DENEYS REITZ
M&A AND COMPETITION
LAW SEMINAR
July 2009

MERGER DEVELOPMENTS – RISKS AND RELIEF

This paper will be looking at recent Competition laws developments in relation to mergers in South Africa, and the implications for companies considering entering into mergers.

Until the recent global economic downturn, the high rate of economic activity worldwide meant that the merger division of the Competition Commission ("the Commission") was kept extremely busy. As the global economy kept growing, the number of merger notifications increased every year and the Competition Commission was swamped with filings. Indeed, the Commission was receiving well in excess of 400 merger notifications per annum.

However, the Commission was also seeking to change its focus, and therefore its resources, from merger analysis to enforcement in respect of prohibited practices. To reduce the merger workload in these circumstances, the solution was found in significantly raising the merger thresholds, which had remained unchanged for the last eight years.

Until recently, a merger had to be notified if the target's assets or turnover amounted to R30 million or more, and the combined assets/turnover of the acquirer and target were R200 million or more. With effect from 1 April 2009, the threshold for a notifiable intermediate merger became R80 million in respect of the target's assets or turnover, and R560 million in respect of the combined assets or

turnover of the acquirer and target. As regards large mergers, the thresholds have increased to R190 million (from R100 million) for the target's assets or turnover, and R6,6 billion (from R3,5 billion) in combined assets and/or turnover. Filing fees have also increased.

This increase in thresholds has not surprisingly led to a significant drop-off in merger notifications to the Competition Commission. At the same time, market conditions have led to a drop-off in merger activity. Although things may be picking up, this year market participants have noticed a significant downturn in the number of mergers being mooted, both here and overseas.

Because merger activity is down, the Commission has more capacity to analyse mergers. Whilst this may lead to a more rapid analysis of non-problematic mergers, they will have more capacity to closely scrutinise problematic mergers.

The Commission has also signalled that it will be keeping an eye out for mergers that would formerly have required notification, but because of the increase in thresholds are now small mergers that are not automatically notifiable. Normally, the competition authorities are only interested in small mergers if they cause competition or public interest concerns. In that event, they have a period of six months from the implementation date within which to call on the parties to notify the transaction and to cease implementing it further until they obtain clearance. Now, they have issued guidelines indicating that they will still require notification, even thought the transaction is a small merger, if at the time of entering into the merger transaction any of the parties to the merger (or entities within their group) are subject to an investigation in respect of alleged prohibited practices, or if they are respondents in pending Tribunal proceedings pursuant to a referral of a complaint by the Commission. Thus companies with activities in a number of sectors will have to notify all small mergers they undertake, if they have activities in a sector under scrutiny, even if those small mergers involve sectors which are not under scrutiny and which raise no competition or public interest concerns. Whilst one may debate the Commission's powers to make such requirements, it is clear that the Commission will be looking out for such transactions, and parties must consider carefully how to deal with such mergers.

This guideline highlights another noticeable trend in relation to merger notifications – the Commission is using its merger investigations to gain more information in relation to sectors in which it is interested. Parties will find themselves being asked questions that are not directly relevant to the merger, but that enable the Commission to broaden their understanding of the sector in

question. Competitors in those sectors are also finding themselves having to answer extensive questionnaires regarding these transactions. It is noteworthy that the cartel investigations into the reinforcing steel, wire and pipes industries had their origin in merger investigations. Clearly, information obtained in those merger filings and investigations led the Commission to conclude that anticompetitive practices were taking place there.

Parties should take note of the sectors that the Commission has on numerous occasions indicated it is focusing on – infrastructure and construction; food and agro-processing; intermediate industrial products; and financial services. Market participants in those areas should be particularly cautious before entering into merger transactions.

In this economic downturn, parties are no doubt merging in distressed circumstances. However, they should not conclude that the "failing firm" defence will be a panacea for all ills. The Tribunal indicated its approach to such transactions some years ago, when Iscor, as it then was, acquired Saldanha Steel. It indicated that the fact that a firm is "failing" is not so much a defence to rely on in obtaining clearance of an otherwise anticompetitive merger, as a factor to be taken into account in the normal merger analysis. They will still require evidence that no other more suitable buyer can be found, and that the failing firm cannot otherwise be saved, by restructuring for example. It is however to be hoped that the authorities will recognise in such circumstances that time is of the essence, and will expedite their review process accordingly.

There is likely to be significant consolidation of businesses as a strategy to stay afloat. As a result, mergers could lead to a significant lessening of competition in the market and parties might seek to rely on public interest issues such as the saving of jobs as a motivating factor for gaining approval of otherwise anti-competitive mergers. However, it should again not be assumed that such mergers will be approved.

Potentially anti-competitive deals will have to be carefully structured in order to obtain clearance. Objecting parties can intervene in large mergers, and potentially delay and even derail transactions which have been some time in the planning unless potential objections are met in advance (for example, by selling off a part of the business which would otherwise be excessively concentrated post-merger).

With more time on their hands, the Commission investigators will also be trawling the newspapers to keep an eye out for transactions which appear to them to be notifiable mergers. Bear in mind that

parties may not implement a notifiable merger without clearance, and failure to comply could lead to significant fines, or even divestiture. The Tribunal may impose a fine of up to 10% of turnover on offending parties. Until now, the fines have not been based on percentages of turnover at all, but the Commission has signalled that this is changing, and one can expect to see significant fines for prior implementation in future.

In summary, the Commission will be alert to merger activity that may lead to anticompetitive outcomes, and will have more time to scrutinise mergers thoroughly to find flaws in the transaction. They will also be keeping an eye out for small mergers which no longer require notification but which are in sectors in which they are interested or raise the concerns.

The Commission will be looking for signs of anticompetitive behaviour in the activities of merging parties. It is also likely to divert analysts who until now have investigated mergers into the enforcement division, where they will channel their energies examining anti-competitive behaviour and cartel investigations. Businesses would be wise to ensure compliance with the law, and if they are thinking of entering into a merger, they should consult our competition law practitioners early on to avoid difficulties in obtaining merger clearance.

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