LAW SOCIETY OF SOUTH AFRICA

SUBMISSIONS TO

THE SELECT COMMITTEE ON BUSINESS AND ECONOMIC DEVELOPMENT

OF THE NATIONAL COUNCIL OF PROVINCES

ON THE B VERSION OF THE COMPETITION AMENDMENT BILL [B23B–2018]

DATED 16 OCTOBER 2018

IN RELATION TO AMENDMENTS TO THE COMPETITION ACT NO. 89 OF 1998

1. INTRODUCTORY REMARKS

1.1 On 11 July 2018, the Minister of Economic Development tabled the Competition Amendment Bill 2018 in Parliament (the so-called A version of the Bill), which proposed new and revised amendments to the Competition Act, 89 of 1998 (the **Principal Act**). Following a consultation process in the National Assembly's Portfolio Committee on Economic Development (the **Portfolio Committee**), the National Assembly, during its plenary sitting on 23 October 2018, passed a revised version of the Bill (Bill number B23B–2018 or the so-called B version of the Bill) (hereafter referred to as the **Amendment Bill**).

1.2 The Law Society of South Africa (**LSSA**) gladly accepts the Select Committee's invitation to make submissions on the Amendment Bill and would welcome the opportunity to debate the submissions with the Committee in person.

1.3 Over the past nineteen years, members of the constituent entities of the LSSA who practise in the area of competition law have experienced the Principal Act in operation and have observed first-hand the extent of its successes and also its shortcomings.

1.4 The LSSA was established as a national non-statutory body to represent the attorneys' profession in South Africa by bringing together in a single entity its six constituent members, the Black Lawyers Association, the National Association of Democratic Lawyers and the Law Societies of the Northern Provinces, the Cape, the Free State and KwaZulu-Natal. Although the Law Societies have ceased to exist on 31 October 2018 with the establishment of the Legal Practice Council, the LSSA continues to exist and speaks nationally on behalf of the attorneys' profession. Its specialist committees, of which the Competition Law Committee is one, consists of practising attorneys who are experts in their field of practice.

1.5 The LSSA believes that the effective and efficient enforcement of the Principal Act is crucial in achieving a free and fair economy in South Africa, for the benefit of its people. If amendments to the Principal Act can address its shortcomings, this should lead to improved competitiveness in markets and enhanced benefits for South African consumers. The LSSA therefore trusts that the Select Committee will find these submissions useful.

1.6 The LSSA commends the manner in which a number of shortcomings in the Draft Competition Amendment Bill, which was published for comment on 1 December 2017, have been addressed. In addition, the LSSA recognises and appreciates the many amendments reflected in the Amendment Bill which are appropriate and positive responses to various comments received by the Portfolio Committee on the A version of the Bill, including submissions made by the LSSA to the Portfolio Committee.

1.7 However, a number of serious concerns with the Amendment Bill remain. Certain provisions of the Amendment Bill, which have not been subject to a public comment process in the National Assembly, may have the unintended result of softening competition between firms or chilling pro-competitive investment. Moreover, if the ideals of the Amendment Bill cannot be met by the Competition Commission and Competition Tribunal (**the Competition Authorities**) which are, by their own admission, under-resourced, this will do severe damage to the well-earned reputations of those institutions.

1.8 Further, the lack of clarity in some of the proposed amendments may result in inconsistencies in application by the Competition Authorities. Fairness is comprised of both objective and subjective elements. Any inconsistency in the interpretation and application of legislation that is, effectively, the "gateway" to the South African economy could result in perceived unfairness, which may in turn discourage potential investors

1.9 The comments of the LSSA set out below aim to (1) clarify aspects of the Amendment Bill that risk creating uncertainty, and (2) mitigate the negative impact on investment and competitiveness that may result from particular provisions, whilst preserving what the LSSA understands to be the underlying objectives of the Amendment Bill, namely to address market concentration and unequal ownership patterns in the South African economy. These submissions are presented with the goal of ensuring that the provisions of the Amendment Bill are as clear as possible to allow for greater certainty for market participants and for the Competition Authorities who are tasked to enforce them.

2. COMMENTS ON THE AMENDMENT BILL

2.1 The role of regulations under the Amendment Bill

2.1.1 The LSSA notes that the Amendment Bill, throughout its proposed amended text (with the exception of sections 21 (gE) and 79), replaces references to guidelines published by the Competition Commission (**Commission**) with references to regulations made by the Minister of Economic Development (**Minister**) instead.

2.1.2 The LSSA recognises the legitimate role of regulation in the law-making process. However, the LSSA is concerned that the regulations currently contemplated by the Amendment Bill will either: (i) not serve the intended function at which the proposed provisions were directed (i.e. providing non-binding guidance as to their practical application); or alternatively (ii) will amount to an inappropriate delegation of substantive law-making powers to the executive arm of Government (**Executive**).

2.1.3 First, the Amendment Bill has replaced the previous requirement in articles 3(b) and 4 thereof for the Commission to publish guidelines regarding the application of sections 4 and 5 of the Principal Act, with a requirement instead for the Minister to make regulations to this effect. The LSSA is of the view that addressing these particular issues by way of regulation creates even more significant concerns than the concerns previously raised by the LSSA and other stakeholders in their submissions to the Portfolio Committee in relation to guidelines.

2.1.4 The LSSA appreciates the need for greater clarity and certainty regarding the Commission's approach to investigating and prosecuting alleged contraventions on sections 4 and 5. Since many of the tests and standards in these sections are necessarily framed in broad terms (often with reference to abstract concepts), practitioners and industry participants would benefit from concrete examples of how these would apply to specific but commonly-encountered practices (such as, for instance, joint ventures, dual distribution arrangements and virtual exclusive territoriality). Such examples can be used to better understand the relevant legal

standards and therefore guide behaviour to comply with the Principal Act, especially where it comes to complicated concepts like "characterisation". It is this purpose that the previously-contemplated guidelines regarding the application of sections 4 and 5 were intended to serve.

2.1.5 Although a useful behavioural guide, guidelines must of necessity be non-binding. After all, they would provide merely an indicative approach to the Commission's view of the tests as they might apply to various factual scenarios. The context will be different for each case brought in practice and the competition authorities should be able to adapt their approach appropriately.

2.1.6 The LSSA respectfully submits that regulations in relation to sections 4 and 5, as proposed in the Amendment Bill, would not effectively serve this purpose. Generally speaking, regulations allow for the Executive to provide additional details regarding the content or procedures to be followed in order to give effect to the provisions of the principal act. However, in this context, it is respectfully submitted that there is no need for the Minister to give additional details regarding the content or procedures of, or substantive tests to be applied in, the provisions under sections 4 and 5 of the Principal Act (including any amendments proposed by the Amendment Bill). Instead, what is needed is an indication of how the Commission will approach these tests in particular circumstances. Regulations are not the appropriate tool by which to provide this guidance.

2.1.7 In addition, guidelines provide for greater flexibility than regulations, since the process involved in their adoption is less stringent and they may be amended more frequently in response to an ever- and rapidly-changing business environment.

2.1.8 While the LSSA appreciates the emphasis that has been placed on the consultative process by which regulations are to be adopted under Amendment Bill (i.e. by requiring that the Minister, in making regulations in relation to these sections, must consult the Commission and invite comments from interested parties), the process

by which guidelines are to be adopted under the proposed section 79 is no less consultative.

2.1.9 As such, for the reasons set out above, the LSSA respectfully submits that the Amendment Bill either: (i) revert to the relevant provisions as they appeared initially in the A version of the Bill (as introduced by the Minister in Parliament), which required that the Commission publish guidelines regarding the application of sections 4 and 5 of the Principal Act, but without the requirement under the proposed section 79(4) that these must be taken into account by any person interpreting or applying the Principal Act (in line with the LSSA's previous comments to the Portfolio Committee to this effect); or (ii) remove any reference to guidelines or regulations being published regarding the application of these sections.

2.1.10 Second, the Amendment Bill has replaced the references to guidelines in A version of the Bill with regulations at the proposed section 8(3)(f), the new section 8(4)(d)(ii), and the new section 9(4)(b). The LSSA submits that the power conferred on the Executive to make regulations which set out the "factors" and "benchmarks" to be applied in determining a contravention, is a broad discretionary power, which ought to lie with the legislature or be developed by the judiciary. In *Dawood and Another v Minister of Home Affairs and Others; Shalabi and Another v Minister of Home Affairs and Others; Thomas and Another v Minister of Home Affairs and Others* [2000] ZACC 8, the Constitutional Court held that –

"[47] . . . if broad discretionary powers contain no express constraints, those who are affected by the exercise of the board discretionary powers will not know what is relevant to the exercise of those powers or in what circumstances they are entitled to seek relief from an adverse decision."

2.1.11 Although the Court in *Dawood* accepted that there may be instances where a broad discretion is permissible, for example, where the factors relevant to exercising the discretion are so numerous and varied that it is inappropriate or impossible for the

legislature to identify them in advance, the discretion to make guidelines containing the “factors” or “benchmarks” relevant to delineating a contravention of a stutute cannot be broad. The power to set “factors” and “benchmarks” goes beyond the manner of implementation, and encroaches on the decision of what constitutes a contravention of the Principal Act.

2.1.12 The LSSA respectfully submits that it is inappropriate for Parliament to delegate to the Minister the power to prescribe substantive legal tests and standards (or an approach to interpretation of such tests and standards), which are not provided for in the Principal Act, that are to be applied in assessing whether there has been a contravention of certain prohibited practices under the amended sections 8 and 9.

2.1.13 To the extent that additional binding tests or standards are required, these must be set out in the Principal Act itself. Accordingly, the LSSA recommends that the references to regulations in the proposed sections 8(3)(f), 8(4)(d)(ii), and 9(4)(b) be removed from the Amendment Bill.

2.1.14 By contrast, the LSSA notes that the regulations contemplated in the proposed new sections 8(4)(d)(i) and 9(4)(a) – which will set the relevant thresholds for determining which firms owned and controlled by historically disadvantaged persons are entitled to protection under sections 8(4) and 9 respectively – are appropriate issues to be addressed in regulations. Such guidelines do not create additional substantive legal tests or standards to be applied, but set the relevant thresholds that are necessary in order to give effect to the substantive provisions set out in the Principal Act (as amended by the Amendment Bill).

2.2 <u>Margin squeeze</u>

2.2.1 The LSSA welcomes the new definition of 'margin squeeze' that is proposed to be inserted into section 1 of the Amendment Bill as it provides greater clarity and captures more accurately the nature of the prohibition.

2.2.2 However, in order to void any doubt as to its meaning, the LSSA would propose that the word "margin" as used in the definition be replaced with "difference" – in economic terms, "margin" connotes a measurement by reference to profit margins, whereas the concept of "margin squeeze" is assessed simply with reference to the difference between the price at which a firm sells an input and the price at which it sells the downstream product.

2.2.3 The LSSA therefore submits that the proposed new definition of "margin squeeze" in the Amendment Bill should be amended to read as follows:

> *" 'margin squeeze' occurs when the ~~margin~~difference between the price at which a vertically integrated firm, which is dominant in an input market, sells a downstream product, and the price at which it sells the key input to competitors, is too small to allow downstream competitors to participate effectively;"*

2.3 Buyer-power provisions

2.3.1 The LSSA recognises the need to address buyer-power in the context of the South African economy and appreciates the objective of the buyer-power provisions in the Amendment Bill. However, some of these amendments raise serious concerns and would benefit from further consideration.

Unfairness

2.3.2 Under the Amendment Bill, the previously-proposed section 8(1)(d)(vii) (as contained in the A version of the Bill) has been replaced by the proposed new section 8(4). Whereas previously the Bill proposed to prohibit requiring a small and medium business or a firm controlled or owned by a historically disadvantaged person *"to sell its products to the dominant firm at a price which impedes the ability of the supplier to participate effectively"*, the prohibition under section 8(4)(a) of the Amendment Bill now prohibits a dominant firm in a designated sector *"to directly or indirectly, require from or impose on a supplier that is a* small and medium *business*

or a firm *controlled or owned by historically disadvantaged persons, unfair – (i) prices; or (ii) other trading conditions."*

2.3.3 While the LSSA supports the objectives of the Amendment Bill to protect small and medium businesses and firms controlled or owned by a historically disadvantaged persons from abuses of buyer power that cause competitive harm, the LSSA is concerned that the reference to "unfair" prices or other trading conditions creates uncertainty and does not address the intended mischief in a manner that is sufficiently clear or accurate. There is no comparable standard of fairness set out in any other provision of the Principal Act or Amendment Bill, and there is therefore also no jurisprudence on what such a standard might entail. What is fair or unfair to one person may not be fair or unfair to another. Specifically, it is not clear as to whether the unfairness standard requires that prices or trading conditions be unfair in comparison to other comparable prices or trading conditions, or whether it is possible that they objectively be unfair in and of themselves. The LSSA submits that the "unfairness" standard is therefore vague and potentially open to abuse.

2.3.4 The LSSA is aware that, for these reasons, the introduction of a standard of unfairness – as a prohibition that is distinct from price discrimination and excessive pricing – has created interpretive difficulties in other jurisdictions, such as Zambia.

2.3.5 The LSSA appreciates that the proposal to have regulations addressing the meaning of unfairness is intended to address this concern, but as noted above, interpretation of legislation or the prescription of substantive legal tests and standards is not appropriate for regulation.

2.3.6 The LSSA therefore recommends that it would be best instead to retain the reference in section 8(4)(a) to prices or trading conditions that *"impede the ability of the supplier to participate"*, which phrase also appears elsewhere in the Amendment Bill (e.g. in the context of price discrimination) and is assisted in its interpretation by a definition of the term "participate".

Non- availability of technological, efficiency or pro-competitive defence

2.3.7 Whilst the LSSA understands the concern with buyer power, especially in a developing economy like South Africa, the proscription of buyer power abuse in a separate sub-section of the Principal Act (section 8(4)) elevates this types of abuse (also known as monopsony power abuse) to a significantly higher enforcement level than abuses by dominant suppliers of products or services (also known as monopoly power abuse). This is done in two ways. First, there is no longer a need for the Commission or the complainant to prove the competitive harm of the monopsony conduct and, second, the so-called "rule of reason" defence, namely that the conduct has technological, efficiency or pro-competitive gains which outweigh the monopsony conduct's effect, is no longer available to a respondent (unlike the availability of such a defence in sections 491)(a), 5(2), 8(c) and 8(d)). This type of abuse is thus effectively rendered a *per se* offence.

2.3.8 Such an approach is simply not supported by the existing body of economic research, nor international best practice, and is likely to have detrimental effects on the ability and incentive of larger firms to continue to seek out efficiencies, in the form of lower input costs that would otherwise have directly benefitted their customers and ultimately consumers.

2.3.9 Moreover, it is well accepted that buyer power could be beneficial to consumers. It is a well-founded presumption in competition economics and competition law that buyers that obtain reductions in variable costs will typically pass on at least a portion of these cost reductions to their own customers (irrespective of the competitive conditions that they face in their own downstream markets). Accordingly, to the extent that the buying power of firms is enhanced, this can be expected to lead to such firms reducing prices to their own customers.

2.3.10 Whilst the LSSA accepts that buyer power can, under particular circumstances, result in competitive harm, it is not appropriate to presume so, even if the buyer/s in question is/are dominant purchasers. Indeed, buyer power is more often likely to

result in lower pricing and other benefits in the supply chain (through incentivising suppliers to be more competitive), while supplier power is far more likely to have negative consequences.

2.3.11 This proposed provision in the Amendment Bill places a large firm at risk simply for attempting to negotiate competitive terms. It will in principle be open to any supplier which is small and medium businesses or firms controlled or owned by historically disadvantaged persons to allege an abuse of dominance each time that a large firm seeks to negotiate price (or declines to contract, or switches supply to a cheaper source) which not only chills commercial negotiation and contractual freedom but could lead to an unjustified multiplicity of complaints – which is important to consider in light of the Competition Authorities' resources to deal with an even greater volume of complaints.

2.3.12 By the same token, over-protecting suppliers from the rigours of competition is not an effective way to build a robust and globally competitive marketplace, and will harm the prospects for economic development and broad-based growth.

2.3.13 Whilst smaller and historically disadvantaged firms should undeniably be protected against monopsony abuses, there is no empirical evidence which indicates that this type of conduct has such far-reaching consequences for the South African economy to justify such an extreme remedy.

2.3.14 The LSSA therefore recommends that the provisions of section 8(4) be moved to section 8(c) or 8(d), alternatively that the "rule of reason" defence be included in section 8(4).

Shifting of the evidentiary burden

2.3.15 The unfortunate situation described above is compounded by the shifting of the evidentiary burden in buyer power offences. It its submissions on the A version of the Bill to the Portfolio Committee, the LSSA commented on the shifting of the evidentiary burden in respect of certain prohibitions, including the prohibition relating to the abuse of buyer power. Those comments are not repeated here. It suffices to

point out that in the context of the new proposed wording of section 8(4)(a) and (c) set out in the Draft Bill, the concerns previously raised by the LSSA are amplified – a dominant firm would now be required to show that its prices or other trading conditions are "not unfair".

2.3.16 Quite apart from the dubious constitutionality of the shifting of the evidentiary burden in this case, it is unclear how this shifting of the evidentiary burden will work in practice. For example, what will constitute a *prima facie* case of unfairness? And what will be required in order for a firm to demonstrate that its conduct is not unfair? Against this standard, it will be extremely difficult for market participants to assess their conduct and risk in advance of setting a price. In addition, it would place an undue burden on dominant firms to proactively demonstrate fairness, particularly where they do not have the authorities' investigatory powers to gather and compel data and information from the supplying firm which is complaining to defend themselves.

2.3.17 While these concerns are present in respect of any provision that creates a presumption or shifts the evidentiary burden, the concerns are even more clearly evident where a new standard of "unfairness" – for which there is no decisional precedent or established principles – is proposed to be introduced.

Prohibition on circumvention

2.3.18 Under section 8(4), paragraph (b) expressly prohibits firms to which section 8(4)(a) applies from circumventing the operation of that provision by avoiding purchasing, or refusing to purchase, goods or services from a relevant supplier. In addition, if a *prima facie* case is made out that a dominant firm has circumvented section 8(4)(a) in this manner (i.e. simply if it has failed or refused to supply a small and medium business or a firm controlled or owned by historically disadvantaged persons), section 8(4)(c)(ii) places the obligation on the dominant firm to show that it did not do so.

2.3.19 The LSSA respectfully submits that: (i) the section 8(4)(b) prohibition is unnecessary; and (ii) to the extent that it is retained, should not be subject to a shifting of the evidentiary burden as set out in section 8(4)(c).

2.3.20 First, at common law, it is in any event unlawful for parties to deliberately circumvent a statutory prohibition when their conduct in effect achieves precisely that which is intended to be hit by the prohibition. When a transaction is designedly disguised so as to escape the provisions of the law, but falls in truth within these provisions, it will be said to be *in fraudem legis* (i.e. in fraud of the law) and falls to be set aside as unlawful as a result.

2.3.21 Whilst the LSSA raised in its submissions to the Portfolio Committee on the A version of the Bill the potential unintended consequences that would arise as a result of a prohibition in the nature of the new proposed section 8(4)(a), it is respectfully submitted that such consequences cannot be cured by simply prohibiting a circumvention of these provisions. Our courts have consistently recognised that the law permits people to arrange their contractual or business affairs so as to obtain a benefit for themselves that a different arrangement would not permit, or so as to avoid a prohibition that the law imposes – unless, as has been identified above, the conduct designedly avoids the prohibition while nevertheless achieving the mischief at which it is directed.

2.3.22 Without imposing a an absolute positive obligation on dominant firms to deal with small and medium businesses or firms controlled or owned by historically disadvantaged persons in all circumstances (which could not legitimately be the case and which is not suggested by the LSSA ought to be the case), the proposed section 8(4)(b) cannot be read to go beyond the restrictions that would in any event exist at common law as outlined above. And, in those circumstances, the provision is an unnecessary addition.

2.3.23 In addition, if this proposed provision is read as an absolute requirement for dominant firms to supply small small and medium businesses or firms controlled or

owned by historically disadvantaged persons, this may be subject to a constitutional challenge on the basis that it is not a reasonable or justifiable infringement upon firms' freedom of trade, as enshrined in section 22 of the Constitution of the Republic of South Africa, 1996.

2.3.24 Second, even if the proposed section 8(4)(b) is retained, the LSSA respectfully submits that it would not be appropriate to subject it to the shifting of the evidentiary burden as set out in section 8(4)(c). The prohibition will likely be read in line with the *in fraudem legis* doctrine, a key component of which is that the parties' real intention was to avoid the prohibition while achieving the mischief at which it is directed. This is supported by the wording of section 8(4)(b) itself, which requires that the avoidance or refusal be *"in order to circumvent the operation of paragraph (a)"* i.e. the parties must have intentionally designed their conduct to avoid the application of paragraph 4(b).

2.3.25 Permitting a shift of the evidentiary burden as currently contemplated risks that the Commission will be able to make out a case for this contravention simply on the basis of conduct that may be objectively justifiable (such as a pattern of consistently not using small and medium businesses or firms controlled or owned by historically disadvantaged persons), without inquiring into the intention of the accused firm. That firm would then bear the responsibility for demonstrating that this was not its intention. However, it is notoriously difficult, if not impossible, to prove a negative.

2.3.26 The LSSA respectfully submits that this places an undue burden on dominant firms and risks undermining ordinary commercial conduct that is legitimate and which does not undermine competition or public interest outcomes.

2.3.27 The LSSA therefore recommends that the proposed section 8(c) be removed from the Amendment Bill.

2.4 Price discrimination

Test for harmful discrimination

2.4.1 The introduction of the word “effectively” in the proposed section 9(1)(a)(ii) serves to modify the defined term "participate" in a manner which is not clear. It is submitted that the test established under the definition of “participate” in section 1 of the Principal Act (as amended by the Amendment Bill) is sufficiently clear and the introduction of the word “effectively” introduces a potential for debate and litigation that threatens the efficacy of the provision.

Defences

2.4.2 Under the Amendment Bill, the proposed new section 9(3)(a) precludes a firm from placing reliance on the fact that price differentials made only reasonable allowance for differences in cost or likely cost of manufacture, distribution, promotion or delivery resulting from *quantities* in which goods or services are supplied to different purchasers, as a defence to an allegation that such price differentials had the effect of impeding the ability of small and medium businesses, or firms controlled or owned by historically disadvantaged persons, to participate effectively.

2.4.3 The LSSA does not see any clear rationale why the existing quantity-based justification in the current section 9(2)(a) of the Principal Act should not be available in such cases. The effect of these new provisions could be to require a dominant firm to supply small quantities to small and medium businesses, or firms controlled or owned by historically disadvantaged persons at the same prices as it may supply large quantities in circumstances where it may not be economically feasible to do so and which would create perverse cost consequences. The proposed new provisions ignore the cost-reducing impact of economies of scale and undermine efficiency. The unintended consequence of these provisions would include loss to competition and consumers. If the dominant firm passes the higher cost on to its customers, consumers will end up paying higher prices for goods.

2.4.4 In addition, excluding this defence would be a departure from the settled and accepted principles governing prohibitions on price discrimination in comparable jurisdictions globally.

2.4.5 The LSSA therefore recommends that the proposed new section 9(3)(a) be removed from the Amendment Bill.

Shifting of the evidentiary burden

2.4.6 The LSSA has previously expressed its concerns regarding the implications of requiring a firm to demonstrate that it has not contravened the Principal Act where there is only a *prima facie* case against it, which are reiterated from paragraph 2.3.15 above.

2.4.7 These concerns are once again highlighted in the case of the proposed new section 9(3)(b) – whether or not a given differential in prices is likely to impede the ability of a small or medium business, or a firm controlled or owned by a historically disadvantaged person, to participate effectively, is a matter that will be within the particular knowledge of that business. The knowledge required to disprove the alleged impact will not be within the domain of the dominant firm. As such, this provision will operate unfairly to the detriment of the dominant firm.

2.4.8 The LSSA therefore recommends that the proposed new section 9(3)(b) be removed from the Amendment Bill.

Prohibition on circumvention

2.4.9 Similarly to the context of the buyer-power provisions discussed above, in relation to price discrimination, the proposed new section 9(1A) of the Amendment Bill expressly prohibits firms to which section 9(1)(a) applies from circumventing the operation of that provision by avoiding selling, or refusing to sell, goods or services to a purchaser that is a small and medium business or a firm controlled or owned by historically disadvantaged persons.

2.4.10 In addition, if a *prima facie* case is made out that a dominant firm has circumvented section 9(1A) in this manner, section 9(3A) places the obligation on that firm to show that it did not do so.

2.4.11 The comments made in relation to these corresponding provisions in the context of the buyer power provisions under paragraph 2.2 above apply equally to these provisions.

2.5 Appeal rights for the Commission in merger decisions

2.5.1 The proposed section 17(1)(b) in the Amendment Bill provides for an automatic right of appeal by the Commission on adverse merger decisions by the Tribunal. The LSSA submits that this may lead to a serious lack of commercial certainty for merging parties – i.e. they could be caught up in litigation long after a merger is commercially viable or a long-stop date expires. This may, in essence, result in a constructive prohibition and a disincentive to invest – especially in high-profile large mergers which already take significant time to be approved.

2.5.2 The LSSA submits that the Commission's right of appeal should, in the very least, not be entirely unfettered. It is therefore suggested that the Commission should be entitled to appeal only in circumstances where leave to appeal has been granted by the CAC.

2.5.3 It is noted that the authoritative International Competition Network (in which the Competition Authorities play a major part and whose guidelines they generally endorse) has set out three pillars to guide the development and implementation of successful merger control:

- Timing: It is important that the merger control regime is designed to allow mergers to be assessed as quickly as possible, so as to minimise the disruption to the underlying competition for corporate control as far as possible. This concern over timing does not arise simply from firms' preference for quicker procedures, but more importantly that the merger control process leaves parties

open to unexpected timing delays – in particular if there is uncertainty about the tests that they face;

- Costs: The overall cost of the merger control process, both in terms of direct (i.e. merger filing fees) and indirect costs (including time and effort spent preparing and defending the merger) should be kept to a minimum so as not to unduly discourage potential pro-competitive mergers. In particular these costs might fall disproportionately on smaller firms, which have less managerial capacity and smaller financial reserves – especially in the context of an appeal. The merger control regime should, therefore, aim to minimise these costs so as to encourage investment and economic growth; and
- Certainty: Above all, predictability should form the cornerstone of any merger-control regime. Mergers should be objectively analysed in terms of established methods of enquiry and which are appropriate to the analysis. This yields reasonable predictability of outcomes for parties in an otherwise risky transaction, a quality increasingly required in today's fast-paced commercial market realities, where bidders for desired assets may face stiff competition from other potential buyers vying for the same target.

2.6 National security review

2.6.1 The LSSA is acutely aware of the need for South Africa to have laws that protect our country against serious threats against its independence, sovereignty and national security. Ours is a hard-won democracy and constitutional state which cannot be allowed to be usurped or undermined by hostile forces, terrorists, terrorist organisations and organised crime.

2.6.2 The LSSA recognises that this laudable objective is the main motivation behind the proposed section 18A. However, the LSSA is concerned that section 18A's

inclusion in the Amendment Bill is inappropriate and premature, and can lead to unintended consequences.

2.6.3 First, it does not appear from the Explanatory Memorandum to the Amendment Bill that there has been consultation with the Government Clusters, Departments or Sectors responsible for Defence, Security, Communications, Trade and Industry, and International Affairs. Provisions relating to national security can be expected to impact on the responsibilities of these clusters and if they have not considered it, conflicts in the enforcement of various statutes and regulations may arise. The Explanatory Memorandum only refers to consultations with the Economic Sectors and Employment Cluster.

2.6.4 Second, it does not appear that the Amendment Bill will be considered by the various Parliamentary Portfolio Committees and Select Committees responsible for Defence, Security, Communications, Trade and Industry, and International Affairs. Provisions relating to national security can be expected to impact on the oversight responsibilities of these committees and if they have not considered it, there is a risk that Parliamentarians who are experts in their respective fields have not been given the opportunity to consider and debate the possible consequences of section 18A.

2.6.5 Third, there has been inadequate public consultation on this far reaching provision which may impact on South Africa's national security and economic well-being. Whilst a draft version of the Competition Amendment Bill was released for comment on 7 December 2017 (with a comprehensive motivational memorandum), the proposed section 18A did not appear therein. This provision was also not referred to in the various public fora where the Executive referred to amendments to the Principal Act, for approximately two years prior to the release of the A version of the Amendment Bill on 7 July 2018. The public therefore had less than two months to get to grips with a complex and far reaching piece of legislation that was not preceded by any white paper or policy document inviting public debate. The

LSSA's understanding it that this provision was also introduced very late in the NEDLAC consultation process and, since the debate in NEDLAC focused on other provisions in the Amendment Bill, section 18A was not given much attention.

2.6.6 Moreover, the specific provision (section 18A) is buried amidst other complex and arcane provisions in a Bill which has nothing to do with national security. After all, it is titled the Competition Amendment Bill. The various departments, stakeholders and interest groups could therefore easily have missed this important provision or not properly appreciated its far reaching implications. This can be contrasted with the Protection of Investments Act 22 of 2015 which elicited comprehensive comments and debate and ultimately resulted in a piece of legislation which were much improved when compared to the Bill that was originally introduced in Parliament.

2.6.7 The issue of how the potential national security risk of an acquisition by a foreign firm of a South African business should be handled, is very complex. It comprises balancing of many conflicting policy concerns. For instance, an overzealous blocking of foreign mergers or overly broad review powers in the hands of the Executive may discourage foreign direct investment, which could be very detrimental to the economy. It is well known that foreign investors compare countries in which they can invest and avoid countries where the regulation is too onerous and unclear. It is interesting to note that both the United Kingdom and the United States of America are in the process of reviewing their respective laws on this issue, but these reviews have undergone intensive study and public consultation. It would be a pity for our economy if South Africa hastily enacts such a far-reaching piece of legislation without subjecting it to proper examination and public consultation.

2.6.8 In view of the above, the LSSA is of the view that the proposed section 18A should be removed from the Amendment Bill at this stage and be referred back to the relevant Government departments for further consideration. Government should

be invited to consider specifically whether a provision of this nature even belongs in competition legislation as opposed to self-standing legislation. The LSSA does not believe it belongs in the Principal Act.

Definition and scope of national security interests

2.6.9 The term “national security interests” has not been defined in the Amendment Bill and that the considerations set out in sub-section 18A(4) are extremely broad. It could potentially impact every merger or acquisition which is contemplated by a foreign firm, regardless of its impact on "national security", as that concept is generally understood. This would allow the Executive to review and block transactions on purely on economic or political grounds which are unrelated to the defence, sovereignty, independence and security of the South African state. If this happens, it would undermine the function of the Competition Authorities and discourage foreign direct investment into South Africa.

2.6.10 Subsections 18A(4)(c), (d), (f) and (h) are particularly broad and appear to go well beyond what could conceivably be national security interests. This could be demonstrated as follows [with the LSSA's comments appearing in bold type in block brackets after the relevant sub-section]:

"(4) *In determining what constitutes national security interests for purposes of this Act, the President must take into account all relevant factors, including the potential impact of a merger transaction -*

…

(c) on the security of infrastructure, including processes, systems, facilities, technologies, networks, assets and services essential to the health, safety, security or economic well-being of citizens and the effective functioning of government; **[There are very few "assets" or "services" which can be said not to be essential to the health, safety, security or economic well-being of citizens and the effective functioning of government. This potentially**

includes at least fuel, transport, electronic communications, education, water, electricity, housing, food, agriculture, housing, medicine, medical services, information technology and administrative services, to name but a few.]

(d) on the supply of critical goods or services to citizens, or the supply of goods or services to government; [**The term "critical goods" is vague and unqualified. Virtually every good or service will be important to someone. Moreover, there are very few goods and services which are not being supplied to government (which concept presumably includes state owned enterprises) in one or other form. This potentially includes at least fuel, transport, electronic communications, food, water, electricity, agriculture, housing, medicines, medical services, toys, legal services, auditing service, information technology and administrative services.]**

(e) …

(f) on the Republic's international interests, including foreign relationships **[Whilst the Republic's relationships with other countries are clearly important for South Africa's security, the concept of "international interests" is vague and imprecise. It may include the international trade of <u>any</u> goods and services and tourism]***;*

(g) …

(h) on the economic and social stability of the Republic." **[These concepts are so vague as to include virtually anything. It is not clear where the dividing line lies between what is economically stable or unstable. Also, it is not clear when a country is social unstable (or indeed stable).]**

2.6.11 The LSSA has undertaken a brief desktop review of South African legislation and could not find any instance where the term "national security" was used in the expansive sense contemplated in the proposed section 18A(4), i.e. being inclusive of the supply of virtually all goods and services and commercial endeavours. The term "national security" is normally not defined in great detail. A few examples are mentioned in Annexure A hereto. To expand this concept beyond the concept of what is normally understood as "national security", represents a significant policy shift, which have not been explained or motivated by the promoters of the Amendment Bill.

2.6.12 A comprehensive review of seventeen other countries' foreign investment review legislation and policies by the Organization for Economic Cooperation and Development (OECD) also shows that the proposed section 18A is more expansive than found in most countries[1]. The LSSA acknowledges that the seventeen countries covered in the OECD Report are perhaps not a representative sample of all countries and that they may not be directly comparable to South Africa; however, considering the diversity of approaches in these countries reinforces the need for a comprehensive and thorough study to be done before a policy approach can be decided upon and far-reaching legislation of this nature being considered.

2.6.13 Should the Select Committee be of the view that the proposed section 18A should remain in the Amendment Bill, the LSSA recommends that the relevant sub-sections setting out factors should at the very least be amended as follows (with

[1] Wehrlé, F. and J. Pohl (2016), "Investment Policies Related to National Security: A Survey of Country Practices", OECD Working Papers on International Investment, 2016/02, OECD Publishing, Paris. http://dx.doi.org/10.1787/5jlwrrf038nx-en

the proposed additional words being underlined and the proposed redundant words being struck through in the proposal below):

"(4) In determining what constitutes national security interests for purposes of this Act, the President must take into account all relevant factors which could seriously threaten the security of the Republic, including the potential adverse impact of a merger transaction -

…

(i) on the security of critical infrastructure, including processes, systems, facilities, technologies, networks, and resources , assets and services essential to the health, safety, or security or economic well-being of citizens and the effective functioning of government;

(j) on the supply of critical goods or services which are essential to the health, safety or security of to citizens, or the supply of goods or services which are critical for the effective functioning of to government;

(k) …

(l) on the Republic's international interests, including foreign relationships with other countries or international organisations;

(m) …

(n) on the economic and social stability of the Republic's financial or payment systems."

Revocation of approval

2.6.14 Under the Amendment Bill, the proposed new section 18A(13)(a) provides that the Committee may, in certain circumstances, *"revoke its approval of the merger or, in respect of a conditional approval, make any appropriate decision regarding any condition relating to the merger."*

2.6.15 The LSSA considers that the wording of this provision may give rise to ambiguity as to whether the Committee is empowered to revoke only unconditional approvals or both conditional and unconditional approvals. If the intention of this provision is to provide for the latter, which the LSSA considers likely (i.e. that the Committee is empowered to revoke any approval, whether conditional or unconditional), the LSSA recommends that the provision be clarified to read as follows:

"(13) (a) The Committee may revoke its unconditional or conditional approval of ~~the~~a merger or, in respect of a conditional approval, make any appropriate decision regarding any condition relating to the merger, if—"

Consequences of failure to notify

2.6.16 The LSSA is concerned that certain of the new amendments proposed under the Amendment Bill, particularly regarding the consequences of non-compliance with section 18A, reveal difficulties that arise from an undue integration of the national security review regime – which concerns national security and is distinct from competition regulation – with the processes and institutions of competition regulation already established under the Principal Act.

2.6.17 For example, the proposed new section 18A(11) provides that the Commission may not consider a merger in terms of section 12A, and the Competition Tribunal (**Tribunal**) may not consider a merger in terms of section 16(2), if the foreign acquiring firm failed to notify the Committee in terms of subsection (6). However, the proposed new section 62(2A) excludes matters involving section 18A (except 18A(14)) from the jurisdiction of the Tribunal and the Competition Appeal Court. It is therefore not clear how the Commission or Tribunal will be capable of making an assessment as to whether or not a notification ought to have been made to the Committee in any given case – as appears to be implicitly required by section 18A(11). This would require the competition authorities to interpret the provisions of section 18 and form a view on whether or not a transaction should have been notified; a power which is expressly excluded by section 62(2A).

2.6.18 Similarly, while the Tribunal is empowered to impose administrative penalties under the proposed new section 18A(14) in the circumstances set out in section 59(1)(d) of the Principal Act (read with the necessary changes), one of the circumstances in which it is contemplated a penalty will be imposed is a failure to give notice to the Committee of a notifiable transaction (section 59(1)(d)(i)). In order to carry out this function, the Tribunal will be required to make an assessment

as to whether or not a particular transaction should have been notified – a matter requiring interpretation of the other provisions of section 18A and expressly excluded from the jurisdiction of the Tribunal.

2.6.19 In light of the complexity of integrating the national security veto with the competition regulatory regime as well as the impact and importance of these provisions on foreign investment, the LSSA respectfully submits that more rigorous debate is required to provide for a complete and workable national security regime, either by way of a further amendment to the Principal Act or in stand-alone legislation.

2.6.20 Alternatively, the LSSA recommends that:

(A) the proposed new section 18A(11) be deleted to avoid the inconsistencies set out above, and given that the proposed new section 18A(13)(c) in any event provides that a decision of the Commission or Tribunal will be deemed to be revoked in circumstances where the Committee ought to have been notified but was not; and/or

(B) the power to impose administrative penalties under the proposed new section 18A(14) be conferred on the High Court, rather than the Tribunal.

Deemed approval

2.6.21 An additional consequence of the proposed new section 18A(14), specifically when read with section 59(1)(d)(iv), is that it will be prohibited for parties to implement a merger prior to receiving approval from the Committee, as opposed to parties being free to proceed to implement a merger (assuming that they have approval from the competition authorities) and thereby assume the risk of having to unwind the transaction in the event of an unfavourable outcome from the Committee. In other words, it now seems clear that the national security regime is intended to be suspensory, rather than non-suspensory.

2.6.22 Mergers are often time-sensitive and therefore need to be decided expeditiously. Furthermore, merger regimes ought to provide appropriate levels of certainty and

predictability in order to facilitate economic activity. The LSSA therefore recommends that a new provision be inserted that deems the Committee to have approved a transaction if it has not made a decision within the initial 60 day time period, unless the failure to meet the approval deadline is due to the parties' delay in providing information requested by the Committee, in which case the time period may be extended by the duration of the delay.

Right of appeal

2.6.23 Consistent with its previous comments on the proposed national security regime, the LSSA recommends that decisions of the Committee should be subject to appeal to the High Court. This would facilitate the Committee being held to the appropriate standards of transparency and accountability, and provide additional comfort to potential investors that their interests will be adequately protected through the national security review process.

2.7 Penalties

Finally, the LSSA notes the proposed amendments of section 59 of the Principal Act to increase penalties and make them applicable to a wider set of prohibitions (by removing the so-called yellow card. It is regrettable that penalties could not be applied more effectively to reverse the adverse effects of the prohibited practices on affected markets and/or market players.

7 November 2018

ANNEXURE A

A. The National Strategic Intelligence Act 34 of 1994 defines "national security" in section 1 as follows:

"national security" includes the protection of the people of the Republic and the territorial integrity of the Republic against—

(a) the threat of use of force or the use of force;

(b) the following acts:

(i) Hostile acts of foreign intervention directed at undermining the constitutional order of the Republic;

(ii) terrorism or terrorist-related activities;

(iii) espionage;

(iv) exposure of a state security matter with the intention of undermining the constitutional order of the Republic;

(v) exposure of economic, scientific or technological secrets vital to the Republic;

(vi) sabotage; and

(vii) serious violence directed at overthrowing the constitutional order of the Republic;

(c) acts directed at undermining the capacity of the Republic to respond to the use of, or the threat of the use of, force and carrying out of the Republic's responsibilities to any foreign country and international organisation in relation to any of the matters referred to in this definition, whether directed from, or committed within, the Republic or not,

but does not include lawful political activity, advocacy, protest or dissent;"

B. **Section 6 of the Protection of Personal Information Act 4 of 2013 reads as follows:**

(1) This Act does not apply to the processing of personal information—

…

(o) which involves national security, including activities that are aimed at assisting in the identification of the financing of terrorist and related activities, defence or public safety; or

(ii) the purpose of which is the prevention, detection, including assistance in the identification of the proceeds of unlawful activities and the combating of money laundering activities, investigation or proof of offences, the prosecution of offenders or the execution of sentences or security measures,

to the extent that adequate safeguards have been established in legislation for the protection of such personal information;

C. Section 41 of the Promotion of Access to Information Act 2 of 2000 provides as follows:

(2) A record contemplated in subsection (1), without limiting the generality of that subsection, includes a record containing information—

(a) relating to military tactics or strategy or military exercises or operations undertaken in preparation of hostilities or in connection with the detection, prevention, suppression or curtailment of subversive or hostile activities;

(b) relating to the quantity, characteristics, capabilities, vulnerabilities or deployment of—

(i) weapons or any other equipment used for the detection, prevention, suppression or curtailment of subversive or hostile activities; or

(ii) anything being designed, developed, produced or considered for use as weapons or such other equipment;

(c) relating to the characteristics, capabilities, vulnerabilities, performance, potential, deployment or functions of—

(i) any military force, unit or personnel; or

(ii) any body or person responsible for the detection, prevention, suppression or curtailment of subversive or hostile activities;

(d) held for the purpose of intelligence relating to—

(i) the defence of the Republic;

(ii) the detection, prevention, suppression or curtailment of subversive or hostile activities; or

(iii) another state or an international organisation used by or on behalf of the Republic in the process of deliberation and consultation in the conduct of international affairs;

(e) on methods of, and scientific or technical equipment for, collecting, assessing or handling information referred to in paragraph (d);

(f) on the identity of a confidential source and any other source of information referred to in paragraph (d);

(g) on the positions adopted or to be adopted by the Republic, another state or an international organisation for the purpose of present or future international negotiations; or

(h) that constitutes diplomatic correspondence exchanged with another state or an international organisation or official correspondence exchanged with diplomatic missions or consular posts of the Republic.