M&A Lab

Jet-Etihad: Jet Gets a Co-Pilot

Deal Dissected

May 2014

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Democratic Enterprise: A Law Firm Shapes Organizational Behavior to Create Competitive Advantage' in the September 2009 issue of Global Business and Organizational Excellence (GBOE).

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Jet-Etihad: Jet Gets a Co-Pilot

November 20, 2013 was a historic day for the Indian aviation industry after Jet Airways (India) Limited ("**Jet**" or "**Target**") and Etihad Airways PJSC ("**Etihad**") concluded the much talked about US$ 379 million investment by Etihad to acquire a 24% stake in Jet ("**Deal**"). In addition to the equity investment, Etihad has also agreed to infuse US$ 150 million into JetPrivilege, the frequent flyer program of Jet, to be managed by its subsidiary, Jet Privilege Private Limited and also provide or arrange for a loan of US$ 150 million to Jet. Earlier this year, Etihad had purchased 3 slots owned by Jet at the Heathrow airport in London for US$ 70 million.

The saga of the Jet-Etihad deal has been in rumours since August 2012, a month prior to the liberalization of the aviation industry to foreign investment by foreign airlines. According to sources, the first step towards what culminated into the first investment by a foreign airline into an Indian airline was taken in July 2012, when Naresh Goyal, the chairman of Jet Airways Limited brought up the idea with James Hogan, the Chief Executive Officer of Etihad Airways PJSC. Considering it beneficial to the economy, Mr. Goyal said *"the infusion of foreign direct investment in the Indian aviation sector will result in economies of scale, grow traffic at Indian airports, and create job opportunities. It will greatly benefit all our stakeholders whilst significantly benefitting our guests who will now have access to a more expanded global network, enhancing connectivity for tourists, business travellers, Indian families and the wider travelling public".*

The Deal has been the most talked about deal of the year 2013 for the various issues faced in its consummation, including various issues raised by the regulators around the 'control' of Jet post the Deal. The Deal continued to be surrounded by controversies with allegations against the government for changing the policies to facilitate the Deal. Time will tell whether Etihad's entry as a co-pilot will ensure safe landing for Jet in future.

In this M&A Lab we have attempted to analyze the legal, regulatory, tax, financing and few other commercial dimensions of the Deal.

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1. Prologue

November 20, 2013 was a historic day in the Indian aviation industry after Jet Airways (India) Limited ("**Jet**" or "**Target**") and Etihad Airways PJSC ("**Etihad**") concluded the much talked about US$ 379 million investment by Etihad to acquire a 24% stake in Jet ("**Deal**").[1] In addition to the equity investment, Etihad has also agreed to infuse US$ 150 million into JetPrivilege, the frequent flyer program of Jet, to be managed by its subsidiary, Jet Privilege Private Limited and also provide or arrange for a loan of US$ 150 million to Jet. Earlier this year, Etihad had purchased 3 slots owned by Jet at the Heathrow airport in London for US$ 70 million.

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After extensive rounds of discussions and a number of disagreements, especially on the valuation of Jet[4], the parties finally agreed on the commercial terms of the transaction to go ahead.

Thereon, this transaction saw various issues and hurdles- ranging from the Government of United Arab Emirates ("**UAE**") seeking protection of UAE investments in India to regulatory approvals of Indian regulatory agencies on grounds of 'control'.

It was when the discussions were in advanced stage between the parties that the Governments came into the picture. The Government of UAE, in the wake of the earlier incidents involving some UAE entities, namely Abu Dhabi National Oil Co., Emaar Properties and Etisalat, was adamant that the Indian Government assures some sort of protection to the investments incoming from the UAE. It was only after the Indian Government acceded to this request that the transaction proceeded.

1. http://www.bseindia.com/xml-data/corpfiling/AttachHis/Jet_Airways_(India)_Ltd2_201113.pdf.
2. http://www.livemint.com/Companies/7kAkK9HVCYF7rwejneedeM/How-the-JetEtihad-deal-was-struck.html.
3. Supra. note 1 http://www.bseindia.com/xml-data/corpfiling/AttachHis/Jet_Airways_(India)_Ltd2_201113.pdf.
4. http://www.livemint.com/Companies/7kAkK9HVCYF7rwejneedeM/How-the-JetEtihad-deal-was-struck.html.

2. Details of The Deal

I. Parties Involved

A. Purchaser

Etihad is the national airline of the United Arab Emirates. It is a public joint stock company set up in July 2003 by the Royal (Amiri) Decree, and commenced its commercial operations in November 2003.[5] Etihad is primarily engaged in the business of international air transport of passengers. Additionally, Etihad is also engaged in maintenance and repair services, ground handling services, cargo transportation and travel management services, with Etihad Cargo and Etihad Holidays being its two main divisions.

B. Issuer

Jet is a public limited company registered under the Indian Companies Act, 1956. After initially setting up Jetair (Private) Limited, Mr. Naresh Goyal ("**NG**"), the non-resident Indian ("**NRI**") promoter of Jet, diversified his business activities in 1991 taking advantage of the opening of the Indian economy and enunciation of the Open Skies policies by the Government of India to set up Jet Airways for the operation of scheduled air services on domestic sectors in India. It was incorporated as a private limited company on April 1, 1992, and commenced operations from May 5, 1993.[6] Gradually, it expanded to various international destinations as well, making it one of the finest airlines in the world. It was on 28 December, 2004 that the company became a public limited company. Jet is listed both on the National Stock Exchange of India Limited ("**NSE**") and the Bombay Stock Exchange Limited ("**BSE**"). Jet also has 3 wholly owned subsidiaries,

i. Jet Lite (India) Limited – a domestic airline providing low cost services to customers;

ii. Jet Privilege Private Limited – as part of its alliance with Jet, Etihad has agreed to buy a majority stake in this company; and

iii. Jet Airways Training Academy Private Limited.[7]

C. Promoters

The following are the promoters of Jet ("**Promoters**"):

i. NG.

ii. Anita Goyal ("**AG**"), wife of NG.

iii. Tailwinds Limited, a company re-registered under the Companies Act, 2006 under the laws of The Isle of Man ("**Tailwinds**").

II. Transaction Documents

The parties have executed following agreements ("**Transaction Documents**") in connection with the Deal:

i. An investment agreement dated April 24, 2013 executed between the Target and Etihad governing the terms of the preferential allotment made to Etihad ("**IA**").

ii. A shareholders agreement dated April 24, 2013 executed between the Company, Promoters and Etihad which relates to various matters agreed between them including in relation to the Company and its management after the acquisition of equity shares through preferential allotment ("**SHA**").

iii. A commercial co-operation agreement dated April 24, 2013 in order to set up an integrated alliance between Jet and Etihad ("**CCA**"). The intention of the parties to enter into the CCA, was to lower administrative costs, sharing of joint resources, better customer service and efficient administration of their respective businesses.

iv. In addition to the above documents, the parties have also agreed to adopt a corporate governance code ("**CGC**") pursuant to the terms of the SHA.

Pursuant to the concerns raised by the regulators, the parties entered into the following agreements on September 19, 2013:

a. Amendment agreement to the IA;

b. Amended and restated SHA;

c. Amended and restated CCA.

5. http://www.etihad.com/en-in/about-us/our-story/
6. http://www.jetairways.com/doc/FactSheet_JetAirways.pdf
7. http://www.jetairways.com/doc/InvestorRelations/AnnualReport201213.pdf

III. Deal Snapshot

Subscription Shares	27,263,372 equity shares of the Target with face value of INR 10 each
Etihad's stake in Jet post issuance	24%
Allotment Price	INR 754.7361607 (Rupees Seven Hundred And Fifty Four Point Seven Three Six One Six Zero Seven Only). The shares were issued to Etihad at a premium of 32%.
Total Consideration	INR 20,576,652,711.02 (Indian Rupees Twenty Billion Five Hundred And Seventy Six Million Six Hundred And Fifty Two Thousand Seven Hundred And Eleven Rupees And Two Paise).
Other Aspects of the Deal	Along with the subscription to the equity shares of Jet, Etihad has also made or agreed to make the following investments in Jet: ▪ US$ 70 million was invested by Etihad to purchase 3 landing and departure slots owned by Jet at Heathrow Airport in February 2013.[8] These slots were acquired by Etihad by way of a sale and lease back arrangement. ▪ An amount of US$ 150 million will be invested by Etihad into Jet's frequent flyer program, 'Jet Privilege'. ▪ In addition to the above, Etihad has also agreed to extend low interest loans of US$ 150 million, to retire the high interest debt on the books of Jet.[9]

IV. Key Terms of the Deal

A. Board of Directors

i. Structure

Under the terms of the original deal, the board of the Target was limited to 14. The Promoters had the right to nominate 4 directors, with 3 directors to be nominated by Etihad and 7 independent directors were to be appointed on the recommendations of the nomination committee to be constituted in accordance with the CGC.

Concerns were raised by FIPB on the structure of the board, pursuant to which the parties agreed to revise the structure of the board. FIPB's main concern was regarding the control of the board and the management polices of Jet, which under the FDI Policy should mandatorily be with Indian nationals. Under the original deal, Etihad had 3 directors on the board and also had a significant say in the appointment of independent directors on the board. The nomination committee was comprised of 5 members with 1 each nominated by Promoters and Etihad and 3 members to be appointed by Promoters' and Etihad's nominees.[10] Under this structure Etihad had the ability to indirectly control more than half the board of Jet.

Under the revised structure the total number of directors was reduced to 12. The representation of the Promoters on the board continued to be 4, however, Etihad had to give up 1 board seat to dispel the concerns of the regulators regarding effective control of the Target. Also under the amended CGC role of the nomination committee, appointment and removal of independent directors has been made advisory in nature and the board is not bound by its recommendations.[11] The manner of constitution of the nomination committee was also revised with, Promoters and Etihad nominated 1 member each and the remaining 3 members to be recommended by the board of Jet.

The terms of the SHA provide that NG will be appointed as the Chairman of the board and Etihad is entitled to nominate the Vice-Chairman. The

8. http://www.bseindia.com/xml-data/corpfiling/AttachHis/Jet_Airways_(India)_Ltd_250413.pdf
9. http://articles.economictimes.indiatimes.com/2013-10-24/news/43366221_1_etihad-airways-stake-sale-jet-airways-group
10. http://www.livemint.com/Companies/32uCgxThgcDjlXAcnHE5CK/Sebi-may-clear-JetEtihad-deal-sans-open-offer.html
11. http://www.rediff.com/business/report/etihad-sets-terms-to-lower-strength-on-jet-board/20130826.htm

Chairman will not have a casting vote in case of equality of votes.

ii. Board Committees

Etihad is entitled to appoint a director nominated by it to be a member of each committee of the board. Further in addition to the appointment of the independent directors, the nomination committee would also recommend the senior officials for Jet. However, after the concerns raised by FIPB, the CGC was amended to provide that a director nominated by Etihad can be appointed to the nomination and audit committees only if such director is nominated by the board of the Target.[12] All the committees formed by the two airlines for administrative and operational functions are to be advisory in nature.[13]

iii. Quorum

The quorum for a board meeting of the Target is at least 4 directors which should include at least one Director nominated by the Promoters and one by Etihad unless either of them waives their presence in writing.

iv. Decisions

Under the terms of the SHA, certain matters such as alteration of share capital, appointment and removal of CEO, amendment of the constitutional documents and declaration of dividend required approval of atleast 3/4th of the directors present and voting. However, due to the concerns expressed by the regulators, under the amended and restated SHA all matters will be resolved by the board by way of simple majority.[14]

B. Share Transfer Restrictions

i. Lock In of Etihad Shares

Etihad and its affiliates are prohibited from directly or indirectly transferring their shares for a period of 3 years from the date of issue of shares, unless agreed by any one of the Promoters. Jet is allowed to transfer the shares directly or indirectly only according to the conditions prescribed. The lock-in will not apply to any transfer between Etihad and its affiliates.

ii. Restriction on Promoters' Shares

In order to protect the value of the investment and to ensure continued interest of Etihad in the Target, Promoters will continue to legally and beneficially own shares representing at least 51% of the equity share capital of the Target. Other than for certain exempted transfers, prior approval of Etihad will be required for any transfer of their shareholding by the Promoters. Further NG shall at all times exercise control either directly or indirectly over at least 26% of the equity share capital and should not directly or indirectly transfer these shares without prior written approval of Etihad.

iii. Right of First Refusal and Tag Along Rights

Any transfer of shares by the Promoters or Etihad will be subject to a right of first refusal of Etihad and Promoters respectively. Additionally, Etihad will also have the right to tag along in a transfer by the Promoters, provided Etihad offers all the shares held by it to the proposed transferee.

C. Further Acquisition of Shares

Any further acquisition of the shares of the Target by the Promoters, Etihad and their respective affiliates and persons acting in concert, is subject to consent of the other party. If a party acquires any shares of the Target, after obtaining the required consent, then it is liable to indemnify the other party for any loss that may be caused as a result of such acquisition. The parties have specifically acknowledged that in such an acquisition, the Promoters and Etihad may be considered as *'persons acting in concert'* under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (**"Takeover Code"**).

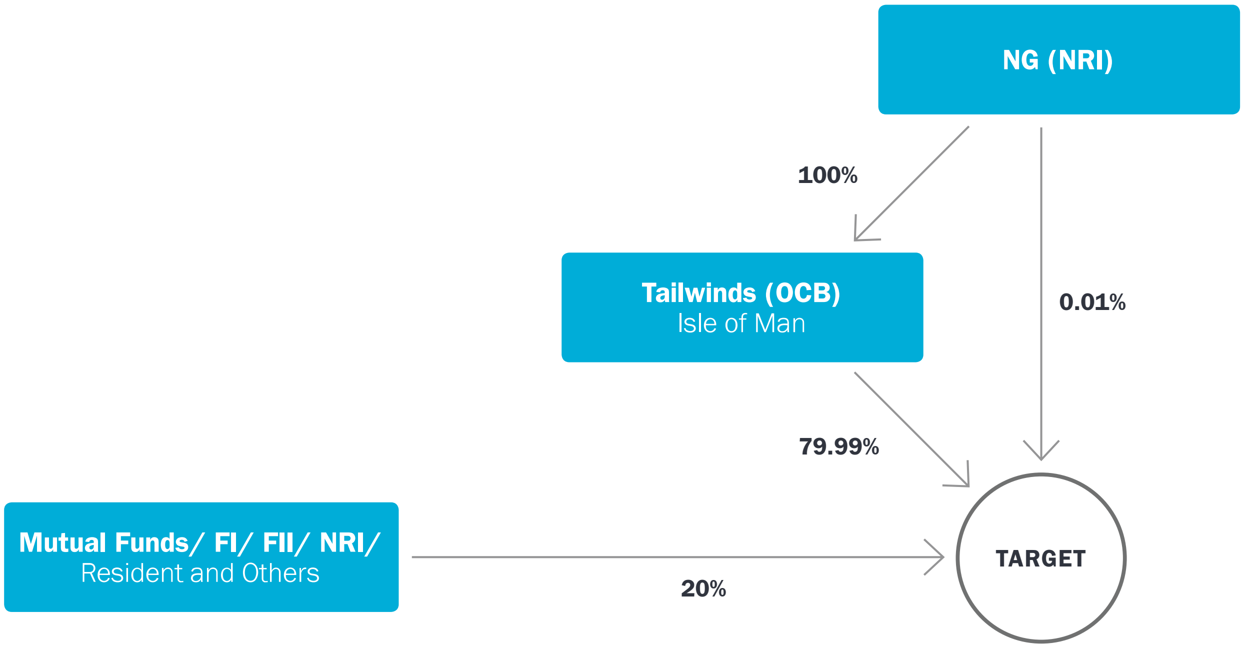
V. Deal Structure

In addition to the issuance of shares to Etihad, the Deal also involved transfer of shares inter se within the Promoters and by the Promoters (Tailwinds) to the public shareholders, in order to comply with the minimum public shareholding norms under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009.

A. Shareholding of the Target Prior to the Deal:[15]

Prior to the Deal, the shareholding of the Promoters in the Target was 80% of the share capital of the Target, out which 79.99% was held by Tailwinds with the remaining 0.01% held by NG and AG.

12. http://www.financialexpress.com/news/with-fipb-s-approval-on-monday-jetetihad-deal-to-take-off-finally/1147202.
13. http://www.business-standard.com/article/economy-policy/jet-etihad-deal-taxies-past-fipb-runway-113072900663_1.html
14. http://articles.economictimes.indiatimes.com/2013-08-02/news/41008570_1_jet-airways-etihad-sebi-nod-capital-market-regulator
15. http://www.bseindia.com/xml-data/corpfiling/AttachHis/Jet_Airways_(India)_Ltd_290413.pdf



B. Transfers by Tailwinds

i. Compliance with Minimum Public Shareholding Requirements

The Securities Contract (Regulation) Rules, 1957 were amended in 2010 to provide for a minimum public shareholding ("**MPS**") of 25% for listed companies in the private sector.[16] The companies were given a period of 3 years, till June 2013 to comply with these requirements. In order to comply with MPS requirements, Tailwinds sold 5% of the shareholding of the Target to public on May 30, 2013. These transfers were made by Tailwinds through an offer for sale ("**OFS**") on the floor of the stock exchange and block deal. As it received bids for only 3.46% of shareholding out of 5% offered under the OFS, it sought exemption from SEBI to make another OFS and sell the remaining 1.54% of the shares on the floor of the stock exchanges.[17]

Further, prior to the issuance of the shares to Etihad, Tailwinds offloaded 7.89% of the shareholding of the Target on November 18, 2013.[18] One of the primary reasons for this was that the Target would have continued to comply with the minimum public shareholding, even if Etihad was considered as joint promoters in the Target.

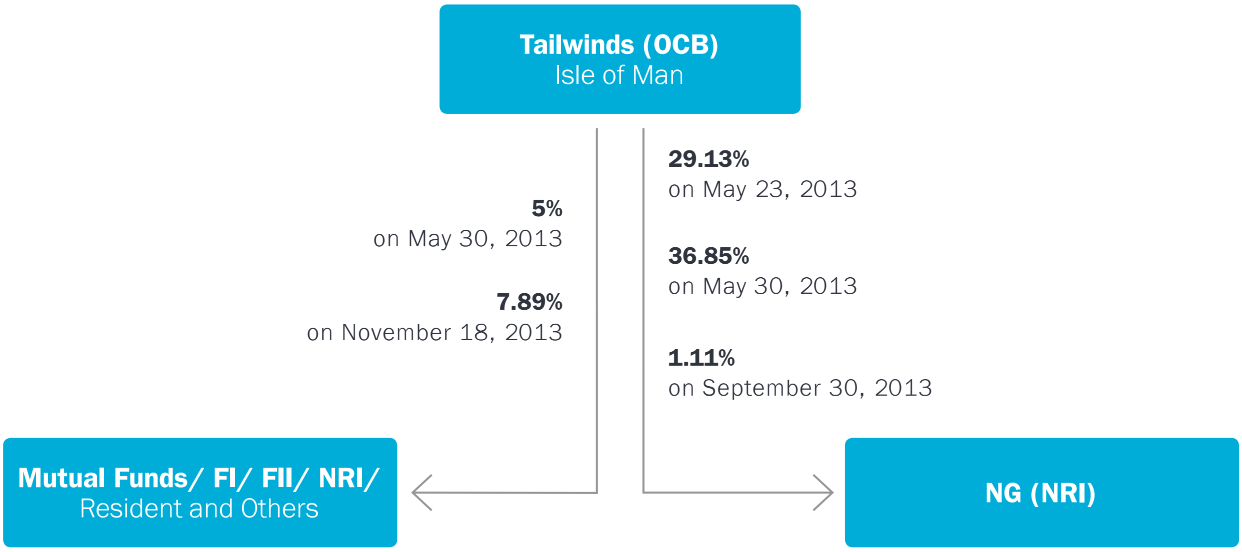
ii. Compliance with the FDI Policy

Under the FDI Policy, foreign investment in an Indian airline is permitted up to 49% of the shareholding of the company and NRIs can hold up to 100% of the Indian airline. Prior to the execution of the Transaction Documents, Tailwind held 79.99% of the Target. As Tailwinds is an overseas corporate body registered in the Isle of Man, its shareholding will be included in calculating the foreign investment in the Target. In order to become compliant with the FDI Policy, Tailwinds, in a series of transactions transferred 67.09% of the shareholding to NG. Since NG is an NRI, as per the FDI Policy, 100% NRI investment is permitted in Jet.

16. http://www.sebi.gov.in/cms/sebi_data/attachdocs/1332906227114.pdf.

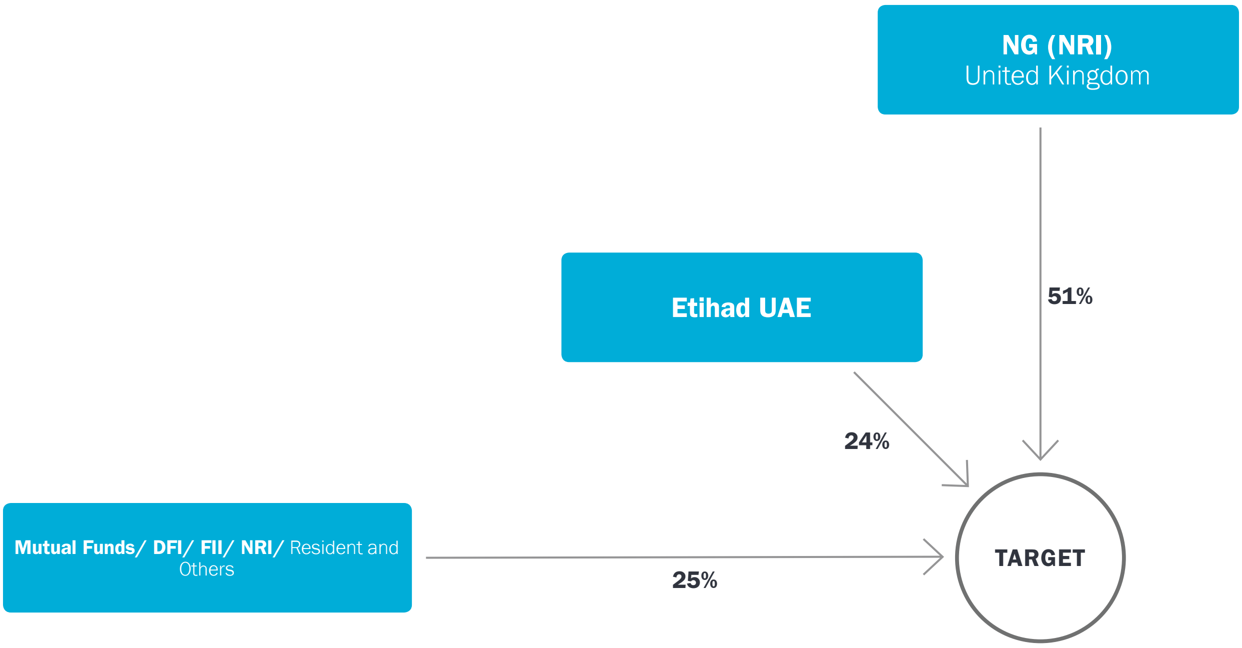
17. Under SEBI Circular No. CIR/MRD/DP/18/2012 dated July 18, 2012, there should be gap of 2 weeks between 2 OFS made by the promoters of a company to meet the MPS requirements. Please see the letter from SEBI granting exemptions under this circular at, http://www.bseindia.com/xml-data/corpfiling/AttachHis/Jet_Airways_(India)_Ltd_310513.pdf

18. http://articles.economictimes.indiatimes.com/2013-11-18/news/44202458_1_jet-airways-tail-winds-deutsche-securities-mauritius



C. Shareholding of the Target Post Completion of the Deal

As per the terms of the transaction agreed between NG and Etihad, post completion of the Deal, NG will hold 51% of the shareholding of the Target with Etihad holding 24% and the remaining 25% shall be held by public shareholders.



VI. Chronology of Events

Date	Particulars
January 3, 2013	Jet informed BSE about talks with Etihad.[19]
February, 2013	Etihad chief executive James Hogan and Jet Airways' chairman Naresh Goyal led a joint delegation of both the airlines and separately met Finance Minister P. Chidambaram, Civil Aviation Minister Ajit Singh and Commerce Minister Anand Sharma to apprise them about a possible stake sale deal.[20]
February 27, 2013	Announcement of Etihad buying Jet's landing and departure slots at Heathrow in a sale and lease back agreement signed on February 26, 2013.[21]
April 24, 2013	▪ Board of Jet approves the issuance of 27,263,372 equity shares by way of preferential allotment to Etihad. ▪ Jet and Etihad along with the Promoters execute the IA, SHA and the CCA.
May 24, 2013	Preferential allotment to Etihad is approved by the shareholders of Jet.
June 14, 2013	FIPB defers the decision on Etihad's investment into Jet.[22]
July 29,2013	FIPB grants conditional approval to Etihad to acquire stake in Jet.[23]
September 16, 2013	BJP leader Subramanian Swamy challenges the Deal in Supreme Court of India.
October 1, 2013	SEBI clears the Deal and clarifies that open offer obligations are not triggered by the investment.[24]
October 3, 2013	The Cabinet Committee of Economic Affairs approves the Deal.
November 12, 2013	The Deal is approved by Competition Commission of India.
November 20, 2013	▪ Jet issues the Subscription Shares to Etihad. ▪ James Hogan, CEO of Etihad and James Rigney, CFO of Etihad are appointed as additional directors of the Target. ▪ Board of Jet approves transfer of 'Jet Privilege' programme to its subsidiary Jet Privilege Private Limited as a slump sale.
December 19, 2013	Competition Appellate Tribunal admitted an appeal against the CCI order. Also imposes a fine of Rs. 10 million on Etihad for non-disclosure of certain information about the purchase of slots at Heathrow, London.[25]
May 8, 2014	SEBI finally cleared the Deal holding that no open offer shall be required under the Takeover Code.

19. http://www.bseindia.com/corporates/anndet_new.aspx?newsid=14d52962-d3f5-47f0-964c-58916954eeda.
20. http://www.thehindubusinessline.com/industry-and-economy/logistics/top-brass-of-etihad-jet-meet-chidambaram/article4368907.ece.
21. http://www.thehindubusinessline.com/industry-and-economy/logistics/deal-alive-etihad-buys-jets-3-heathrow-slots-for-70-m/article4458417.ece.
22. http://www.fipbindia.com/admin/case_approval/case07032013.pdf.
23. http://in.reuters.com/article/2013/07/29/jet-etihad-fipb-idINDEE96S08920130729.
24. http://articles.economictimes.indiatimes.com/2013-10-01/news/42576616_1_abu-dhabi-based-etihad-commercial-cooperation-agreement-jet-airways.
25. http://economictimes.indiatimes.com/news/news-by-industry/transportation/airlines-/-aviation/cci-slaps-rs-1-crore-fine-on-etihad-in-jet-airways-deal/articleshow/27661027.cms

3. Commercial Considerations

I. What are the Challenges in the Indian Aviation Industry?

Prior to discussing intricacies of the Deal, it is important to get an overview of the aviation sector in India, which will also help us understand some of the Deal terms.

The domestic carriers in India reported a combined loss of US$ 1.6 billion for the financial year ("**FY**") 2012-13 with more than 40% of the loss accounted during the last quarter (January-March) of the FY.[26] High taxes on fuel, high airport and operational costs continue to plague domestic airlines. Among a comparison of 140 countries, it was seen that Indian ticket taxes and airport charges are 24th highest.[27]

Another major cost component for Indian airlines is the maintenance, repairs and operations ("**MRO**"). Currently there are only 2 MRO facilities in India, which results in most maintenance and operation activities to be conducted outside India.[28] With fees for technical services paid to non-residents being increased from 10% to 25% by the Budget 2013-14, the pressure only mounts on the Indian aviation sector.[29]

High airport costs and inadequate airport space utilization is another concern that needs to be addressed. The rising costs of airports are yet another factor for rise in passenger fares and therefore contribute to the loss making industry. Adding to the woes is the lack of infrastructure and procedural lapses for airport development.[30] Effective from May, 2012, the Airports Economic Regulatory Authority of India increased charges at the Delhi Airport by 346%, which it is estimated will result in a US$ 400 million increase in operating cost for airlines.[31]

In addition, regulatory hurdles have not helped the aviation sector. The airlines operating on the lucrative metropolitan routes are compelled to ply on unviable routes, with the intention of connecting remote areas under the Route Dispersal Guidelines.[32] Further, any airline proposing international operations has to have a track record of domestic operations of at least 5 years.[33]

The Government is also proposing to privatize six airports in India which shall another matter of concern for airlines. It is claimed that private developers might charge increased tariffs which will result in additional operating costs.[34] While the same may be true, it is interesting to note that after the increase in the charges at the Delhi Airport, the Delhi Airport pays 46% of its revenue to the AAI, which is used to subsidize other public sector airports- Chennai (118% increase) and Kolkata (242% increase) are notable examples.[35]

After a rough patch through the previous FY, things are starting to look up for the industry in the upcoming years. The liberalization in Foreign Direct Investment ("**FDI**") in domestic passenger airlines and the exit of Kingfisher Airlines from the market are encouragement to other domestic players to accelerate their market presence.

While, the Tata group has already received approvals for two its two separate joint ventures with AirAsia and Singapore Airlines and the ventures are expected to be operational by the next year[36], there have been talks of an alliance between SpiceJet and Emirates Airways.

II. What was Etihad's Interest in India Prior to the Transaction?

In 2008, Etihad entered into a code-share agreement with Jet for connecting various cities in India to destinations in Europe. Under the code-share agreement, Jet had rights to codeshare flights between India and Abu Dhabi and between Abu Dhabi and Paris.[37] The code-sharing was available from Chennai, Delhi, Hyderabad, Kochi, Kozhikode, Mumbai and Thiruvananthapuram in India.[38] Jet is in the process

26. CAPA Centre for Aviation, South Asia, Yearbook 2013.
27. http://www3.weforum.org/docs/TTCR/2013/TTCR_DataTables10_2013.pdf.
28. http://www1.grantthornton.in//html/tax/budget/2012-13/ind/Budget_2012-13_Impact_on_Aviation_Sector.pdf
29. Section 115A, Income Tax Act, 1961.
30. http://articles.economictimes.indiatimes.com/2012-05-31/news/31922058_1_tax-on-air-tickets-aviation-service-tax.
31. http://www.iata.org/publications/airlines-international/october-2012/Pages/india.aspx.
32. http://centreforaviation.com/analysis/indian-aviation-in-201314-part-2-immense-change-ahead---but-a-policy-vacuum-persists-109703
33. http://articles.economictimes.indiatimes.com/2013-04-26/news/38843427_1_singapore-airlines-civil-aviation-sector-kingfisher-airlines
34. http://www.livemint.com/Politics/xOPT50AjBvBAbLHjf5lHHK/Govt-in-a-rush-to-privatize-six-airports-by-year-end.html
35. http://www.iata.org/publications/airlines-international/october-2012/Pages/india.aspx
36. http://www.thehindu.com/business/Industry/fipb-approves-tata-singapore-airlines-venture/article5267944.ece
37. http://www.rediff.com/money/report/jet-to-expand-code-share-pact-with-etihad-airways/20130610.htm
38. http://www.jetairways.com/EN/IN/AboutUs/CodeShare.aspx

of expanding its code sharing agreement with Etihad to the Mumbai- Brussels- Newark route as well.[39]

Simultaneously with the code-share agreement, Jet and Etihad also entered into an agreement to link their frequent flyers programs.[40] Etihad has now agreed to invest US$ 150 million into Jet Privilege Private Limited ("**JetPrivilege**"), a wholly owned subsidiary of Jet. Post completion of this transaction, Etihad will hold 50.1% of JetPrivilege with 49.9% being held by Jet.[41]

DGCA issued *Guidelines for Grant of Permission to Operate Scheduled International Air Transport Services by the Indian Air Transport Undertakings* dated July 17, 2009 which require Indian air transport undertakings to obtain prior permission of the Central Government (Ministry of Civil Aviation) for entering into any code-share arrangements with foreign airlines and as per which the Indian air transport undertaking is the marketing carrier and the foreign airline, the operating carrier.[42]

III. What is the Importance of Codeshare Agreements for Etihad?

Code sharing agreements have been one of the most important strategic tools used by airlines globally, and Etihad's business strategy is also heavily reliant on such arrangements. It has been reported that as of July 2013, Etihad had 46 codeshare partners, such as Air Berlin, Air France, South African Airlines, Korean Air, amongst a host of other airlines across the globe with a total coverage of approximately 350 destinations.[43]

This network of codesharing arrangements has provided Etihad access to a large number of passengers in various countries. It is interesting to note that with a small fleet of 70 airplanes, compared to that of Emirates and Qatar Airways, Etihad has a larger network of destination than the other two Middle East airlines.[44]

The revenue generated by Etihad through codeshare agreements in the first two quarters of 2013 amounted to US$ 182 million, approximating 20% of its total revenues.[45]

IV. Why did Etihad Infuse Capital into JetPrivilege Despite Having an Alliance with it?

In 2008, Etihad and Jet entered into an alliance by which travelers flying by either Jet or Etihad can claim benefits of the privilege program of the other airline.[46] Jet Privilege, Jet's frequent flyer program is being hived off to JetPrivilege, a wholly owned subsidiary of Jet by way of a slump sale.[47] In order to cement its strategic alliance with Jet, Etihad decided to invest an amount of US$ 150 million for a 50.1% stake in JetPrivilege. This investment is subject to approval of the CCI.

Typically, frequent flyer programs are more profitable than other operations of an airline. For this reason a number of airlines across the globe have been spinning off their frequent flyer programs to separate entities to improve margins through more focused management. Consequently, it is a commercially viable option for Etihad to invest in JetPrivilege, as it is more likely to provide a better return on investment for Etihad compared to its 24% stake in Jet.

V. Why did Jet and Etihad not set up a Joint Venture?

AirAsia Berhad has agreed to set up a JV with Tata Sons Limited ("**Tata**") and Telestra Tradespace Private Limited ("**Telestra**") to set up operations in India. Etihad might also have set up a JV with Jet, like AirAsia's proposed venture. However, acquiring an equity stake seemed as the more commercially viable option for the following reasons:

- Jet and Etihad are both established players in the

39. http://www.livemint.com/Companies/VLhqUlER4jlXpyAJlPO2aO/Jet-to-extend-codeshare-agreement-with-Etihad.html
40. http://www.jetairways.com/EN/IN/PressReleases/Etihad_Airways_and_Jet_Airways_sign.aspx. (last visited on August 19, 2013)
41. http://www.bseindia.com/corporates/anndet_new.aspx?newsid=9f9506a4-daee-4dd5-88dc-710cd396a142
42. http://dgca.nic.in/aic/aic08_09.pdf
43. http://centreforaviation.com/analysis/etihad-reports-another-6-months-record-double-digit-growth-20-of-revenues-from-partnerships-117863
44. http://forbesindia.com/article/boardroom/how-etihad-will-digest-jet/35839/1 (last visited on August 19, 2013)
45. http://centreforaviation.com/analysis/etihad-reports-another-6-months-record-double-digit-growth-20-of-revenues-from-partnerships-117863
46. http://www.etihadairways.com/sites/etihad/global/en/guestrecognition/visitor/etihadguest/PartnerDetails/Pages/JetAirways.aspx and http://www.jetairways.com/EN/IN/JetPrivilege/Partners/Airline/EtihadAirways.aspx
47. http://www.jetairways.com/doc/InvestorRelations/AnnualReport2012-13.pdf and http://www.jetairways.com/doc/InvestorRelations/JAR_2012.pdf

aviation industry. While Etihad has its commercial presence globally, Jet is a dominant player in India, along with substantial global operations. Setting up a new JV would not have been agreeable to Jet, as the primary objective of this deal for Jet was to raise capital for repayment of its existing debt and reduce its interest expenses.[48] Further, setting up a JV would require infusion of capital by Jet, which would have been a tough ask for the debt ridden airline. In the AirAsia-Tata JV, AirAsia is the only airline operator, while Tata and Telestra both did not operate in the aviation sector. Hence a JV makes commercial sense in that case.

- India has a complex web of regulatory approvals that are required for a new company/ venture to commence aviation operations. These include no-objection certificates for scheduled or non-scheduled operators; security clearance for board of directors of ground handling agencies and airline operators; approval for international traffic rights, etc.[49] Being an established player in India, Jet has all these approvals, as a result of which Etihad will not have to wait for commencement of operations post the investment. Since neither Tata nor Telestra had any of these permits, it made more commercial sense for AirAsia to set up a JV. In the alternative, if Tata and Telesta first created an airline operating company, and then AirAsia decided to invest in the newly formed company, the investment would have had to seek approvals for investment post the formation of the company, which would have been a long drawn out process.
- A JV between Jet and Etihad would have been a competitor to Jet in the Indian markets, and to Etihad and Jet in the international markets. The growth of such a JV would have been limited considering the competition between the two JV partners.

VI. What are the Considerations for Etihad for Investing in Jet?

Etihad's investment into Jet was based on a host of Considerations.

i. While India had privatized its aviation sector in 1995, the doors for foreign airlines to make strategic investments were not opened till September 2012. The Government of India amended the FDI policy in in September 2012, permitting foreign investment by foreign airlines into scheduled/ non-scheduled air transport service operators up to 49% under the Government approval route.[50]

ii. Post permission of investment by foreign airlines, rumours of a number of Indian airline operators reaching out to foreign airlines for strategic alliance started. While the FDI policy was revised in September 2012, Jet and Etihad entered into negotiations early in August itself.[51] Etihad had a first mover advantage, and the Jet-Etihad deal became the first investment by foreign airline to invest in an Indian airline. By moving first, it seems Etihad might be able to get a major share of the outbound passengers from India.

Etihad which has grown to be one of the major airlines has relied on an inorganic growth strategy. As compared to Emirates Airline which believes in organic investments by increasing its fleet size, Etihad, with deep pockets, has entered into alliances globally to increase its market share in the global airspace.[52] Some of its significant investments include:

A. Airberlin

Being Etihad's first equity investment into another airline, Etihad and Airberlin entered into a codesharing alliance. Under the codesharing agreements, Airberlin operates flights from Berlin and Dusseldorf to Abu Dhabi and from Abu Dhabi to Phuket in Thailand.

B. Virgin Australia

Etihad had entered into a strategic alliance with Virgin Australia encompassing codesharing on flights, joint marketing initiatives and alliances on the frequent flyer programs. Later, Etihad picked up a 10% stake, and has recently been given approval to pick up another 9.9% stake in the airline.[53]

48. Explanatory statement for the extraordinary general meeting of Jet for approving the issuance to Etihad states the object of the issue as: *"The Board proposes to raise money by issuing shares for various purposes including repayment of debt in order to improve the earnings before interest and tax, enter into a strategic partnership with Etihad giving access to a number of other markets and accordingly expanding the service areas of the Company. Therefore the Board is of the view that given the Company's business plans and the current position of capital markets in India, the Company needs to undertake a capital raising process by way of a preferential issue of shares to Etihad."*
49. For a brief background, please see http://civilaviation.gov.in/cs/groups/public/documents/newsandupdates/moca_000706.pdf
50. http://www.dipp.nic.in/English/acts_rules/Press_Notes/pn6_2012.pdf
51. http://www.livemint.com/Companies/7kAkK9HVCYF7rwejneedeM/How-the-JetEtihad-deal-was-struck.html
52. http://articles.economictimes.indiatimes.com/2013-05-05/news/39027604_1_air-india-emirates-airline-jet-airways
53. http://www.etihad.com/Documents/PDFs/Corporate%20profile/Fast%20facts/june_2013_en.pdf.

C. Air Seychelles

To gain a foothold in Africa, Etihad acquired a 40% stake in Air Seychelles by investing US$ 20 million, along with the Government of Seychelles which invested an equivalent amount. As a part of the investment was a codesharing agreement between the two airlines, by virtue of which Etihad got access to around 100 additional flights per week.[54]

D. Aer Lingus

Picking up a 2.98% stake in the Irish carrier, Etihad entered into codesharing agreement with Aer Lingus. In addition, Etihad has now been permitted to use its code on flights to Boston, Chicago and New York via Dublin.

VII. What are the Benefits being Derived by Jet and Etihad from the Investment?

A. Jet

The most important benefit that Jet shall derive from this deal is the reduction of interest payments on the debt outstanding on its books.

The debt on Jet's books amassed to approximately US$ 2.1 billion in December 2012.[55] The capital infused by Etihad shall be used by Jet to retire some of the outstanding debt on the books of Jet. Jet is currently paying interest payments of approximately US$ 167 million annually.[56] In terms of the total investment that would be received from Etihad, estimates suggest that Jet would be able to retire substantial amounts of debt which would result in cost savings of INR 190-200 crores annually.[57]

In addition to investing funds directly, Etihad is also providing low interest loans to Jet. Jet currently pays an average annual interest rate of 14%.[58] Pursuant to the retiring of the current debt by the low interest loans provided by Etihad, Jet would save approximately US$ 30 million annually on interest alone.[59]

Jet currently flies only to Brussels, Milan and London on its own, while through code share agreements, it can fly to 14 other cities.[60] Etihad, has a much larger international presence, especially in Europe, where it flies to 17 destinations on its own, and to 88 destinations through code share agreements.[61] The deal would give Jet access to Etihad's wide European network.

One of the main concerns for Indian airlines is the huge fuel costs. It is estimated that the deal would result in cost savings of approximately 8-10% in fuel costs. This would be the case especially in long international operations when the flights would now halt at Abu Dhabi.[62]

B. Etihad

Etihad has been on a globalization phase acquiring stakes in airlines globally, as discussed above. It had been looking to expand in the Indian market place, especially considering the competition it has seen in the Indian airspace from Emirates. While Emirates has 13% market share, Etihad has a mere 2% share.[63] Emirates currently flies 185 flights weekly to 10 Indian destinations as compared to Etihad's 59 to 9 destinations.[64]

Tying up with Jet will help Etihad provide passengers a substitute hub at Abu Dhabi as against Emirate's Dubai. Most of the west bound passengers use Dubai as a hub currently. The deal would allow Jet to fly flights directly from 23 locations in India to Abu Dhabi and from there to the European and American destinations.

C. Mutual benefits

Both Jet and Etihad are Going to Mutually Benefit from the Deal

United Arab Emirates ("**UAE**") has agreed to provide the change of gauge facilities to Indian airlines at Abu Dhabi. This will now permit Indian airlines to change

54. http://www.etihad.com/Documents/PDFs/Corporate%20profile/Fast%20facts/june_2013_en.pdf
55. http://articles.economictimes.indiatimes.com/2013-05-02/news/38983515_1_jet-airways-etihad-first-airline
56. http://articles.economictimes.indiatimes.com/2013-04-30/news/38930385_1_jet-airways-etihad-abu-dhabi-based-airline
57. http://content.icicidirect.com/mailimages/IDirect_JetAirways_EventUpdate.pdf
58. http://articles.economictimes.indiatimes.com/2013-04-30/news/38930385_1_jet-airways-etihad-abu-dhabi-based-airline
59. http://articles.economictimes.indiatimes.com/2013-04-30/news/38930385_1_jet-airways-etihad-abu-dhabi-based-airline
60. http://www.sify.com/finance/what-the-jet-etihad-deal-means-news-airlines-neyr8Wccfag.html
61. http://www.sify.com/finance/what-the-jet-etihad-deal-means-news-airlines-neyr8Wccfag.html
62. http://content.icicidirect.com/mailimages/IDirect_JetAirways_EventUpdate.pdf
63. http://www.sify.com/finance/what-the-jet-etihad-deal-means-news-airlines-neyr8Wccfag.html
64. http://www.forbes.com/sites/naazneenkarmali/2013/04/25/etihad-buys-stake-in-indias-jet-airways-amid-protests/

an aircraft without changing the flight number.[65] Under the proposed plan of operations, it seems Jet would use wide body aircrafts to transfer passengers from Delhi, Mumbai and Bengaluru to Abu Dhabi, and use narrow body aircrafts for transport to nearby locations.[66]

The alliance would enable Jet and Etihad to cater to a large number of destinations collectively. Currently, Jet flies to 72 destinations, out of which 20 are international, and Etihad flies to 84 destinations.[67] Cumulatively, post the investment, it is claimed that Jet and Etihad would fly to 140 destinations.[68]

Jet and Etihad would also look at joint purchasing of fuel, spare parts, etc.

65. http://www.thehindu.com/business/Industry/etihad-deal-with-jet-provides-for-stake-increase-in-future/article4653193.ece.
66. http://www.firstpost.com/business/deal-with-etihad-what-it-means-for-jet-airways-724605.html.
67. http://www.telegraphindia.com/1130425/jsp/business/story_16824985.jsp#.Ug9copIweoB.
68. http://www.bseindia.com/xml-data/corpfiling/AttachHis/Jet_Airways_(India)_Ltd_250413.pdf.

4. Legal, Regulatory and Tax Considerations

I. FDI in Aviation - Brief Overview

Until September 2012, while FDI in domestic airlines by non-residents was permitted up to 49% and investment by Non-resident Indians (NRI) was permitted up to 100% under the automatic route, there was a specific prohibition on foreign airlines directly or indirectly investing in domestic airlines.

On September 20, 2012, Government altered its position and allowed foreign airlines to invest, in the capital of Indian companies operating scheduled and non-scheduled air transport passenger services, up to the limit of 49% of their paid-up capital. However, such investment would be subject to certain restrictions.[69] Some of which are as follows:-

- It would be made under the government approval route and hence FIPB approval would be required for any such investment.
- The 49% limit will subsume FDI and FII investments.
- The investments so made would need to comply with the relevant and applicable regulations of SEBI, such as the Issue of Capital and Disclosure Requirements (ICDR) Regulations, Takeover Code as well as other applicable rules and regulations.
- All foreign nationals likely to be associated with Indian scheduled and non-scheduled air transport services, as a result of such investment will require security clearance from Ministry of Home Affairs ("**MHA**") before deployment; and
- All technical equipment that might be imported into India as a result of such investment shall require clearance from the relevant authority in the Ministry of Civil Aviation.

While complying with the above conditions with respect to foreign investment it is also pertinent to note that a permit to operate a Scheduled Air Transport Services/Domestic Scheduled Passenger Airline can be granted only to an airline company satisfying the following conditions:

- *The airline company has to be registered in India, and must have its principal place of business in India;*
- *The Chairman and at least two-thirds of the directors on the board must be Indian citizens; and*
- *The substantial ownership and effective control of which is vested in India nationals.*

II. Why is Etihad only Acquiring 24%, when it is Permitted to Acquire 49% under the FDI Policy?

Investment in Indian airlines is permitted up to 49%. However, Etihad has proposed to purchase only 24% stake in Jet. Under the Takeover Code, an acquirer acquiring 25% or more of voting power of the target company, is required to make an open offer for a minimum of additional 26% shares from public shareholders. Etihad's acquisition of a merely 24% stake is to avoid the open offer obligations under the Takeover Code. Another trigger point for open offer obligations is acquisition of control of the target company.

The intent of Etihad is further manifested by the fact that Jet and Etihad amended the shareholders' agreement on the regulators raising apprehensions that the provisions of the SHA may amount to Etihad acquiring control, thereby triggering open offer obligations.

Further, Etihad's acquisition strategy globally may further substantiate this. Etihad has continuously adopted an approach under which it acquires such number of shares which does not obligate it to make an open offer under the laws of the respective country.

Under German takeover law, any acquirer who acquires direct or indirect control over a listed company is obligated to make an open offer for the acquisition of all shares of the target company. Such control is presumed on the acquirer acquiring 30% of the voting rights of the target company.[70] In December 2011, Etihad increased its stake in AirBerlin, Germany's second biggest carrier from 3% to 29.21%.[71]

Under Australian law, any acquisition of shares of a company is subject to acquirer making an open offer, if the voting power of the acquirer after the acquisition would increase beyond 20% of the voting

69. http://www.dipp.nic.in/English/acts_rules/Press_Notes/pn6_2012.pdf and http://dgca.nic.in/aic/AIC06_2013.pdf
70. Germany, Takeover Guide, http://www.ibanet.org/Document/Default.aspx?DocumentUid=25D0B767-A098-4066-A65E-CD1A95F8A895
71. http://www.bbc.co.uk/news/business-16242121; and http://mb.cision.com/Public/MigratedWpy/80056/9200964/9de52d84d7d62342.pdf

power of the target company. A person can only exceed the 20% threshold on making an off-market open offer to all shareholders for all or a nominated portion of their shareholding, or an unconditional on-market takeover bid on the Australian Stock Exchange.[72] Etihad had increased its stake in Virgin Australia from 5% to 10% in September 2012. It has recently announced that it shall increase its stake in Virgin Australia from 10% to 19.9%, staying clear of the open offer obligations.[73]

III. What Approvals were Required by Jet and Etihad in Connection with the Deal?

While the Deal had its share of heated negotiations and walkouts by the parties, the biggest roadblock in Etihad's entry into India was numerous approvals that were required for the consummation of the Deal. The following approvals were obtained for the Deal.

A. FIPB Approval

As discussed earlier, any investment into a domestic airline by a foreign airline is subject to approval by FIPB. Accordingly, the Target had filed for the requisite approval from the FIPB for the preferential allotment of shares to Etihad. The proposal was first considered by FIPB in its meeting on June 14, 2013 and was deferred due to apprehensions regarding the effective control of the Target passing to Etihad, which would have been a violation of the FDI Policy.[74] While deferring the proposal, FIPB sought clarifications from Jet and Etihad on the ownership and effective control of Jet post consummation of the Deal.

Thereafter, a revised proposal was submitted to FIPB, which after due consideration gave its approval to the Deal in July 2013, subject to the following conditions:

- Any amendment to the shareholders' agreement entered into between Jet and Etihad shall require the prior approval of the Indian Government;
- Any change in Etihad's shareholding will also require approval from the Indian Government;
- The shareholding of Tailwinds has to be transferred to NG;
- All disputes relating to the SHA are to be settled under Indian law, as against English law, as was earlier proposed.

B. CCEA Approval

Under the FDI Policy, any proposal with total equity inflow of more than INR 12,000 million requires the approval of the Cabinet Committee on Economic Affairs (**"CCEA"**), after the same has been approved by FIPB. The Deal was approved by the CCEA on October 3, 2013.

C. SEBI Approval

As per the Regulation 3(1) of the Takeover Code, an acquirer, together with persons acting in concert cannot acquire shares or voting rights in a target company which would entitle them to exercise 25% or more of voting rights in such target company without making a public announcement of an open offer. Further, Regulation 4 of the Takeover Code states that irrespective of any acquisition of shares or voting rights, if the acquirer directly or indirectly acquires control over a target company, then it must make a public announcement of an open offer for the acquisition of shares from the public shareholders. As per the Takeover Code, such open offer must be atleast for 26% of the total shares of the target company calculated as of the tenth date from the closure of the tendering period and after factoring all potential increases contemplated during the offer period.

In the present case, no open offer was made by Etihad as the parties were of the opinion that open offer thresholds under the Takeover Code were not triggered as a result of the Deal.

The Deal was scrutinized by SEBI to verify if Etihad acquired control over the Target or if it was acting in concert with the Promoters for the purpose of the Deal. After various submissions made by the parties to SEBI and amendments to the terms of the Transaction Documents, SEBI observed that the rights proposed to be acquired by Etihad do not *prima facie* appear to result in change of control and thus the provisions of the Takeover Code with respect to open offer do not get attracted.[75] SEBI was also of the opinion that Etihad will not be considered as promoters of the Target. However, SEBI, while giving its nod to the Deal, said it reserves the right to declare Etihad as a promoter if any other regulator or

72. http://www.ibanet.org/Document/Default.aspx?DocumentUid=829DE877-E880-4C5C-B6B1-B27064FD550F
73. http://www.thenational.ae/business/industry-insights/aviation/etihad-airways-to-raise-stake-in-virgin-australia
74. Please refer to Terms of Deal for discussions on FIPB concerns on the clauses in the Transaction Documents.
75. http://articles.economictimes.indiatimes.com/2013-10-01/news/42576616_1_abu-dhabi-based-etihad-commercial-cooperation-agreement-jet-airways

agency decides that Etihad is acquiring control over Jet.[76]

CCI had in its order dated November 12, 2013, which we have discussed in the next section, observed that the governance code under the CCA establishes Etihad's joint control over Jet especially over the assets and operations of Jet. In spite of a request from the parties to rectify this observation claiming that the proposed investment is purely a strategic investment and that Etihad will not acquire any degree of control over Jet, CCI refused to clarify the same.

Subsequent to the concern of the CCI that there seems to be joint control by Etihad over Jet, several reports indicated that SEBI may re-examine its order and also approach the CCI seeking clarity on its order which may require Etihad to make an open offer.[77]

Finally, on February 11, 2014, SEBI served show cause notices ("**SCN**") on the promoters of Jet, namely Naresh Goyal, Anita Goyal and Tail Winds Limited and Etihad ("**Noticees**") alleging joint control over Jet by Etihad under the Takeover Code requiring an open offer under regulation 4 of the Takeover Code by Etihad.

In response to the SCN, the Noticees raised a number of contentions, including, *inter alia*, the following:

- SEBI should not rely on the decision of the CCI since theobjective of the Competition Act, 2002 ("**Competition Act**") (i.e. to regulate combinations which cause appreciable adverse effect on competition in the market) was different than that of the Takeover Code;
- The purpose of the CCA was merely to facilitate exploitation of synergies and expansion of networks, by rationalization of costs and efficiencies of scale;
- Relying on the decision of the Supreme Court in *Daiichi Sankyo v. Jayaram Chigurupati*[78], it was contended that since the CCA is entered into between Jet and Etihad only, it cannot be said that Etihad is a 'person acting in concert' with the target company itself, i.e. Jet;
- Etihad did not have any substantial control rights such as veto or affirmative rights, board or shareholders' meeting quorum rights, any casting vote or any pre-emptive rights on the transfer of shares.

Finally, on May 8, 2014, SEBI held that an open offer would not be required under the Takeover Code[79] SEBI reached this conclusion, *inter alia*, for the following reasons:

- FIPB and CCEA had already approved the Deal, and accordingly, the Deal was in compliance with the FDI Policy, which permitted a foreign airline investing in an Indian airline only if the 'effective control' was vested in Indian nationals;
- The definition of 'control' under the Competition Act deals with 'controlling the affairs and management' is much wider than that under the Takeover Code, which deals with the right to 'appoint majority of the directors' or controlling 'the management or policy decisions', and accordingly CCI's decisions must not be the guiding factor for SEBI;
- There was no commonality of objective to acquire shares or voting rights or control of the target company, as is required to be construed as 'person acting in concert' under the Takeover Code;
- Etihad could not be a 'person acting in concert' with Jet, since the acquirer could not be a 'person acting in concert' with the target company, as held in the Daiichi Sankyo decision of the Supreme Court;
- The lack of any control rights with Etihad, including, *inter alia*, the following:
  - Etihad's right to nominate merely 2 out of 12 directors;
  - Promoters' right to appoint the chairman of the board of Jet, who shall have a casting vote;
  - Etihad not having any veto/ affirmative voting rights;
  - Lack of any quorum rights at the board or general meeting;
  - Lack of any pre-emptive or tag along rights with Etihad.

D. CCI Approval

On November 12, 2013, the CCI approved the Deal removing the last hurdle and paving the way for the first investment by a foreign airline in to an

76. http://www.moneycontrol.com/news/business/analyse-if-jet-etihad-open-offer-was-triggered-cci-to-sebi_1009872.html?topnews=1
77. http://www.moneycontrol.com/news/business/sebi-may-re-examine-its-orderjet-etihad-sources_1008392.html, http://www.taxmann.com/topstories/222330000000002121/sebi-may-again-take-up-open-offer-issue-in-jet-etihad-deal.aspx.
78. AIR 2010 SC 3089
79. http://www.sebi.gov.in/cms/sebi_data/attachdocs/1399545948533.pdf

Indian airline.[80] The issue that arose before the CCI was whether the Deal will cause an appreciable adverse effect on competition (“**AAEC**”) in India under Section 3 of the Competition Act. CCI with a 2:1 majority approved the combination, which crosses the threshold limit under Section 5 of the Competition Act, the CCI has *inter alia* considered the impact of the alliance on the competition in the India-Abu Dhabi route and on the Indian aviation sector.

i. Relevant Market

As Etihad does not provide services for transportation of passengers within India, CCI held international air passenger transportation from and to India to be the relevant market for the combination.

ii. Determination of AAEC

In order to assess the impact of the transaction on competition in India, the CCI determined the relevant market for passenger air transport services based of point of origin or point of destination (“**O&D**”) pair approach on a non-directional basis. Basing its analysis on the O&D pairs, it also factored in the duration of the flight, connecting time, schedule, price and time-sensitivity of the consumers, and availability of alternate routes to the consumers. Following were the important factors considered by CCI in approving the deal:

a. Market Share

The CCI noted that Jet has about 20% market share in the India-UAE sector and Etihad about 5%. On the combination, these two airlines will stop competing with each other and would be able to provide better services. Further it pointed out that there are 38 routes to/from India to other destinations where Etihad and Jet fly and there is at least one competitor on each route. Of all these routes, Jet and Etihad have a combined market share of 50% in only 7 of these routes and of these 7, on 3 routes either Jet or Etihad have a market share of less than 5%. Thus post transaction the market share would only be marginal and not affect competition and on analyzing several routes the CCI concluded that on all routes there are other players which ensure that consumers can make choice between airlines.

b. Network Effects

CCI in its order emphasized that the O&D approach is itself not sufficient for assessing the competition so due consideration has to be given to the network effects of the competition which includes competition between airline hubs. In addition to studying the market share between cities in India to the hub, CCI also analysed the competition in the onward bound traffic and systems. In this case, a linked hub-and spoke airlines network form an integrated system of complementary routes which increases efficiency. It clarified that high market share would not indicate absence of competition as competition would still be present from alternative networks and alliances/systems, especially for the west-bound traffic to North and South America.

c. Abu Dhabi as the Exclusive Hub

One of the main conditions in the Transaction Documents require Jet to use only Abu Dhabi as an exclusive hub for services to and from Africa, North & South America and UAE and restricts Jet to code share with other airlines in certain O&D pairs. Jet will have to cancel its code share with other airlines and flow its traffic through Abu Dhabi. But since there is stiff competition from other players on these routes, CCI was not concerned with these code share agreements leading to abuse of dominance. The combined market share of Jet and Etihad on a majority of these O&D pairs is less than 30%.

Further since this relationship between Jet and Etihad results in more choices to the Indian consumer as the Jet flights from multiple points in India operate to Abu Dhabi and then continue to other places in Middle East and North and South America which thus allows more connectivity as they create a whole new host of city pairs.

Also Abu Dhabi’s proximity to India will allow for deployment of smaller and narrower body aircraft in which larger wide body aircraft would have been unviable. So Jet would be able to sustain larger traffic on the routes from Delhi and Mumbai to North America which would increase capacity and choice available to the Indian consumers.

iii. Rectification of Order

Subsequent to the CCI order, the parties made a request to CCI to clarify that the proposed investment by Etihad into Jet is purely strategic investment and Etihad will not acquire any control over Jet. However the CCI did not rectify the order and clarified that the investment amounts to joint control.[81]

80. http://www.cci.gov.in/May2011/OrderOfCommission/CombinationOrders/C-2013-05-122%20Order%20121113.pdf

81. http://www.cci.gov.in/May2011/OrderOfCommission/CombinationOrders/C-2012-05-122%20261113.pdf.

E. Ministry of Civil Aviation/DGCA

The Directorate General of Civil Aviation ("**DGCA**") established under the Ministry of Civil Aviation is the main regulatory body that supervises civil aviation in India.

i. Approval for Change in Management

The DGCA has issued certain minimum requirements for grant of permission to operate scheduled passenger air transport services according to which prior permission of the DGCA/ Ministry of Civil Aviation is required *inter alia* for any change in the management of the Company arising out of changes in the equity holdings of the Company.[82] Therefore approval from the DGCA was required for the appointment of the directors nominated by Etihad on the board of Jet.

ii. Change in Control

The Guidelines for Foreign Direct Investment in the Civil Aviation Sector dated June 30, 2008 ("**CA FDI Guidelines 2008**"), prescribed that a domestic airline will not enter into any agreement with a foreign airline which gives such foreign airline effective control in the management of the domestic airline or right to interfere in the management of the domestic airline. These restrictions were in line with the FDI policy prevailing at the time, which necessitated keeping out the foreign airline out of the management of the domestic airline. The CA FDI Guidelines 2008 were superseded by Guidelines for Foreign Direct Investment in the Civil Aviation Sector dated March 1, 2013 ("**CA FDI March 2013 Guidelines**"). Under the CA FDI March 2013 Guidelines, while the restriction on entering into an agreement by virtue of which the foreign airline has the right to interfere in the management of the domestic airline still exists, the restriction on agreements by which the foreign airline is empowered to have effective control in the management of the domestic airline has been deleted.

CA FDI March 2013 Guidelines were superseded by Guidelines for Foreign Direct Investment in the Civil Aviation Sector dated October 1, 2013 ("**CA FDI October 2013 Guidelines**"). Under the CA FDI October 2013 Guidelines, the restriction on entering into agreements by which foreign airline has the right to interfere in the management of the domestic airline has been substituted to state that the domestic airline shall not enter into an agreement with any foreign airline which may give the foreign airline the right to control the management of the domestic airline.

iii. Lending Arrangements

The CA FDI Guidelines 2008 stated that a domestic airline may enter into any financial agreement with a foreign airline for the purpose of lease-finance, hire- purchase or other loan arrangements, while such agreements were not permitted with foreign airlines. The CA FDI March 2013 Guidelines, as well as the CA FDI October 2013 Guidelines, permit such agreements with foreign airlines.

IV. What was Controversy Around the Bilateral Air Services Agreement ("BASA") Executed Between India and UAE?

Bilateral Agreements[83] are negotiated and *inter se* entered into by countries to benefit from mutual commercial activity. In order to strengthen economic ties and promote co-operation for mutual commercial activities, India has entered into a number of Bilateral Investment Treaties ("**BIT**") with various countries.

On April 24, 2013, India and UAE (Abu Dhabi) signed a BASA to expand the air transport services between them.

Under the current existing BASA between India and UAE (Abu Dhabi), both sides have a capacity of 13,330 seats per week, increased by 2% of flexibility.[84] In the recent negotiations, UAE had requested for 40,000 additional seats per week, and also requested for additional points of call at Goa, Pune, Amritsar and Lucknow. India had sought change of gauge facility at Abu Dhabi for Indian carriers.

Under the revised BASA, both parties have agreed to provide for 36,670 additional seats per week. The 2% flexibility has been done away with, and no additional points of call have been granted to UAE. India has been granted the change of gauge facility as sought. In addition, both parties also agreed to extend third country and domestic code sharing of airlines in both countries.[85]

82. http://dgca.nic.in/rules/car-ind.htm.

83. As the name suggests, a 'bilateral' agreement is an agreement between two parties, herein between two countries, which lays down provisions for mutual dependence and gain from certain resources and ensures co-operation in trade (exchange of goods and services) between such signing countries.

84. http://www.pib.nic.in/newsite/erelease.aspx?relid=95006

85. http://www.pib.nic.in/newsite/erelease.aspx?relid=95006

BASA raised several issues in India as it was signed only a few hours before the decision by Etihad to invest in Jet. It has been alleged that the Abu Dhabi officials made it clear, that unless their carrier, Etihad got a major share of the seats, they would not allow the deal between Jet and Etihad to proceed.[86] Thus it is claimed that it was entered into for the purpose of enabling one airline to strike a deal with a foreign airline at a huge premium.[87]

A special leave petition (**"SLP"**) has been filed in the Supreme Court alleging lack of transparency in the manner in which the BASA was executed by Indian officials. The SLP is currently pending before the Supreme Court, and the Supreme Court has in December 2013 clarified that the Deal may be quashed if it is discovered that there were irregularities in the execution of BASA.[88]

V. What are the Tax Implications of the Deal?

A. On Etihad and Jet

As the issuance of shares is by way of preferential allotment there will be no tax incidence on the parties.

B. On Tailwinds

Since the transfer of securities from Tailwinds was by way of block deals on the stock exchange and by way of an offer for sale on the floor of the stock exchange, Tailwinds shall not be liable to pay any capital gains tax, but only securities transaction tax at the rate of 0.1%.

86. http://www.firstpost.com/business/decoding-the-jet-etihad-seat-entitlement-controversy-921277.html

87. http://www.livemint.com/Politics/ZBVbsyzITJlVED4ynmX8OK/IndiaAbu-Dhabi-agreement-may-have-clinched-JetEtihad-deal.html

88. http://articles.economictimes.indiatimes.com/2013-12-07/news/44865551_1_jet-etihad-airways-deal-subramanian-swamy-aviation-sector].

5. Epilogue

The Deal presents a win-win situation for the parties, and the consumers. For Jet, which had in recent times lost its numero uno position in the Indian skies to the low cost Indigo Airlines, this Deal comes as a lifeline to revive its position in the market. Additionally it would be able to reduce its debt levels by around 30% which would result in saving significant interest costs. It would also benefit from the management expertise brought in by Etihad in increasing its efficiencies of operation. For Etihad, the Deal provides access to a large market of consumers in the Tier II and Tier III cities in India where Jet operates. The consumers will also benefit from the improved connectivity and better services at affordable prices. It remains to be seen whether Etihad's entry as a co-pilot will ensure safe landing for Jet in future.

As you are aware, we have always taken initiatives to provide updates and analysis on the latest legal developments. M&A Lab is one such initiative which provides insight and analysis of the latest M&A deals. We believe in knowledge sharing and hence would appreciate any feedback or comment. Feel free to direct your comments/views on this Lab to-:

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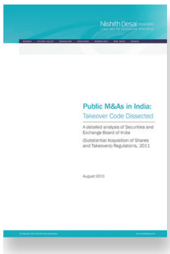
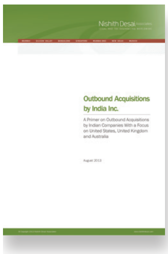


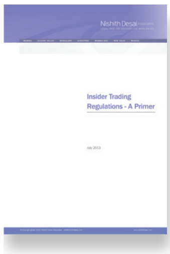
Takeover Code Dissected

August 2013



Outbound acquisitions by India Inc

August 2013



Insider Trading Regulations

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Mergers & Acquisitions in India

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Warburg-future capital deal dissected

January 2013

Cairn-Vedanta deal dissected

January 2012

Patni plays to iGate's tunes

January 2012

Fund structuring and operations

March-2014

Doing Business in India

May 2014

NDA Insights

TITLE	TYPE	DATE
File Foreign Application Prosecution History With Indian Patent Office	IP Lab	02 April 2013
Warburg - Future Capital - Deal Dissected	M&A Lab	01 January 2013
Public M&A's in India: Takeover Code Dissected	M&A Lab	August 2013
Copyright Amendment Bill 2012 receives Indian Parliament's assent	IP Lab	September 2013
Real Financing - Onshore and Offshore Debt Funding Realty in India	Realty Check	01 May 2012
Pharma Patent Case Study	IP Lab	21 March 2012
Patni plays to iGate's tunes	M&A Lab	04 January 2012
Vedanta Acquires Control Over Cairn India	M&A Lab	03 January 2012
Corporate Citizenry in the face of Corruption	Yes, Governance Matters!	15 September 2011
Funding Real Estate Projects - Exit Challenges	Realty Check	28 April 2011
Real Estate in India - A Practical Insight	Realty Check	22 March 2011
Hero to ride without its 'Pillion Rider'	M&A Lab	15 March 2011
Piramal - Abbott Deal: The Great Indian Pharma Story	M&A Lab	05 August 2010
Bharti connects with Zain after two missed calls with MTN	M&A Lab	05 June 2009
The Battle For Fame - Part I	M&A Lab	01 April 2010
Great Offshore Takeover Saga - Bharati Shipyard v/s ABG Shipyard	M&A Lab	16 December 2009
Second missed call: Bharti Airtel fails to reconnect with MTN	M&A Lab	09 October 2009

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Research is the DNA of NDA. In early 1980s, our firm emerged from an extensive, and then pioneering, research by Nishith M. Desai on the taxation of cross-border transactions. The research book written by him provided the foundation for our international tax practice. Since then, we have relied upon research to be the cornerstone of our practice development. Today, research is fully ingrained in the firm's culture.

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