

COMPETITION

The prohibition of the Burger King merger and the increasing importance of Broad-Based Black Economic Empowerment factors for South African competition law

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1. The recent decision by the [Competition Commission](#) to prohibit the sale by Grand Parade Investments (“**GPI**”) of Burger King South Africa (“**BKSA**”) to private equity firm, ECP Africa is important because –

1.1 the merger raised no competition concerns and the sole reason for the Commission’s prohibition was that the shareholding of “historically disadvantaged persons” in BKSA would decrease from 68% to 0% as a result of the merger. The Competition Act (“**Act**”) requires the Competition Commission to determine whether the merger may be justified on public interest grounds and the Commission is obliged by a 2018 amendment to the Competition Act (which came into effect on 12 July 2019) (“**2018 Amendment**”) to consider the effect of the merger on “the promotion of a greater spread of ownership, in particular to increase the levels of ownership of historically disadvantaged persons and workers in firms in the market”. The term “historically disadvantaged person” is defined in the Competition Act as a category of individuals who were disadvantaged by unfair discrimination on the basis of race before the South African Constitution came into effect (or an association or juristic person majority owned and/or controlled by such persons) (“**HDPs**”);

1.2 although permitted by the Competition Act, in practice no merger has been prohibited solely due to public interest concerns since the Competition Act came into force on 1 September 1999.

2. The prohibition has unfortunately caused uncertainty about the interpretation and scope of the 2018 Amendment. In May 2016, the Competition Commission issued guidelines on its assessment of public interest grounds in mergers (“**2016 Guidelines**”). The 2016 Guidelines have not however been updated to cover the 2018 Amendment and it is hoped that the Competition Commission will do so as soon as possible.

3. The Competition Commission’s 2016 Guidelines state that the Commission’s general approach to assessing the public interest grounds in the Competition Act is to –

3.1 determine the likely effect of the merger on the public interest grounds;

3.2 determine whether such effect is merger specific;

3.3 determine whether such effect is “substantial”;

3.4 consider any likely positive public interest effects which could justify an anticompetitive merger or, where a merger raises no competition concerns, whether substantial negative public interest concerns arise from the merger;

3.5 consider possible remedies to address substantial negative public interest effects.

4. The Competition Commission has stated that it effectively had no choice but to prohibit the BKSA merger and was simply enforcing the law as provided in the 2018 Amendment. However the legal interpretation of the 2018 Amendment is complex. It merely provides that the Commission must “consider” the effect of the merger on the “promotion of a greater spread of ownership” and increasing levels of ownership by HDPs and workers. The Competition Act does not impose an obligation on the Competition Commission to prohibit a merger (or impose conditions) simply because it does not “promote a greater spread of ownership” and in practice the vast majority of notified mergers are approved unconditionally. The Commission accordingly has a discretion. It must “consider” whether the merger has a negative effect on a public interest ground and whether such effect results in the merger not being justifiable. The 2016 Guidelines state that such

effect must be both merger specific and “substantial” and that remedies to address any concern should be considered to address any public interest concerns. The Competition Commission has advised that it engaged with the merging parties in the BKSA case but did not get a satisfactory response. Details of such engagement have not yet been made public.

5. The 2018 Amendment also specifically requires the Competition Commission to consider the effect of the merger on increasing the levels of ownership of HDPs and workers in “firms in the market”. The express wording is not limited to assessing the target firm (in our case BKSA) only. The mere fact that the HDP ownership of a target firm will decrease is not necessarily definitive proof that a merger raises a “substantial” public interest concern that warrants its prohibition. Reference is specifically made to “the market” which indicates that the analysis must include a more general assessment of HDP and worker ownership in the “market” as well as a definition of the “market”.

6. The Competition Commission’s reason for its prohibition of the BKSA merger is solely based on the reduction of HDP shareholding in BKSA from 68% to 0%. Such reduction is arguably “substantial” if one considers BKSA in isolation as the target firm. However as stated above, the test in the Competition Act is more complex. The Competition Commission has not clarified what level of reduction in the HDP ownership of a target firm would, in its view, constitute a “substantial” public interest concern. For example is any reduction in the target’s HDP shareholding viewed as “substantial”? Or is there some other threshold for example a 10% reduction? Or is only a loss of majority ownership or control by HDPs viewed as “substantial”? Or is the Commission requiring that the existing HDP shareholding (whatever it may be) must be maintained? These issues must be clarified urgently as the effect of the Commission’s BKSA decision has very serious implications particularly for HDP owned and controlled firms who wish to sell their investments and/or businesses to realise value for their HDP owners/shareholders.

7. Requiring that a HDP owned/controlled firm may only sell its business to (or may only be acquired by) a firm with at least the same or substantially similar level of HDP ownership, would have a massive chilling effect on the ability of HDP owned/controlled firms to realise value from their investments by restricting the pool of potential buyers and potentially (and unintentionally) weakening the negotiating position of the HDP sellers. Any buyer (especially foreign investors) will balk at being required by the Competition Commission to give up majority control of their acquisition to third party HDPs. GPI’s share price on the Johannesburg Stock Exchange dropped 17% in reaction to the Competition Commission’s prohibition decision resulting in losses to its HDP shareholders. The merger with ECP Africa had also been approved by 99% of GPI’s shareholders so the Competition Commission’s prohibition decision overrides the wishes of GPI’s HDP shareholders.

8. One result of a restriction on HDPs exiting their majority controlled investments could be that they are “locked in” to their investments on a potentially indefinite basis. This would not be in line with the Government’s general policy of supporting and promoting HDP owned and controlled firms. Furthermore, while “lock ins” are common in Broad-Based Black Economic Empowerment (“**BBBEE**”) ownership transactions, they generally only apply for a commercially agreed fixed term and not indefinitely. The BBBEE Commission (established in terms of the BBBEE Act) has in practice often raised concerns about “lock ins” or other restrictions on the ability of HDP shareholders to exit their investments. There accordingly is a potential conflict in approach between the Competition Commission and the BBBEE Commission. The Codes of Good Practice issued in terms of the BBBEE Act set targets for HDP ownership for the purposes of measuring a firm’s BBBEE ownership score and these targets are 25% in the so called “generic” BBBEE Codes (the targets are 30% in certain BBBEE Codes for specific sectors of the economy). This raises further questions, For example would the Competition Commission prohibit a merger where HDP shareholding decreased from 68% to the 25% or 30% target in the applicable BBBEE Codes?

9. The 2018 Amendment is also not the only public interest ground which the Commission is obliged to “consider” in terms of the Competition Act. The other grounds are the effect of the merger on –

9.1 a particular industrial sector or region;

9.2 employment;

9.3 the ability of small and medium sized businesses and firms owned or controlled by HDPs to “effectively enter into, participate in or expand within the market”;

9.4 the ability of national industries to compete in international markets.

10. The media statement of the Commission’s prohibition decision in the BKSA case did not refer to the results of its assessment on these other public interest grounds. This indicates that the merger did not raise any concerns on these other grounds. Another interpretational issue arises in this regard. The merging parties were prepared to agree to the following conditions for an approval –

10.1 investing at least R500 million for the establishment of new Burger King stores in South Africa and increasing the number of stores to at least 150. This would have a positive effect on the industrial sector and/or regions in which BKSA operates;

10.2 increasing the number of permanent employees employed in South Africa by at least 1 250 HDPs and increasing the total value of all payroll and employee benefits in respect of all employees employed by the merged entity by at least R120 million. This would have a positive effect on employment in South Africa;

10.3 subject to supply on reasonable commercial terms, increasing the procurement of products and/or services from “BBBEE accredited suppliers” in South Africa from approximately R665 million to an aggregate value of at least R930 million per year. This would potentially have a positive effect on the ability of firms owned or controlled by HDPs to “effectively enter into, participate in or expand within the market”;

10.4 within 24 months of the implementation date, the merged entity would allocate an “effective interest” of 5% of its shares for an “appropriate BBBEE ownership structure”. This would have a positive effect on the ownership by HDPs of “firms in the market”.

11. A key question is whether the mere decrease in HDP ownership in the target (BKSA) amounts to a “substantial” public interest concern having regard to the significant public interest benefits offered in the conditions proposed by the merging parties. The Competition Act obliges the Commission to “consider” the effect of a merger on all the listed public interest grounds but does not give any weighting or preference to any one of the five grounds. Does the Competition Act require a “silo” or a holistic approach to public interest? Can concerns with regard to one of the five public interest grounds be mitigated or resolved by positive effects of the merger on the other grounds especially where (as in the BKSA case) a prohibition based on only one of the five public interest concerns will have serious commercial consequences as set out above? From a policy perspective, a more holistic approach to public interest is preferable.

12. The above issues and questions will hopefully be clearly addressed and clarified by the Competition Tribunal. The Tribunal’s previous approach is instructive. In the Shell/Tepco merger in 2002, the Tribunal raised concerns about competition authorities “second-guessing” the legitimate commercial decisions of HDPs and held that considerable caution was needed when competition authorities use public interest as a basis for intervention in a merger where there are no competition concerns and when such intervention is expressly rejected by the only HDP investors whose interests are directly affected. The Tribunal’s more recent merger decisions include conditions –

12.1 in the Pepsico/Pioneer merger (March 2020) that a broad based workers trust acquires up to a 13% direct shareholding in Pioneer within 5 years;

12.2 in the Comair airline merger (October 2020) that the merged entity shall allocate an agreed (confidential) percentage of its shares to an “appropriate BBBEE structure” within an agreed (confidential) period from the “flying start date” with a minimum 5% shareholding to be held by an employee share ownership programme (with a broad participation of black participants) within 12 months;

12.3 in the Thabong Coal/South 32 SA Coal merger (December 2020) that an employee trust and community trust would each acquire a 5% shareholding in the merged firm on a “carried interest” basis (ie at no cost and without encumbrances). In this case the merged firm would become HDP owned and controlled;

12.4 in the Coca Cola merger (February 2021), a previous condition to increase HDP ownership to 30% was reduced to 20% on the basis that a 10% shareholding would be issued to an existing or new employee share ownership programme;

12.5 in the Dotsure/Hollard merger (February 2021), a condition that the merging parties “consider” setting up a worker’s shareholding structure within 5 years;

12.6 in the Trade Retail/Agrifin/BKB merger (May 2021), a condition that at least a 25% shareholding in BKB Fuel Retail be directly or indirectly held by one or more HDP shareholders within 2 years.

13. The Tribunal’s previous decisions indicate a nuanced and commercial approach to the imposition of public interest conditions relating to the post-merger ownership of the merged firm. Such a more flexible approach is a preferable alternative to prohibiting mergers which raise no competition concerns, are approved by and financially benefit HDP investors and involve foreign direct investment. In the BKSA case, the buyer (ECP Africa) is one of the largest and oldest Africa-focused private equity firms whose investors are a broad group of public and private investors, including the African Development Bank (AfDB), the development finance institutions of the United States (DFC), France (Proparco) and Germany (DEG) and various South African and African pension funds. Attracting credible investors such as ECP Africa falls within the Government’s general strategy to attract foreign investment into South Africa. The Tribunal’s decision on the BKSA mergers is likely to be a “test case” on the future interpretation and application in practice of the 2018 Amendment and it is hoped that the Tribunal will bring both clarity and certainty to this very important issue.

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