

July 03, 2017

## CCI ISSUES GUIDANCE NOTE ON NON-COMPETE RESTRICTIONS

In accordance with international best practices, Competition Commission of India (“CCI”) has issued a Guidance Note on non-compete restrictions (“**Guidance Note**”).

The Guidance Note is intended to highlight CCI’s “*general approach*” when dealing with non-compete clauses entered into by parties to transactions which are notified to CCI for approval.

As a preface, CCI has clarified that the Guidance Note is not binding on the parties to a combination but it is intended to serve as an important tool in drafting non-compete clauses. Additionally, CCI has clarified that the standards set forth in the Guidance Note would not be applied mechanically but upon consideration of the specific circumstances of each case.

### General Principles

According to the Guidance Note, a non-compete restriction should be “*directly related and necessary to the combination*” in order to merit approval.

#### Directly Related

- A non-compete restriction is considered directly related where it is economically related to the main combination and it is intended to allow a smooth transition to the post-combination scenario.
- In order to be directly related, the non-compete restriction must be connected and closely linked to the combination, but ancillary or subordinate to its main object.
- It is NOT sufficient if the restriction has been entered into at the same time or in the same context as the combination.
- It is also NOT sufficient if the non-compete restriction is “*merely stated*” to be so related.

#### Necessary

A non-compete restraint is considered necessary if:

- In the absence of such non-compete restriction the combination could not be implemented;  
OR
- In the absence of such non-compete restriction the combination could only be implemented under more uncertain conditions, at substantially higher cost, over an appreciably longer period or with considerably higher difficulty.

Additionally, in order to be considered directly related and necessary to the combination, the scope of the non-compete restriction in terms of its duration, subject matter, geographic field of application and scope of application “*should not exceed what is reasonably required*” having due regard to the nature of the business concerned.

The Guidance Note clarifies that if equally effective alternatives are available for achieving the same object as the non-compete clause, parties must have chosen one which is the “*least restrictive of competition*”.

#### Duration of Non-Compete Clause

- If the transaction involves transfer of both goodwill and know-how, the non-compete is justified for a maximum period of 3 years.
- If the transaction involves transfer of goodwill only, the non-compete is justified only for a period of 2 years.
- Longer durations than the above may be justified in a “*limited range of circumstances*” where for example:
  - In certain industries, customer loyalty will persist for longer durations, or
  - The nature of the know-how transferred justifies an additional period of protection.
- In case of a joint venture (“**JV**”), the duration of the non-compete restriction can normally be the standing period of the joint venture. However, a non-compete restriction for a longer duration may also be justified in certain circumstances.

#### Geographic Scope of Non-Compete Clause

- In case of an acquisition, the geographical scope of a non-compete clause must be limited to the area where the seller has offered the products or services prior to the transfer.
- The geographical scope of the non-compete may also extend to those areas where the seller was planning to enter at the time of the transaction, provided that the seller has “*already invested in such a move*”.
- In case of a JV, the geographical scope of the non-compete should be limited to the areas in which the JV partners were offering the “*relevant products and services*” before establishing the joint venture (including areas where the JV partners were planning to enter at the time of the transaction provided investments advancing this intention have been made).
- Any extension of the non-compete to territories where the JV “*may in the future decide to become active*” will not be considered ancillary to the combination.
- Where a JV is being set up to enter a new market, the scope of non-compete restrictions can be extended to products, services and territories where the JV is supposed to operate pursuant to the JV agreement.

- However, a non-compete should not be used to prevent competition between JV partners in markets other than those in the JV will be active from the outset.

### Subject Matter

- A non-compete obligation must be restricted to the products and services comprising the “*main activity*” of the transferred business/enterprise or joint venture, as the case may be.
- The scope of the non-compete restraint may also include:
  - Improved version or updates/successor models of products, or
  - Products and services at an advanced stage of development at the time of the combination, or
  - Products which are fully developed but not yet marketed.

### Scope of Application

- A non-compete obligation may bind only the seller, its subsidiaries and agents. Non-compete obligations imposed on others, such as resellers, will not be considered ancillary to the combination.
- Non-compete obligation may be imposed only on controlling shareholders of an enterprise. A non-compete obligation on non-controlling shareholders will not be considered ancillary to the combination.
- Clauses which limit a seller’s/JV partner’s right to purchase or hold shares in a competing company will be considered ancillary to the combination if they are in compliance with the conditions specified above. However, such a clause will **NOT** be considered ancillary if it prevents the seller/JV partner from purchasing or holding shares “*solely for investment purposes*”, without granting him/her, directly or indirectly, management functions or any material influence in the competing company.

### **Key Takeaway**

The Guidance Note is consistent with CCI’s proactive advocacy role best evidenced by the regular release of compliance manuals, booklets etc. so as to improve the understanding of competition laws among the stakeholders.

Though restricted to non-compete clauses, the Guidance Note reflects the best practices of other jurisdictions such as the European Commission’s *Commission Notice on Restrictions Directly Related and Necessary to the Concentrations in the EU* (“**EU Commission Notice**”).

Significantly, when the EU Commission Notice was amended in 2001, it was clearly specified that the Commission would no longer assess the ancillary restrictions *together* with the transaction. Though the CCI Guidance Note does not expressly state so, it would be interesting to see if CCI intends to follow a similar practice whereby the fate of the transaction is not necessarily hinged on the non-compete clause.

The Guidance Note does clarify that where a non-compete restriction is not found to be directly related and necessary to the combination by the CCI, the CCI's order approving the combination would not cover such a restriction but it would NOT automatically lead to a presumption that such clauses would infringe the provisions of the Competition Act, 2002.

The Guidance Note, as intended, is also likely to play an important role for stakeholders in designing suitable and legally-acceptable non-compete clauses for their transactions.

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