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CCI CONCLUDES ITS 8TH PHASE II INVESTIGATION WITH BEHAVIORAL COMMITMENTS IN THE COMBINATION OF LARSEN & TOUBRO AND SCHNEIDER

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The Competition Commission of India (CCI) recently published its order granting a conditional approval to the combination between Larsen & Toubro Limited (L&T), Schneider Electric India Private Limited (SEIPL) and MacRitchie Investments Pte. Ltd. (MacRitchie), which involves (Proposed Combination):

- acquisition by SIEPL of L&T's electrical and automation business (E&A Business) (excluding certain assets) by way of a slump sale on a going concern basis pursuant to a business transfer agreement; and

- acquisition of 35% shareholding in SIEPL by MacRitchie by way of a share subscription agreement after the business transfer.

The transaction forms part of the global agreement entered between L&T and Schneider Electric Industries SAS (Schneider) whereby Schneider will acquire the international E&A Business of L&T.

Relevant Market(s)

The Proposed Combination is a consolidation of 2 closest competitors in the low voltage switchgear industry in India (LV Switchgear Market). The CCI carried out the competition impact assessment of the Proposed Combination at 2 levels, (a) product level; and (b) cluster/portfolio level.

- *Product Market:* While 29 overlapping products were identified between the parties comprising various products and solutions used in the LV Switchgear Market, the CCI narrowed down the scope to 15 product markets which were highly concentrated and where the combined market share of the parties was on an average more than 30%; and

- *Cluster/Portfolio Market:* At the cluster level, 6 products were identified where the combined market share of the parties was in the range of 55-60%.

CCI's prima facie opinion on appreciable adverse effect on competition

The CCI formed a *prima facie* opinion that the Proposed Combination was likely to cause an appreciable adverse effect on competition (AAEC) in the overall LV

Switchgear Market in India and conducted a *phase II* investigation. This was due to the high market share of the parties, the level of combination in the LV Switchgear Market, the peculiar characteristics of the LV Switchgear Market (discussed below) and the absence of any specific or verified efficiencies resulting from the Proposed Combination.

Red flags and findings of the CCI

- The Proposed Combination pertains to consolidation of the top 2 leading players in the LV Switchgear Market in India. The next competitor would be 3 to 4 times smaller than the combined entity (such as, ABB and Siemens).

- L&T and Schneider have the widest range of product offerings in the LV Switchgear Market. There is a strong industry preference for the use of same brand of products in building a switchboard and thus a player offering a complete portfolio of components has an inherent advantage in the LV Switchgear Market.

- The consolidation would enable the combined entity to push its portfolio to the distributors by way of bundled offerings, rebates, volume discounts, etc., and would also lead to *de facto* exclusive dealership arrangements.

- Given the industry practice of executing long-term exclusive distributorship agreements and the stable/ static market share trends of the last 3 years, the potential of new and credible entrants entering the market is also very low.

- Combined entity will also have an incentive to completely discontinue product offerings of L&T or Schneider altogether.

- The market strength of the combined entity would enable it to unilaterally dictate the prices, quality and the entire commercial culture of the LV Switchgear Market.

Seesaw of Remedies

To alleviate its AAEC concerns in the 6 cluster markets (comprising, Air Circuit Breakers (ACBs), Moulded Case Circuit Breakers (MCCBs), Switch Disconnect Fuse (SDFs), Motor Protection Circuit Breakers (MPCBs), Contactors and Overload Relays), the CCI had proposed divestment of 2 of L&T's plants in Ahmednagar and Vadodara (along with distribution networks/ channel partners) to an approved purchaser. However, the parties considered the remedy proposal of the CCI unviable and disproportionate and offered an alternative remedy package which was ultimately accepted by the CCI based on European Commission's decisions:

- *Strengthening existing third-party LV Switchgear manufacturers*: SIEPL would strengthen existing third-party LV switchgear manufacturers by offering them "white-labelling" product manufacturing services in relation to the 5 products manufactured by L&T solely for products to be sold in India, and for the product ranges existing as at the date of closing (except to ABB and Siemens). SIEPL would also allocate a specified level of its installed capacity for the 5 products for a period of 5 years;

- *No de facto exclusivity in distributorship and commercial agreements*: SIEPL would amend its distributorship and commercial agreements to remove any barriers that encourage *de facto* exclusivity (such as, deletion of termination clauses, discontinuation of loyalty rebates) for a period of 5 years from the date of closing of the Proposed Combination;

- *Maintenance of existing number of distributors by SIEPL:* SEIPL would not replace or increase any of the distributors existing as of the date of closing of the Proposed Combination for a period of 3 years from the date of closing;

- *Transfer of technology:* SEIPL would provide a mutually acceptable, non-transferable, non-sub licensable, royalty bearing non-exclusive technology license for a period of 5 years to a single third party that had availed white labelling manufacturing services for any of the 5 products of L&T; and

- *Other commitments:* Certain other remedies were also accepted by the CCI which included, pricing mechanism, minimum export commitments, non-rationalisation of parties' product range, and maintenance of R&D expenditure.

Comment

The decision assumes significance as it is the first-of-its kind in so far as it mandates pure play behavioural remedies ranging between 3 to 5 years. Until now, the CCI's preferred remedy has been the convenient and straightforward divestment or a combination of divestment coupled with certain behavioural commitments.

The CCI continues to place reliance on (without re-inventing the wheel) and learn from the dealings of its global counterparts while assessing similar sectors that often pose unprecedented challenges in the context of the Indian markets. The LV Switchgear Market appears to be one such market which warranted bespoke remedies in view of the highly integrated and indivisible nature of the sector. The effectiveness of the behavioural commitments to create viable, credible and long-term competitors however remains to be seen.

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