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The 2013 guide to

Mergers and Acquisitions

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Fairer trade

Rittidej Mohprasit of Weerawong Chinnavat & Peangpanor examines the evolving sector-specific M&A environment in Thailand and the results

Thailand's economy continues strong despite the recent global economic repression and a decade of local political struggles. Last year alone, the country experienced considerable growth in merger and acquisition activity, both in number of deals and volume of deals. UBS statistics show the total value of merger and acquisition activity in Thailand increasing from an average of $3.7 billion per year in 2002–2009 to an average of $13.1 billion per year in 2010–2012, and ultimately hitting a record of $18.7 billion last year. This market trend is expected to continue upward in future years. As in 2012, the biggest acquisitions occurred in the financial (financial institutions), energy production (especially natural gas), consumable products, healthcare, and hotel/resort sectors. This substantial increase was assessed to be partly attributed to the results of nationwide flooding in the second half of 2011, relatively stable political atmosphere, record high stock market price, high availability of loans, and disciplined fiscal and monetary policies.

In spite of the economic boom, the main market sectors in Thailand are known to be highly concentrated. Several key factors arguably contribute to this market characteristic; a notable one is the lack of enforcement of competition law.

Merger-control rules

For years, it could be said that the Royal Thai Government has regarded the issue of free and fair competition as less pressing than other items on the political and economic agenda. In 1999, Thailand enacted a Thai Trade Competition Act (TCA) in an aim to ensure economic stability and allocative efficiency of the Thai markets. The TCA contains the main antitrust principles found in most other antitrust laws, including abuse of market dominance (section 25), merger control (section 26), and collusion (section 27). Beside a few horizontal restrictions, such as price fixing, quantity fixing, and bid rigging, other restrictive practices are governed by a quasi-rule of reason doctrine. In addition to civil compensation, the law imposes criminal penalties for violations. The TCA mainly applies to the private sector, with exemptions for state enterprises, agricultural and other cooperatives, central and regional government agencies, and various other businesses which are to be covered by other ministerial regulation.

Some provisions of the TCA, however, were not instantly enforceable once the law took effect. Instead, the TCA setup an independent trade regulator, the Trade Competition Commission (TCC), to further specify procedural and substantive provisions regarding enforcement of the TCA. The TCC commissioners consist of four bureaucrats and a maximum of 12 trade competition experts (the Minister of Commerce as a chairperson of the TCC, and other individuals from the private sector). The TCA has given the TCC responsibility to prescribe sub-legislation (in the form of TCC notifications) regarding the enforcement of merger-control provisions of the TCA, including the responsibility to issue notifications concerning the specific process by which a certain merger will be examined. The TCC may also set out a minimum threshold of market share, total sales, amount of capital, and number of shares or quantity of assets of a merger which will be subject to prohibition under this section. Further, pursuant to section 26 of the TCA, the merger of businesses which fall under the following criteria will be deemed regulated mergers: (i) the merger of a manufacturer and another manufacturer, a distributor with another distributor, a manufacturer with a distributor, or a service provider with another service provider, where the mergers will result in one business being maintained while the other is extinguished or a new business is formed; (ii) the purchase of all or part of the assets of another business for the purpose of controlling business administration policy, administration or

> "The main market sectors in Thailand are highly concentrated"

> **"Foreign ownership in telecommunications is stringently monitored"**

management; and (iii) the purchase of all or part of the shares of another business for the purpose of controlling business administration policy, administration or management. Once a transaction is determined to be within the scope of regulated merger, the transaction will be evaluated against the criteria set by the TCC. A business operator, who is involved in the merger of businesses which trigger the minimum threshold, as prescribed in the notification by the TCC, must obtain an approval from the TCC.

As of today, the TCC has set threshold figures determining when a business operator is considered to have a "dominant" market position; however, the TCC has not yet issued any notification pursuant to section 26. Without criteria such as a minimum threshold in determining the regulated merger, or a procedure by which the TCC will examine a merger, section 26 is thus unenforceable. Therefore, it can be concluded that mergers in Thailand can be implemented without being subject to a general competition law.

In terms of competition regulation in Thailand (as well as in other countries), however, there are two levels of authority involved. The first is the competition authority, such as the TCC, which has a regulatory mandate over competition issues covering all sectors of the economy. The second level is the sector regulator with a mandate over trade in a specific sector. Despite sharing a common goal, the competition authority and sector regulators may generally have different legislative mandates and their perspective regarding competition matters may be different, and sometimes may overlap.

Developments in the telecommunications sector

The development of Thai telecommunication regulations is largely based on the historical context of the Thai telecommunication sector. From the early 1950s, telecommunications services in Thailand were legally monopolised by governmental entities, namely the Post and Telegraph Department, the Telephone Organization of Thailand (TOT), and the Telephone Organization of Thailand (CAT). Later, in the 1980s, as demand for telecommunications services increased rapidly and the government was not in a position, financially, to invest heavily on networks, Thailand introduced the build-transfer-operate concession scheme. Under this scheme, a concession issued by the TOT or CAT allowed the private-sector operator to operate a telecommunications business. As for considerations, the TOT or CAT gained ownership of the telecommunications networks built by the private-sector operator immediately after the construction of the network was completed and, in return, the private-sector operator was granted the exclusive rights to operate the network and offer telecommunication services to the public. The TOT and CAT received an annual concession fee, which was based on a portion of the revenue generated by the private-sector operator. At this stage, mergers and acquisitions in the telecommunication market were not subject to any regulation.

In the late 1990s, Thailand was under an international commitment to open up the telecommunications sector. Pursuant to the new telecommunication frameworks, the National Telecommunications Commission (NTC), a now-defunct national regulatory agency for the telecommunication sector, was established with duties to regulate the telecommunication sector and to ensure free and fair competition between telecommunication operators. It is worth noting that, since the build-transfer-operate concession agreements have not expired and are protected under a grandfather clause, and the two regimes are now co-existing in the Thai telecoms market. It should also be noted that the NTC was abolished in late-2010, and the National Broadcasting and Telecommunications Commission (NBTC), the successor of the NTC, was subsequently formed and mandated with the authority to regulate broadcasting and telecommunications sectors (a converged regulator). As a part of the succession, NTC regulations are still fully in effect and are now under supervision of the NBTC, except in the case that a regulation is inconsistent with the new legal framework, or the new regulation has been promulgated by the NBTC.

Limitations on foreign participation in the telecommunications sector

Foreign ownership in telecommunications was more stringently monitored than other sectors under the general Foreign Business Act. Section 8 of the Telecommunication Business Act BE 2543 (2000) establishes foreign ownership limits in Type 2 and 3 telecommunications licences (required for the majority of all telecommunications services) for applicants at a maximum of 25%. In addition, at least three-quarters of directors and persons authorised to sign on behalf of these applicants must be Thai nationals. The NTC will have the power to prescribe that an applicant must not commit any act that leads to the taking over of the business by a non-Thai person. In 2006, the Telecommunication Business Act was amended to match the foreign ownership limit pursuant to the Foreign Business Act. Foreign ownership of a telecommunications operator is limited to no more than 50% of all voting rights.

In 2012 the NBTC promulgated the Foreign Dominance Regulation BE 2555 (FDR) in which the NBTC goes further than just a simple ownership restriction. The FDR prohibits the forms of foreign dominance listed below, by which all licensees must prepare a submission of foreign dominance restriction measures, show adoption, and submit this to the NBTC for consideration of the compliance measures:

- dominance of a licensee by foreigners or their representatives through control of shares;
- dominance where foreign shares have a favourable status over domestic shares;
- dominance where a foreigner directly or indirectly controls policy, management, operations, appointment of directors and management;
- dominance through financing and loans, guaranteeing of loans, provision of loans at lower than market rates or any funding mechanism that is discretionary and controlled by a foreigner;

About the author

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- dominance through control of intellectual property, franchises, sole distributorships where that relationship involves transfer of money or other remuneration to a foreigner;
- dominance through control of procurement contracts with remuneration involving a foreigner;
- dominance through transfer of costs with a foreigner; and
- dominance through transfer pricing with a foreigner.

The authorised directors of the licensees must certify that they will not take any action in violation of such restrictions. Moreover, the licensee is required to conduct an annual review of the foreign dominance restriction measures and subsequently propose such measures to the annual general meeting of shareholders for approval. Once approved by the shareholders and certified by authorised directors, the licensee must submit the measures and report its foreign dominance status to the NBTC within 30 days from the date of the shareholders' meeting. If there is a high risk of violation, the licensee must report the risk to the NBTC immediately and propose preventive or remedial measures.

Merger-control rules in the telecommunications sector

The NTC promulgated sector-specific regulations regarding merger control which are still being used today. There are three main notifications in place to address this issue:

- the NTC Notification on Measures to Prevent *Monopolistic and Unfair Competition Practices in Telecommunications BE 2549 (2006)* (the "Competition Code");
- the NTC Notification on Market Definition and Relevant Markets in Telecommunications BE 2551 (2008) (the "Market Definition Code"); and
- the NTC Notification on Merger and Cross-Holding Rules and Procedure BE 2553 (2010) (the "Merger Code").

As a general competition framework for the telecommunications market, the Competition Code was promulgated with an aim of ensuring that telecommunications licensees would compete under the principle of free and fair trade. Pursuant to section 8 of the Competition Code, a telecommunications licensee is prohibited from holding or acquiring more than 10% of the total voting rights, or to own wholly or partly the assets of other licensees in the same business, either directly or indirectly, so that it could have controlling power over other licensee's policy or business, except where the acquirer obtained permission from the NBTC. The Competition Code requires that the NBTC must not permit an acquisition if it might prevent or restrict competition or a monopoly might be formed with respect to telecommunications. In the case that permission is granted, the NBTC may set certain conditions for the acquirer to follow to prevent undesirable effects on competition. This regulation specifically addresses the case where one telecommunications operator might gain certain controlling power over another licensee which, in effect, could restrict the level of competition in the market.

These issues become even more sophisticated with respect to the Merger Code, where special rules will be applied where:

- a licensee or its controlling shareholder merges with the other licensee (a case where one licensee will cease to exist);
- a licensee or its controlling shareholder acquires wholly or partly the assets of other licensee; or
- a licensee or its controlling shareholder acquires more than 30% of total voting rights, either directly or indirectly, of other licensee, or significant control over another licensee so that it could dictate the other licensee's policy, governance, management or operation.

The controlling shareholder means a shareholder or any person which holds, directly or indirectly, more than 25% of the total voting rights of the licensee, is able to appoint or discharge a director, is able to dictate the licensee's policy or management, or is *de facto* responsible for the management of the licensee.

In the event that a business combination falls under any of the aforementioned circumstances, the acquirer must file a merger review petition to the NBTC at least 60 days before the execution of the combination agreement. Pursuant to section 8 of the Merger Code, the NBTC may only grant a permission to the acquirer to execute a merger which does not cause market dominance. To determine whether a market is dominant, the NBTC will apply the Herfindahl–Hirschman Index (HHI) to identify the level of concentration in a relevant market. The following cases will be deemed to indicate that the merger causes market dominance and hence it will not be allowed pursuant to the Merger Code:

- the pre-merger HHI is lower than or equal to 1,800 and the post-merger HHI is higher than 1,800, where the difference of HHI between pre- and post-merger is more than 50; or
- the pre-merger HHI is higher than 1,800 and the post-merger HHI has been increased by more than 100.

The Merger Code further requires the NBTC to periodically examine the effect on competition of a permitted merger for at least two years after a permission to merge has been granted. To prevent double filing, a licensee who filed the petition pursuant to the Merger Code will not be required to obtain permission under section 8 of the Competition Code. Also, the short-form petition, with less stringent requirements, is also available for a merger in which the amount of the deal falls below a certain threshold.

A relevant market will be defined using procedure and methodology specified by the Market Definition Code. The NBTC will take into consideration the market characteristics such as supply substitutability, demand substitutability, barrier to entry and structure of the market. Economic tools such as Hypothetical Monopolist Test (SSNIP Test), Own-Price and Cross-Price Elasticity of Demand will be used to assist the NBTC in defining a relevant market, so that the NBTC could determine whether a merger would prevent or restrict competition in a certain market. Additionally, the Market Definition Code sets out a list of pre-defined markets in order to streamline the process of the NBTC in reviewing a merger petition, among other things. The pre-defined markets are domestic fixed-line retail service, domestic mobile retail service, international telephony retail service, low-speed internet retail service, high-speed internet retail service, domestic fixed-line wholesale service, domestic mobile wholesale service, international telephony gateway service and international internet gateway service.

"Merger and acquisition activity is projected to remain robust"

The scope of application of the Merger Code is broader than the Competition Code in terms of merger control. Where the Competition Code focuses mostly on the relationship between licensees, the Merger Code examines multiple layer of control over the licensee as well as the characteristics of a market. Moreover, the Merger Control and the Market Definition Code employ economic tools to determine the effect of a merger in the telecommunications sector. It is worth noting that the Competition Code and the Merger Code do not exempt the licensee from the application of the TCA. The TCA, once the criteria under section 26 are set, will concurrently apply to merger activities in telecommunications sector.

In summary, with the existing competition legal framework, merger and acquisition activity in Thailand is projected to remain robust. The lack of enforcement pursuant to the general competition law does not necessarily mean, however, that merger and acquisition activities are unregulated. The problem of a trade law vacuum is being addressed by sector-specific regulators. The telecommunications regulator, for example, is gradually adopting the fair trade principle into its legislative regime so that regulatory gaps are minimising rapidly. Therefore, investors can expect more sector-specific competition laws in the future.