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THE INVISIBLE ASSET: WHY INDIAN M&A LAW IS UNPREPARED FOR AI ACQUISITIONS?

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I. INTRODUCTION: A TRANSACTION THAT BREAKS THE TEMPLATE

In 2023, Microsoft concluded its takeover of Nuance Communications for around $19.7 billion, amount that baffled conventional accounting measures.[1] The asset base of Nuance did not consist of its factories, properties, or even the patented technology it held. Rather, the value of the company was in its huge data sets of speech from clinics and the neural network weights generated from them. No independent auditor had put a price tag on this model. No regulatory authority had studied the competitive implications of using this technology in healthcare. The transaction took place, and a market was changed.

Today, India is also witnessing its own phase of AI acquisitions. In these acquisitions, domestic corporate giants, foreign multinational companies operating from India, and startup ventures financed by venture capitalists have been involved in transactions where the value comes from assets consisting of artificial intelligence. However, the Indian legal system still assesses the transaction on the basis of a valuation methodology that belongs to another age where the valuation of assets consisted of revenues multiples, and intellectual property meant registered patents and trademarks.

The Competition Commission of India (CCI), exercising its powers under the Competition Act, 2002, invokes jurisdiction in transactions that meet certain asset and turnover tests.[2]

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[1] See Microsoft Corp., Form 10-K (Annual Report), at 7 (2023); see also Bret Swanson, The $19.7 Billion Question: What Did Microsoft Really Buy?, Discourse Mag. (Apr. 14, 2023), https://www.discoursemagazine.com (discussing valuation of AI speech assets).

[2] Competition Act, 2002, § 5, No. 12 of 2003 (India) (setting asset and turnover thresholds triggering mandatory notification to the Competition Commission of India).

However, in this context, the flaw is fundamental. An AI firm capable of fundamentally altering the market can have virtually no assets on the books and no revenues at all if it is yet to launch. The whole regime of India's merger control system can be sidestepped in exactly those circumstances where it will matter most for the health of competition in the market.

The paper is divided into four sections. Section II discusses the limitations of current Indian legal frameworks in analysing AI acquisitions. Section III considers the three invisible assets entrained models, proprietary data, and human capital that current laws fail to take into account. Section IV analyses the various comparative approaches that could be adopted by India.

II. THE STRUCTURAL INADEQUACIES OF INDIA'S M&A FRAMEWORK

A. THE COMPETITION ACT'S THRESHOLD PROBLEM

Under Section 5 of the Competition Act, 2002, the merging parties must inform the CCI if the aggregate worth of their assets surpasses the ₹2,000 crore mark in India or ₹8,000 crore mark internationally, or if the turnover limits are breached.[3] Such figures were set considering capital-heavy industries. The thresholds were inherently oblivious to any intangibility of value.

Take, for example, a startup company in Bengaluru which created a huge language model trained on Indian legal texts. It had a team size of thirty people, ₹50 lakh worth of assets on it books, and zero turnover as it had not yet started commercial operations. The firm was purchased by a global technology conglomerate for ₹3,000 crore. The deal did not meet the asset limit under Section 5, bypassing any CCI examination and ensuring the competitive moat remains lopsided.[4] The problem is neither theoretical nor imaginary; it is practical and occurring.

Section 17 of the Competition (Amendment) Act, 2023 has included a "deal value" criterion, whereby transactions having a value greater than ₹2,000 crore involving a target with "substantial business operations" in India need to be notified.[5] While this has been a much-

[3] Id. § 5(a)–(c) (prescribing ₹2,000 crore domestic asset threshold, ₹8,000 crore global asset threshold, and corresponding turnover thresholds for enterprises and groups).

[4] . See NASSCOM, India AI Startup Ecosystem Report 2023, at 22–24 (2023) (noting that a significant proportion of AI acquisitions in India involve pre-revenue targets with minimal book-value assets).

[5] Competition (Amendment) Act, 2023, § 6(a), No. 22 of 2023 (India) (inserting a deal-value threshold of ₹2,000 crore for transactions where the target has substantial business operations in India); see also Competition Commission of India, Draft CCI (Combinations) Regulations, 2023

needed change, its execution has uncovered a further issue, in that there has been no precise definition of what constitutes "substantial business operations" by either the amended legislation or the draft guidelines issued by the CCI, especially for a software model.

B. COMPANIES ACT AND DISCLOSURE DEFICITS

Procedural architecture relating to the mergers and acquisitions of Indian companies is governed by the Companies Act, 2013, and Sections 230 to 240 define the scheme of arrangements, with court or tribunal approval being necessary along with obtaining fairness opinions.[6] Nevertheless, the disclosure provisions of the Act, which are founded upon the principles of financial statements prepared according to Indian Accounting Standards (Ind AS), do not provide any way to determine the value of AI assets.

As per Ind AS 38 on Intangible Assets, if an internal generation of an AI system takes place, the same cannot be recognised in the research stage. Further, even during the development stage of such internally generated AI system, its recognition depends on establishing a future economic benefit, which in most cases will not be possible for foundational AI assets during acquisition.

C. SEBI'S TAKEOVER CODE AND THE VALUATION VACUUM

The SEBI Substantial Acquisition of Shares and Takeovers Regulations, 2011 (also called the Takeover Code) becomes applicable when there is an acquisition by other firms of listed companies.[7] Open offer provisions kick in at particular shareholding levels and are made at prices which are the highest between the market price and the book value. In the case of a listed firm engaged in artificial intelligence business, whose market value includes speculative AI value which has no relationship whatsoever with the asset base, the protection provided by the provision is more theoretical in nature.

III. THE THREE INVISIBLE ASSETS

A. TRAINED MODELS: THE UNREGISTERED CROWN JEWEL

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[6] Companies Act, 2013, §§ 230–240, No. 18 of 2013 (India) (governing mergers, amalgamations, arrangements, and reconstructions, including the requirement of National Company Law Tribunal approval and fairness opinions).

[7] SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, regs. 3–4 (prescribing open-offer obligations triggered at 25% shareholding and pricing methodology based on volume-weighted average market price or negotiated price, whichever is higher).

The AI model itself, its weightings, architecture, and fine-tuning setup is, arguably, the single biggest commercial asset of an AI acquisition. However, there is no place for it in India's intellectual property regime.[8] Under the Copyright Act, 1957, the source code might be subject to copyright protection, but the weightings are not code; they are numeric arrays that result from the process of training. Patent protection, in theory, could cover such an invention, but in practice, it is out of reach, under the Patents Act, 1970, mathematical methods and computer programs as such cannot be patented.

The effect on valuation is immediate. The absence of any legal tool to establish ownership means that the due diligence process cannot, in good faith, confirm that the buyer will receive what he is paying for. The weightings of a model can be duplicated; its training pipeline cloned by defected engineers. The deal closes under the impression that the crown jewels are being handed over but there is no legal way to make sure that happens.

B. PROPRIETARY DATA: THE INPUT THAT BECOMES THE OUTPUT

Proprietary datasets, in most instances, represent the actual competitive moat of the AI enterprise. While the algorithm may be replicated, the data, the result of countless hours of human labelling, years of expertise and even private personal records cannot be.[9] However, data is not recognized as a form of property by Indian laws. Both the Information Technology Act, 2000 and the Digital Personal Data Protection Act, 2023 (DPDPA) do not grant any proprietary right over data they govern, not the commercial aspects of the asset.[10]

Although the DPDPA sets out certain duties related to the processing of personal data, it does not address how the purchase of a company in possession of substantial amounts of personal data should take place, what needs to be declared about the transaction, and if it presents an anticompetitive concern. The purchase of a business that controls behavioural patterns of one hundred million Indian individuals represents a very valuable asset for the acquirer. Yet, the legislation neither accounts for its value nor analyses potential harms of its concentration.

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[8] See Arun Mohan Sukumar, Regulating AI in India: A Framework for Emerging Technologies, Observer Research Foundation Occasional Paper No. 302, at 15–17 (2021) (noting the absence of dedicated intellectual property protection for AI model weights under Indian law).

[9] See Stucke & Grunes, Big Data and Competition Policy 143–57 (2016) (arguing that proprietary datasets function as barriers to entry and can entrench dominant positions in data-driven markets).

[10] Digital Personal Data Protection Act, 2023, No. 22 of 2023 (India); Information Technology Act, 2000, No. 21 of 2000 (India). Neither statute characterises data as a form of property capable of ownership, transfer, or valuation in the ordinary commercial sense.

C. TALENT AND THE KNOWLEDGE-PERSON PROBLEM

The value created by most firms lies in the intellectual property that resides in the minds of the most important individuals at the company, namely those who have built up a body of intuition and know-how around architectural design, training, and emergent behaviour that can never be fully written down.[11] Acqui-hires are fairly common in the AI industry, which are acquisitions mainly based on the hiring of talent, not the product. Indian law does not know the concept of such deals. Under both the Companies Act and the Competition Act, the person making the deal is irrelevant, and all the focus is on the company.

This has legal consequences because, in practice, the consequence is a failure to disclose risks. If a company makes an asset purchase worth ₹500 crore for an AI team of twelve people, nobody will think about the risk that six of these twelve could quit the company within two years, thereby nullifying the entire value of the deal. There is nothing in SEBI guidelines regarding this aspect.

IV. WHAT OTHER JURISDICTIONS ARE DOING

India is not the only country facing this issue, and there is merit in examining how other, more mature legal systems address this issue, with a definite focus on what works and does not work when transplanting the approach into the Indian framework.[12]

The European Union can be used as an example. In its dealings under the EU Merger Regulation, the European Commission has come to adopt a “significant impediment to effective competition” (SIEC) test that considers the impact of data collection and algorithmic market power, beyond just looking at market share.[13] For instance, in its probe into Microsoft’s

[11] See Hanna Krasnova et al., Acqui-hiring in the AI Industry: Motives, Mechanisms and Market Effects, 45 J. Info. Tech. 201, 207–10 (2023) (empirically documenting that talent acquisition is the primary stated motive in a majority of AI-sector acqui-hires).

[12] On the limits of legal transplantation, see Alan Watson, Legal Transplants: An Approach to Comparative Law (2d ed. 1993); see also Ralf Michaels, Comparative Law by Numbers, 58 Am. J. Comp. L. 765, 790–95 (2010).

[13] Council Regulation (EC) No 139/2004 of 20 January 2004 on the Control of Concentrations Between Undertakings (EU Merger Regulation), art. 2 (establishing the "significant impediment to effective competition" test); European Commission, Case M.10646 – Microsoft/Activision Blizzard, Commission Decision (Feb. 22, 2023) (examining data accumulation effects on AI product development as part of competition analysis).

takeover of Activision Blizzard, the Commission analysed how gaming data could be used in AI product development, something which Indian competition laws do not have.

In the US, the 2023 Merger Guidelines of the Federal Trade Commission and Department of Justice have provided a methodology for determining whether acquisitions may be deemed to "entrench or extend a dominant position" by virtue of their AI capabilities.[14] On the other hand, the FTC has been examining so-called "killer acquisitions" in tech, whereby the buyer does not intend to innovate on the acquired product but rather kill it. Likewise, in AI, a big player acquiring a small AI start-up is simply trying to ensure that this start-up does not emerge as a potential rival.

The UK system post-Brexit, too, merits Indian attention. The Competition and Markets Authority employs the share of supply test, rather than merely revenue or asset tests, which enables it to claim jurisdiction even where the target provides, in any form whatsoever, a significant portion of goods and services within the UK. Such a functional approach may similarly be applied to AI model capabilities.

V. REFORM PROPOSALS

A. A DEAL-VALUE THRESHOLD WITH AI-SPECIFIC GUIDANCE

Threshold based on deal value under the Competition (Amendment) Act, 2023 is certainly a step in the right direction. What is needed here is subordinate legislation that translates the policy into actionable practice for AI deals.[15] The CCI must bring out regulations stating that in every deal where the target company operates as an AI business, the 'value' in relation to which threshold will be calculated comprises (i) the costs of replicating the trained AI models, which would be estimated computationally; (ii) proprietary datasets whose market value will be assessed according to a method to be laid down; and (iii) the annual pay of key technical staff members.

B. A MANDATORY AI ASSET REGISTER IN DISCLOSURE DOCUMENTS

[14] U.S. Dep't of Justice & Fed. Trade Comm'n, Merger Guidelines 13–15, 27–29 (2023) (articulating framework for assessing whether acquisitions entrench or extend dominance through technological capabilities including AI).

[15] Competition (Amendment) Act, 2023, § 6(a); see also CCI, Draft Regulations on Combinations (2023) (open for public comment), which as of the time of writing had not finalised guidance on intangible asset valuation for AI companies).

SEBI should amend its disclosure requirements under the LODR Regulations and the Takeover Code to mandate an "AI Asset Register" as part of any material transaction disclosure.[16] This register should identify all trained models being transferred, the datasets used in their training, any licensing restrictions on those datasets, the nature of any third-party model dependencies (including open-source models with licence obligations), and key-person concentration risk. This is analogous to the intellectual property schedule already required in M&A due diligence.

C. CCI SECTOR-SPECIFIC GUIDELINES FOR AI MARKETS

The CCI has historically provided sector-specific guidance for industries like pharmaceuticals and media.[17] The CCI should provide such sector-specific guidance to clarify its approach to evaluating market power within sectors connected to AI, specifically in markets for foundation models, markets for AI applications, and the cloud computing and specialized chips layer. Such guidance should clearly explain that data hoarding is a factor that can help establish market power, determine when commitments regarding data access and model interoperability will be sought, and demonstrate the CCI's readiness to investigate acqui-hires.

D. AMENDING IND AS 38 FOR AI-ERA INTANGIBLES

Ind AS 38 needs to be reviewed by the Ministry of Corporate Affairs in collaboration with the Institute of Chartered Accountants of India, to come up with an independent recognition and measurement standard for AI models and proprietary data sets.[18] The IASB is currently deliberating on the same reforms at the international level, and India must contribute to the process, adopting its own standard as appropriate based on international convergence and the unique nature of the Indian AI economy, where many of the most valued AI firms are still pre-commercial when they are acquired.

VI. CONCLUSION

[16] SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, reg. 30 (India) (requiring listed entities to disclose material events; SEBI circular SEBI/HO/CFD/CFD-PoD-1/P/CIR/2023/123 expanding disclosure requirements, though not yet specifically addressing AI asset registers).

[17] See CCI, Guidance Note on Merger Control (2019) (providing sector-specific observations on pharmaceutical, media, and financial-services transactions); CCI, Market Study on the Telecom Sector (2021).

[18] See Inst. of Chartered Accountants of India, ICAI Exposure Draft – Amendments to Ind AS 38 Intangible Assets (2022); International Accounting Standards Board, IASB Work Plan: Intangible Assets Research Project (2023) (noting that the IASB has placed a project on intangible-asset recognition on its research agenda, with particular relevance to AI and digital assets).

The core question posed by this paper is straightforward but far from simplistic: if the single most important asset a business possesses cannot be found on its balance sheet, listed in its regulatory reports, or analysed using the tools of competitive regulation, how much of the deal is actually within the domain of the law? In India, the truth is that for AI acquisitions, the response would be: not enough.

This is not a defeatist position. Indian law has shown itself capable of adapting to revolutionary changes in economics before; the reforms of 1991 necessitated a full-scale restructuring of competition law, leading to the creation of the Competition Act, 2002. It is time for another such revaluation, and this time the resources under consideration are no longer factories or markets but the skills and abilities captured by numbers and determining which businesses can and cannot compete in the world of AI.

The institutional infrastructure required to develop an outstanding legal framework for AI-driven M&As already exists in India - CCI, SEBI, NCLT, and IBBI. The problem with which India is faced is the lack of the necessary doctrinal framework that would allow the above institutions to be used for their optimal functioning. These proposals are not idealistic; they are rather realistic and incremental changes based on what we have now.[19] Moreover, the invisible asset will become even more valuable in the future.

[19] On the role of institutional capacity in competition law reform in developing economies, see Eleanor Fox & Mor Bakhoum, Making Markets Work for Africa: Markets, Development, and Competition Law in Sub-Saharan Africa 55–68 (2019) (noting that effective competition regimes depend on both doctrinal adequacy and institutional deployment capacity).