

M&A Hotline

May 13, 2014

SEBI CLEARS JET-ETIHAD DEAL

- Jet- Etihad deal cleared by SEBI
- SEBI holds no open offer required under the Takeover Code
- The ambit of 'control' under the Competition Act is wider than that under the Takeover Code
- Acquirer cannot be 'person acting in concert' with the target company

Securities Exchange Board of India ("**SEBI**"), by way of its order dated May 8, 2014 ("**Order**") has given a green signal for the proposed investment by Etihad Airways PJSC ("**Etihad**") in Jet Airways (India) Limited ("**Jet**").¹ With this, the proposed transaction seems to have cleared all regulatory hurdles finally.

BACKGROUND

In September 2012, foreign investment in aviation industry in India was liberalized. In January 2013, Jet was the first airline to make a public announcement when it informed the Bombay Stock Exchange of talks with Etihad of potential investment by Etihad in Jet. The transaction was to be carried out by way of preferential allotment of 27,263,372 shares of Jet to Etihad ("**Transaction**"). For the purpose of consummating the Transaction, the parties entered into (a) investment agreement dated April 24, 2013 ("**IA**"), (b) a shareholders' agreement between the promoters of Jet, Jet and Etihad ("**SHA**"), (c) a commercial cooperation agreement dated April 24, 2013 ("**CCA**") and (d) a corporate governance code pursuant to the SHA ("**CGC**"). The IA, SHA and the CCA were amended on September 19, 2013 on the basis of certain issues raised by regulators (the amended agreements and the CGC are collectively referred to as the "**Transaction Documents**" hereinafter). The proposed preferential allotment was approved by the board of directors and the shareholders of Jet on April 24, 2013 and May 24, 2014, respectively.

The Transaction required the approval of a number of regulators, including the Cabinet Committee on Economic Affairs ("**CCEA**"), Foreign Investment Promotion Board ("**FIPB**"), the Competition Commission of India ("**CCI**") and SEBI.

APPROVALS

FIPB	The FIPB was to consider approving the Transaction in its meeting on June 14, 2013. ² However, the decision was deferred by FIPB stating that more clarity was required with respect to Etihad's rights under the Transaction Documents. Subsequently, the Transaction was approved by FIPB in its July 29, 2013 meeting. The approval was conditional requiring certain conditions as mentioned therein to be satisfied.
SEBI	SEBI had approved the Transaction on October 1, 2013 stating that the Transaction would not trigger open offer obligations under the SEBI (Substantial Acquisition of Shares and Takeovers Regulations), 2011 (" Takeover Code "). <i>However, SEBI did not comment on the CCA, and had specifically stated that it would be guided by the decision of the other regulators in this regard.</i>
CCEA	On October 3, 2013, the CCEA approved the Transaction. ³
CCI	The CCI approval (" CCI Order ") for the Transaction was received on November 12, 2013. ⁴

ISSUE

The CCI Order⁵, in light of the surrounding facts, including (a) Jet and Etihad were in the business of providing air transport services, (b) the terms of the CCA which, *inter alia*, laid the framework for co-operation in operations, pricing, joint marketing, sales, and distribution, joint airport handling, (c) Etihad's recommendation of candidates for Jet's senior management and (d) utilization of Abu Dhabi as an executive hub, stated:

It is observed that the Parties have entered into a composite combination comprising inter alia the IA, SHA and the CCA, with the common/ultimate objective of enhancing their airline business through joint initiatives. The effect of these agreements including the governance structure envisaged in the CCA establishes Etihad's joint control over Jet, more particularly over the assets and operations of Jet.

In light of the above observation of the CCI, SEBI served show cause notices dated February 11, 2014 ("**SCN**") on the

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promoters of Jet, namely Naresh Goyal, Anita Goyal and Tail Winds Limited (“Promoters”) and Etihad (“Noticees”) alleging joint control over Jet by Etihad and the Promoters under the Takeover Code requiring an open offer under regulation 4 of the Takeover Code by Etihad.

CONTENTIONS OF THE NOTICEES

Tailwinds

With respect to Tail Winds, it was contended that since it was no longer a shareholder of Jet, the question of joint control with it would not arise.

Naresh Goyal and Anita Goyal

- SEBI should not rely on the CCI’s decision since the purpose of the Competition Act, 2002 (“CA 2002”), i.e. to regulate combinations which cause appreciable adverse effect on competition in the market was completely different from that of the Takeover Code, which aims at providing an exit to shareholders in the case of a change in the target company. CCI holding that the proposed Transaction is not exempted from the CCI (Procedure in regard to the Transaction of Business Relating to Combinations) Regulations, 2011 would not tantamount to the same being an acquisition of control under the Takeover Code.
- The Transaction Documents do not give Etihad any veto or affirmative rights, right to appoint only 2 out of 12 directors on the board of Jet, any casting vote, any quorum rights at the board or shareholder level or any pre-emptive / tag rights.

Etihad

- The CCA has been entered into to exploit synergies and expand their respective networks. These agreements facilitates rationalization of costs, efficiencies of scale and leverages presence of partner airlines in the market
- The provisions of the Transaction Documents are to be carried out in a manner that is in compliance with applicable Indian laws. Under the Department of Industrial Policy and Promotion’s Press Note No.6 of 2012 (“PN 6”)⁶, while rationalizing investment in Indian airlines by foreign airline operators, one of the conditions laid down were:

“A Scheduled Operator’s permit can be granted only to a company:

... -

(c) the substantial ownership and effective control of which is vested in Indian nationals”

While giving the approval for the Transaction, FIPB had implied that the ‘effective control’ of Jet remained with Indian nationals.

- With respect to the CCA, which has been entered into between Jet and Etihad and not the Promoters, Etihad relied on the decision of the Supreme Court of India in *Daiichi Sankyo v. Jayaram Chigurupati*⁷ to state that an ‘acquirer’ cannot be a ‘person acting in concert’ with the target company itself under the Takeover Code.
- The rights of Etihad under the Transaction Documents indicate that it does not have any control over Jet under the provisions of the Takeover Code. In particular, the shareholders’ agreement is not indicative of control being transferred, lack of any veto rights or any pre-emptive rights.
- The parties to the various agreements executed amendment agreements to remove contentious clauses which were questioned by the regulators from a ‘control’ perspective, such as:

- Removal of the right to recommend candidates to senior management positions of Jet;

- Abu Dhabi no longer the exclusive hub for flights flying towards Africa, North America, South America and UAE;

- Etihad’s lead role in negotiations for acquisition of aircrafts now replaced by reciprocal arrangements subject to approval of both Jet and Etihad’s boards.

DECISION

The whole time member of SEBI held that the Transaction would not attract the provisions of the Takeover Code. In concluding the same, it relied on the following points.

- The Ministry of Finance (“MoF”) has clarified that the mandate of FIPB/ CCEA is merely to ensure compliance with the FDI Policy. The FDI Policy has been revised by PN 6 to state ‘A Scheduled Operator’s permit can be granted only to a company the substantial ownership and effective control of which is vested in Indian nationals’⁸ Accordingly, FIPB and CCEA’s approval is evident that the Transaction is in compliance with the FDI Policy.
- Comparing the definitions of ‘control’ under the FDI Policy and the Takeover Code, the Order mentioned that the definitions are *para materia*. While comparing the Takeover Code definition of control with that under the CA 2002, the Order held that the definition as under CA 2002, which deals with ‘controlling the affairs and management’ is of much wider import than that under the Takeover Code, which includes the right “to appoint majority of the directors” or controlling *the management or policy decisions*. Accordingly, the decision of CCI would not be the guiding factor for SEBI in determining if control has been acquired under the Takeover Code.
- In determining whether Etihad was a person acting in concert, the Order emphasized that the definition of persons acting in concert, read with Justice P.N. Bhagwati committee’s observations⁹ required a common objective of acquisition of shares or voting rights or control of the target company. Unless the commonality of objective of acquisition of shares/ voting rights/ control was established, the concerned persons would not be persons acting in concert. The objective of the CCA was merely to exploit synergies by detailing operational modalities.
- Since the Promoters were not parties to the CCA, and as per the Supreme Court’s verdict in *Daiichi Sankyo*, an acquirer cannot be a person acting in concert with the target company itself, it was held that the Etihad and Jet are not persons acting in concert.
- The right to control the decisions rests with the Cooperation Committee and the four Facilitation Groups (formed under the CCA), which would make recommendations, and such recommendations would need to be approved by

the boards of both Jet and Etihad. Since the recommendation would also need to be approved by Jet's board, the CCA does not affect the right to control policy decisions.

■ The Order also relied on the lack of substantial controlling powers with Etihad, which included, inter alia:

- Etihad's right to nominate only 2 out of 12 directors;
- Promoters being able to nominate the chairman of the board of Jet, who shall have a casting vote;
- Etihad not having any quorum rights at the board or general meeting;
- Lack of any veto/ affirmative voting rights with Etihad;
- Any pre-emptive/ tag along rights with Etihad.

CONCLUSION

SEBI's verdict is a welcome move, since it has clarified that while interpreting the respective statutes, the intent and the objective of the statute needs to be looked into. While with this verdict, the Transaction has been cleared by all regulators, a public interest litigation is pending before the Supreme Court in India alleging, *inter alia*, lack of transparency in the entering of the bilateral agreement entered into by India with UAE for increase in passenger seat capacity. The Supreme Court has already clarified that the Transaction may be quashed if irregularities are discovered. This might result in complicating the Transaction further since the shares have already been allotted to Etihad on November 20, 2013 post approval from the CCI.¹⁰

At a macro level, our regulators and the government need to ensure that deal timelines do not get stretched on account of delay in decision making. Certainty in law, faster decision making by regulators and better coordination amongst regulators is quintessential for a robust M&A regime in India. With the election results around the corner, it would be important for the incoming government to give comfort to international investors on ease of doing deals in India. As far as the regulatory hurdles to the Jet-Etihad partnership is concerned, it seems the sky is clear for the time being. However, time will tell whether a smooth take off also results in smooth landing.

For a detailed analysis of the Transaction, please refer to our M&A Lab [here](#).

- **Abhinav Harlalka & Nishchal Josphipura**

You can direct your queries or comments to the authors

¹ Order in the matter of acquisition of shares of Jet Airways (India) Limited (hereinafter referred as "Jet") by Etihad Airways PJSC (hereinafter referred as "Etihad") available online at http://www.sebi.gov.in/cms/sebi_data/attachdocs/1399545948533.pdf

² FIPB Approval would be required as under Paragraph 6.2.9. 3.1 (c) (i) of the FDI Policy, any investment by a foreign airline into an Indian company providing scheduled air transport services would be under the Government Route, i.e. with the prior approval of FIPB.

³ Under the FDI Policy any transaction involving more than INR 12,000 million requires CCEA approval.

⁴ For a detailed analysis of the approval from CCI, please refer to our hotline available [here](#).

⁵ Available online at <http://www.cci.gov.in/May2011/OrderOfCommission/CombinationOrders/C-2013-05-122%20Order%20121113.pdf>

⁶ http://www.dipp.nic.in/English/acts_rules/Press_Notes/pn6_2012.pdf

⁷ AIR 2010 SC 3089

⁸ Paragraph 6.2.9.3.1 (c) (iv) (c) of the FDI Policy 2014.

⁹ Para 2.2 of the Justice P.N. Bhagwati Committee Report on Takeovers states

"To be acting in concert with an acquirer, persons must fulfill certain "bright line" tests. They must have commonality of objectives and a community of interests which could be acquisition of shares or voting rights beyond the threshold limit, or gaining control over the company and their act of acquiring the shares or voting rights in a company must serve this common objective. Implicit in the concerted action of these persons must be an element of cooperation. And as has been observed, this cooperation could be extended in several ways, directly or indirectly, or through an agreement - formal or informal"

The report is available online at <http://www.sebi.gov.in/commreport/bagawati-report.html>

¹⁰ [http://www.bseindia.com/xml-data/corpfiling/AttachHis/Jet_Airways_\(India\)_Ltd2_201113.pdf](http://www.bseindia.com/xml-data/corpfiling/AttachHis/Jet_Airways_(India)_Ltd2_201113.pdf)

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