and no longer a mere a technical violation) thereby attracting a maximum penalty of 1% of combined turnover/assets of the parties to a combination.³⁰ Further, where the parties to a proposed combination have any queries or seek clarification on turnover calculation or Target Exemption or filing requirements, they can avail pre-filing consultation offered by the CCI. Taking these matters into consideration, parties to proposed M&A transactions relating to India must make full assessment of the proposed transaction notification requirements after due and careful consideration of CCI's view on calculation of turnover.

APPENDIX – A

S. No.	Type of transaction	Target Enterprise	De Minimis/Target Exemption	Thresholds under Section 5
1.	Acquisition of assets/shares/voting rights/control of an enterprise. ³¹	The enterprise whose assets/shares/voting rights or control is being acquired.	Entire value of turnover of the target enterprise is taken into account.	<p><u>Parties Test</u> - The value of turnover of (i) the target enterprise and (ii) the acquirer.</p> <p><u>Group Test</u> - The value of turnover of (i) the target enterprise and (ii) the group to which the target enterprise would belong post combination.</p>
2.	Acquisition of portion of an enterprise/division/business. ³²	The portion of enterprise/division/business which is being acquired.	The value of turnover of the said portion of enterprise/division/business which is being acquired is taken into account.	The value of turnover attributable to (i) the portion of enterprise/division/business being acquired and (ii) the acquirer.
3.	Acquisition of control over an enterprise when acquirer already has a direct/indirect control over enterprise in similar/identical/substitutable line of business. ³³	The portion of enterprise/division/business which is being acquired or enterprise whose control is being acquired.	The value of turnover of the said portion of enterprise/division/business or the enterprise which is being acquired is taken into account.	<p><u>In case of acquisition of control over a portion of enterprise/division/business</u></p> <p>The value of turnover attributable to (i) the portion of enterprise/division/business being acquired (target business) and (ii) the turnover of enterprise over which the acquirer already has direct/indirect control.</p> <p>Or</p>

				<p><u>In case of acquisition of control over enterprise being acquired</u></p> <p><u>Parties Test</u> - The value of turnover of (i) the target and (ii) the turnover of enterprise over which the acquirer already has direct or indirect control.</p> <p><u>Group Test</u> - The value of turnover of (i) the group to which the target enterprise would belong and (ii) the enterprise over which the acquirer already has direct or indirect control.</p>
4.	Merger/Amalgamation of enterprise(s) into another enterprise. ³⁴	The enterprises being merged or wound up would be considered as the target enterprise.	The value of turnover of the enterprises being merged or wound up is taken into account.	<p><u>Parties Test</u> - The value of turnover of the enterprise remaining after the merger (surviving enterprise).</p> <p><u>Group Test</u> - The value of turnover of the group to which the enterprise remaining after the merger would belong after the merger/amalgamation.</p>
5.	Merger/Amalgamation of two or more existing enterprise(s) (amalgamating enterprises) to form a new	All amalgamating enterprises would be treated as the target enterprises.	The value of turnover of the amalgamating enterprises would be taken into account.	<u>Parties Test</u> - The value of turnover of all the enterprises merging/amalgamating.

	enterprise (amalgamated enterprise). ³⁵			<u>Group Test</u> - The value of turnover of the group to which the amalgamated enterprise would belong after amalgamation.
6.	Merger/Amalgamation of portion of an enterprise/division/business with another enterprise. ³⁶	The portion of enterprise/division/business which is being merged or amalgamated.	The value of turnover of the said portion of enterprise/division/business which is being merged or amalgamated is taken into account.	The value of turnover of the said portion of enterprise/division/business and the turnover of another enterprise which is being merged or amalgamated is taken into account.

¹ Nandish Vyas is a partner at Veritas Legal, India and Geet Sawhney is an associate at Veritas Legal, India.

² <https://www.cci.gov.in/node/2847>

³ Notification No. S.O. 2039(E) dated 29 June 2017, <https://www.cci.gov.in/sites/default/files/notification/S.O.%202039%20%28E%29%20-%2029th%20June%202017.pdf>

⁴ Notification No. S.O. 988(E) dated 29 March 2017, <https://www.cci.gov.in/sites/default/files/notification/S.O.%20988%20%28E%29%20and%20S.O.%20989%28E%29.pdf>

⁵ Exchange rates used: (i) 1 USD = 69.76 INR and (ii) 1 EUR = 79.33 INR.

⁶ CCI imposed a penalty of (i) INR 1 crore (USD 0.14 million/ EUR 0.12 million) each on Baxter Incorporated in [C-2015/07/297](https://www.cci.gov.in/sites/default/files/notification/C-2015/07/297) and on Eli Lilly and Company in [C-2015/07/289](https://www.cci.gov.in/sites/default/files/notification/C-2015/07/289); (ii) INR 10 lakh (USD 14,335/EUR 12,606) on SRF Ltd. in [C-2015/12/347](https://www.cci.gov.in/sites/default/files/notification/C-2015/12/347); (iv) INR 2 lakh (USD 2,867/EUR 2,521) on Diasys Diagnostics Systems GmbH, Germany and DiaSys Diagnostics India Private Limited in [C-2015/09/313](https://www.cci.gov.in/sites/default/files/notification/C-2015/09/313); (v) INR 25 lakh (USD 35,837/ EUR 31,514) each on Schulke & Mayr GmbH in [C-2015/12/349](https://www.cci.gov.in/sites/default/files/notification/C-2015/12/349) and on Reydel Automotive Holdings B.V. in [C-2015/08/298](https://www.cci.gov.in/sites/default/files/notification/C-2015/08/298); (vii) INR 10 lakh (USD 14,335/EUR 12,606) each on Avago Technologies Limited in [C-2015/09/312](https://www.cci.gov.in/sites/default/files/notification/C-2015/09/312) and on Future Consumer Enterprise Limited in [C-2016/03/384](https://www.cci.gov.in/sites/default/files/notification/C-2016/03/384); and (viii) INR 5 lakh (USD 7167/EUR 6,303) on ITC Limited in [C-2017/02/485](https://www.cci.gov.in/sites/default/files/notification/C-2017/02/485).

⁷ The CCI on 4 July 2018 launched an online guidance system 'Do It Yourself (DIY): A notifiability check for mergers & acquisitions under the Competition Act, 2002'. <https://efilingcci.gov.in/DIY>

⁸ Council Regulation (EEC) No 4064 / 89 of 21 December 1989 on the control of concentrations between undertakings', <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:31989R4064>

⁹ Section 6(1) of the Competition Act states that 'No person or enterprise shall enter into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and such a combination shall be void.'

¹⁰ This includes any acquisition as referred to in Section 5(a) and Section 5(b) of the Competition Act.

¹¹ This includes any merger or amalgamation as referred to in Section 5(c) of the Competition Act.

¹² Section 2(y) of the Competition Act

¹³ Section 6(2)(b) of the Competition Act and Regulation 5(8) of the Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011 (**Combination Regulations**).

¹⁴ Order dated 7 May 2018 passed under Section 43(A) against [Intellect Design Arena Limited](https://www.cci.gov.in/sites/default/files/notification/C-2018/05/18);

¹⁵ As per Polaris Financial Technology Limited Investor Release for financial year ended 31 March 2013. Link:

-
- http://www.polarisft.com/investor/presentations/investor_presentation_2013_14_q4_services.pdf. Further, in the CCI Combination Order *Polaris Consulting & Services Limited/ Virtusa Consulting Services Private Limited C-2015/12/348* the CCI had mentioned that for financial year 2014-15 Polaris Consulting & Services Limited (formerly known as Polaris Financial Technology Limited) had generated 74.55% of its total revenue from exports. Therefore, based on the financial statements, the target entity (Polaris) was an export oriented enterprise.
- ¹⁶ The *de minimis/target exemption* in 2014 exempted transactions involving acquisition of control/shares/voting rights/assets where the target enterprise had assets not more than INR 2.5 billion (USD 35.83 million/EUR 31.53 million) or generated turnover of not more than INR 7.5 billion (USD 107.51 million/EUR 94.54 million). Notification No. S.O. 482(E) dated 4 March 2011, <https://www.cci.gov.in/sites/default/files/notification/SO479%28E%29%2C480%28E%29%2C481%28E%29%2C482%28E%29240611.pdf>
- ¹⁷ Article 5(1) of the Council Regulation (EEC) No 4064 / 89
- ¹⁸ Avago Technologies Limited/ Broadcom Corporation ([C-2015/09/312](#)), Order dated 7 June 2017,
- ¹⁹ Broadcom had two wholly owned subsidiaries in India viz, Broadcom Communications Technologies Pvt. Ltd. (*BCTPL*) and Broadcom Semiconductors India Private Limited (*BSIPL*).
- ²⁰ First subparagraph of Article 5(1) of Council Regulation (EEC) No 4064 / 89
- ²¹ Article 5(1) of Council Regulation (EEC) No 4064 / 89.
- ²² Article 5(1) of the Council Regulation (EEC) No 4064 / 89.
- ²³ The CCI prescribes filing of [Form I](#) (short form) or [Form II](#) (long form), as set out in Schedule II of the Combination Regulations, for notification of combinations.
- ²⁴ The interpretation of term 'control' is critical from the perspective of examining whether a combination may avail the benefit of exemptions. 'Control' is defined under Section 5 of the Competition Act to include 'controlling the affairs or management by (i) one or more enterprises, either jointly or singly, over another enterprise or group; (ii) one or more groups, either jointly or singly, over another group or enterprise.' The CCI, in its limited decisional practice, has interpreted control to mean "the ability to exercise decisive influence over the management or affairs and strategic commercial decisions" of a target enterprise, whether such decisive influence is being exercised by way of a majority shareholding, veto rights (attached to a minority shareholding) or contractual covenants.
- ²⁵ <https://www.ibef.org/industry/ecommerce.aspx>
- ²⁶ As per the *Guidance Note on Tax Audit under Section 44AB of the Income-tax Act, 1961* - In the case of a travelling agent, the amount received from the clients for payment to the airlines, railways etc. where such amounts are received by way of reimbursement of expenses incurred on behalf of the client, do not form part of "gross receipts in business" for purposes of section 44AB. If, however, the travel agent is conducting a package tour and charges a consolidated sum for transportation, boarding and lodging and other facilities, then the amount received from the members of group tour should form part of gross receipts.
- ²⁷ Meru Travel Solutions Pvt. Ltd. vs. M/s ANI Technologies Pvt. Ltd. & Ors., [Case No. 25-28 of 2017](#)
- ²⁸ Reliance Jio Infocomm Limited/ Reliance Communications Limited [C-2018/01/550-553](#)
- ²⁹ In terms of Section 43A of the Competition Act, the CCI can levy a maximum penalty of 1% of the total turnover or assets of such combination, whichever is higher.
- ³⁰ Order under S.43(A) in Eli Lilly and Company/ Novartis AG, [C-2015/07/289](#)
- ³¹ Section 5(a) of the Competition Act.
- ³² Notification No. S.O. 988(E) dated 29 March 2017
- ³³ Section 5(b) of the Competition Act.
- ³⁴ Section 5(c) of the Competition Act.
- ³⁵ Section 5(c) of the Competition Act.
- ³⁶ Notification No. S.O. 988(E) dated 29 March 2017