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Competition Commission's focus on Agriculture and Food value chains

Rising food prices, globally and nationally, combined with the uncovering of alleged collusive behaviour by companies in bread, milling, dairy and poultry, has increased suspicions about possible collusion, abuse of dominance and other anti-competitive behaviour in the entire food value chain. This has thus brought sharp focus on the agricultural value chain and increased calls for more intervention by the government and competition authorities.

The Competition Commission has identified food and agro-processing as a priority area and is currently studying staple foods specifically. This article explains the Commission's approach and situates it within the historical evolution of agricultural policy in South Africa.

Historical background

Agriculture plays an important role in the South African economy contributing to production of food, employment creation, the supply of raw materials to the agro-industrial processing and manufacturing sectors, and foreign exchange income through exports. The agricultural value chain broadly consists of five key levels, that is, the input level, agricultural producers, processing, retail, and end consumption. There are also some vital support activities in the value chain, such as transportation, grading and classification, storage, trading, packaging and distribution.



By: Mapato Rakhudu
Enforcement and Exemptions
Division

The industry has a long history of intense state intervention. The apartheid government instituted extensive controls on the production and marketing of food products with state sanctioned 'control boards' under the 1937 Marketing Act, re-promulgated in 1968. This was largely done to the benefit of farmers which included support for farmers through price protection, subsidised finance and export subsidies. Farmer co-operatives also played an important role in providing inputs and services such as storage, packaging and processing, as well as representing the broad interests of white farmers.¹

Under the first democratic government the far-reaching liberalisation that started in the 1980s continued, with the closure of the control boards under the 1996

¹ This was underpinned by various legislation that included the 1913 Land Act, the Land Bank Act of 1912, the Land Settlement Act of 1912, and the Co-operative Societies Acts of 1922 and 1939.



Editorial Note

The last quarter has seen the Commission involved in several important competition forums, including the Commission's own Annual Conference. There have also been important cases in both mergers and enforcement. And, the Commission's process of prioritising key areas, as described in the previous issue of Competition News, continues. In this issue the lead article by Mapato Rakhudu explains the process and concerns in food and agro-processing in more detail.

Specific enforcement cases reported on here include the recent referral of abuse of dominance and collusion by the Commission to the Tribunal of a complaint in the poultry sector, described below by Neo Chabane. The Commission however, withdrew a complaint in the timber sector, brought by new Scotland Sawmills against Komatiland Forests, relating to supply of sawlogs, this is set out in an article by Reena Das Nair and Itumeleng Lesofe.

Lastly related to enforcement, the High Court issued a decision in favour of

Telkom (and against the Commission) with regard to complaints brought by value added network service providers against Telkom, this is explained by Ngoako Moropene.

Significant mergers in the quarter are reviewed by Tembinkosi Bonakele. These include deals in the markets for transformers, adhesives and motor vehicles. The Commission co-hosted the Annual Conference on Competition Law, Economics and Policy with the Competition Tribunal and Wits University's Mandela Institute on 6 June 2008. Molebogeng Taunyane explains how the conference papers covered a wide range of key competition issues, reflecting on the ongoing development of case precedents and the appropriate tests to be used. The Commission participated in two other major international events during the quarter in the form of the International Competition Network's Annual Conference held in Kyoto, Japan, and the meetings of the OECD's Competition Committee in Paris. Both of these groups enable the South African authorities to share experience and to learn from the

ongoing international developments in competition law.

The growing awareness of the Competition Commission's role in the economy is reflected in three articles addressing relationships with other regulators, corporate compliance and understanding minority protection in assessing control. In the first of these, Mulalo Shandukani describes the Memorandum of Understanding reached by the Commission with the National Liquor Authority which sets out the mutually reinforcing roles each institution can play. Sbusiso Madonsela then sets out why competition compliance is an integral part of corporate compliance and good governance. Finally, Bukhosibakhe Majenge assesses the implications of minority protection provisions for analysing control which impacts, for example, on the evaluation of mergers.

We hope you find all these articles interesting and look forward to your comments and feedback.

Simon Roberts
Editor-in-Chief

Marketing of Agricultural Products Act, conversion of quantitative trade restrictions to tariffs and gradual reductions in the tariffs themselves.² It represented a wide-ranging move away from statutory intervention and was geared towards promoting market efficiency and competitiveness in the sector, aiming also to address socio-economic factors such as the increased participation of previously disadvantaged individuals in agriculture, to promote equitable access to markets by emerging black producers and speed up the process of land reform in the country.³

Anticompetitive Market Structure

It is now clear that liberalisation has not necessarily created competitive markets but, in many areas it appears as if state intervention has been

supplanted by private regulation in the form of anti-competitive conduct. In addition, agricultural value chains remain characterised by high levels of concentration, as well as vertical integration by a few major firms. Overall, the picture is one of high levels of concentration in the manufacture and supply of inputs such as fertilizer, and high levels of concentration also in processing, packaging and retail. The actual farming is relatively unconcentrated, meaning farmers are prices takers on both sides.

The existence of barriers to entry in the value chain is significant in that anti-competitive conduct would not be sustainable if entry was easy. Barriers include the significance of research and biotechnology in the provision of seeds, and economies of scale in other major inputs such as fertilizer, through

to the costs of establishing large grain silos and large-scale milling operations. In some instances branding and marketing pose significant barriers, as well as access to prime retail space, suitable sites for new stores, capital outlay and retailing experience. Such barriers mean that existing market players have an incentive not to respond fully to the changes in market dynamics such as increased demand, but to benefit through increased profit margins. Conversely, their position would be weakened by new entrants attracted by the higher returns present in the market.

In addition, there is an important link between a competitive supply of agricultural products, the availability and affordability of food, and the effectiveness of policies impacting on agricultural production. In particular,

² An important exception is sugar.

³ Department of Agriculture (1998) 'Discussion Document on Agricultural policy in South Africa'.





in biofuels; as well as growth in GDP per capita, which is a variable driving the demand for food.

The implications of anti-competitive market structures and conduct is not that they cause the price increases, but they may mean food prices were already at a higher supra-competitive level, and that the pressures listed above may have a bigger impact to the extent that supply is constrained by low levels of competition. It

these markets includes price fixing and market allocation.

Alleged anti-competitive practices have also been uncovered in some vital agricultural inputs and services, such as fertilizer and silo storage, where cases are pending before the Competition Tribunal. High prices of such products and services achieved through anti-competitive practices would impact on the overall high prices for basic foodstuffs and squeeze the margins of farmers, forcing out marginal farmers and inducing a shift in land use, such as to game farming thus reducing the overall quantity of food produced in South Africa.

Such findings by the Commission support the analysis over many decades by Nobel laureate Amartya Sen of famines in different countries as being due not to food scarcity but to the manipulation of food prices and supply by those with power in the supply chain.

Prioritisation of Staple Foods by the Competition Commission

The Commission's approach to the wider study of food, as a priority sector, has been to identify the main staple food products consumed by the large proportion of South Africans living on low incomes. In identifying the staple food basket the Commission assessed consumption patterns through looking at the food items in the basket of goods for the calculation of the Consumer Price Index ("CPI"), the latest Household Income and Expenditure Survey conducted by Statistics South Africa, as well as data on food consumption patterns in the Living Standards Measurement ("LSM") categories. Unsurprisingly, these data reveal that food consumption patterns differ significantly between different income categories. For example, the expenditure pattern of LSM 1 households shows that virtually their entire household budget is devoted to the bare food necessities; while LSM 6

agriculture and agro-processing has been identified as a sector capable of driving growth, employment creation and industrialization in the economy by the National Industrial Policy Framework ("NIPF") and yet the players along the production chain may not be able to respond appropriately to such sector strategy incentives because of anticompetitive structure/conduct in the industry.

Food Price Increases

The South African economy is characterised by very high levels of poverty, as well as malnutrition and stunting of children, which make the production of food at competitive prices extremely important. Meanwhile, food price inflation has been extremely high over the past one to two years, leading to protests and grave concerns over the implications for consumers, particularly for low income households. Such households typically have to spend a very high share of their income on food.⁴

There are many different factors contributing to the recent food price increases in South Africa, as internationally. These include amongst others, exchange rate movements given the internationally traded nature of many foodstuffs (such as maize); increasing input costs (such as fertiliser);⁵ fuel costs; developments

was expected that under de-regulated conditions, free competition would prevail and as such, prices would, on average, be lower and that firms would be more efficient as competitive rivalry spurred them to cut costs. Instead, it would be fair to infer that market structures have directly impacted on maintaining prices above the competitive level as well as on producers' profitability and viability.

While the anti-competitive structure of the agricultural value chain has been acknowledged before, until recently studies have tended to downplay its implications. For instance, the Food Price Monitoring Committee, established by government to probe the dramatic food price increase during 2002/3, while noting such concerns, discounted them by concluding that "*no profiteering on basic foodstuffs has occurred*". This echoed the earlier findings of Vink and Kirsten in a 2002 report on the same questions for the National Treasury.

We now know this is incorrect as price-fixing cartels are being uncovered by the Commission in investigations into products such as bread, mealie-meal, dairy and poultry products. Anti-competitive behaviour uncovered by the Commission in

⁴ It is estimated that the poor spend more than a third of their income on food, whilst the ultra-poor spend over 50% of their income.

⁵ According to the Bureau of Food and Agricultural Policy Research ("BFAP") (2008), input costs have increased tremendously, and are projected to rise by over 53% during 2008.



and above households are able to purchase a number of more luxurious food items.

The Commission then reviewed pricing patterns and market structure in these sectors. It is evident that there have been significant price increases over the past year in staple food products with devastating impacts on the poorest part of the population.

Following the initial identification of the main areas of focus, the Commission is currently conducting more in-depth assessments of markets and firm conduct in areas such as: fats & oils; grain, milling & baking; poultry; and dairy product. These assessments may lead to the initiation of further formal investigations, in addition to the specific cases already underway in some of the product groupings.

Conclusion

The far reaching liberalisation has not yielded the desired policy outcomes, in that the agricultural value chain appears to be still largely characterised



by anti-competitive outcomes, including high concentration, high barriers to entry, concentration of ownership, vertical integration, as well as anti-competitive behaviour in the pricing of food. These have serious consequences for the welfare of the poorest households given the importance of key staple foodstuffs in South Africa.

Further, the highly concentrated and vertically integrated market structures of the industry may ultimately hinder

constructive responses to a more developmental state approach including increasing participation in the sector. Addressing current competition concerns in the value chain is thus an important component in promoting more competitive outcomes going forward. The Commission's study fits within this wider picture. As part of the focus on food and agriculture, the Commission is also engaging with the relevant government departments, public institutions and other stakeholders.

Commission refers poultry complaint



By: Neo Chabane
Enforcement &
Exemptions Division

The Competition Commission recently referred the findings of its investigation into complaints of anti-competitive conduct by Astral Operations Limited and Elite Breeding Farms to the Competition Tribunal. The Commission found that Astral and Elite have contravened the Competition Act and has asked the Tribunal to levy an administrative penalty of 10% of both companies' annual South African turnover as well as their exports from South Africa for the 2006/7 financial year. Astral Operations and Elite Breeding Farms operate in the poultry market.

Astral Operations Limited is involved in the breeding and rearing of poultry across all levels of the value chain mainly through its control of Ross Poultry Breeders (Pty) Ltd, National Chicks (Pty) Ltd, and Meadow Feeds (Pty) Ltd. Elite Breeding Farms is a joint venture between Astral and Country Bird (Pty) Ltd. Astral owns 82% of Elite while Country bird controls the remaining 18%. The joint venture is involved in the supply of parent breeding stock to the joint venture partners, that is, Astral and Country Bird.

In addition to this specific complaint, the Commission is also studying the





poultry sector more widely as part of its focus on staple foods.

The Poultry Industry in Brief

The complaint centred around the market for the breeding of grandparent and parent stock, as well as the market for the rearing of broilers. The breeding market generally consists of two activities, namely the production of grandparent stock and the production of parent stock. Great-grandparent stock is sourced internationally from international breeding companies, most notably Aviagen, which supplies the Arbor Acres and Ross birds and Cobb Breeding Company which supplies the Cobb bird. Until recently, the breeding market was served by just two major breeders namely, Rainbow which supplies the Cobb breed, and RPB, a subsidiary of Astral, which supplies the Ross 788 and Ross 308 breeds. The Arbor Acres Breed which is supplied by Supreme entered the breeding market and has become an aggressive competitor, managing to secure 14% of the market share within a period of approximately two years.

The second market falling under the scope of the investigation was that

for the production of broilers using parent stock. At this level of the value chain, parent stock is used to produce broilers, which are then supplied to the broiler market. Parent stock chickens produce 150 eggs during 48 weeks, per female chicken. The eggs produced are collected daily and sent to the hatchery for incubation. These day old chickens are then sent to a broiler farm to be brought up and slaughtered.

The poultry industry is generally characterised by high barriers to entry. The breeding market is particularly difficult to enter, due to factors such as high levels of expertise, significant capital investment, and the need for sufficient volumes to justify a breeding programme. The most significant barrier, however, is the need to secure a franchise arrangement with the international intellectual holder of the breed. The strong reputation of brands associated with certain breeds also makes it very difficult for a new breed to enter the market successfully.

Barriers to entry across the other levels of the poultry value chain are also quite high, with only a few companies active in the market. These

barriers are mostly due to the large capital investments needed as well as due to the highly vertically integrated nature of the industry. Almost all the major poultry players are vertically integrated, some even up to feed level, which is very significant given that feed is as much as three quarters of the costs of producing a broiler chicken. In particular, Rainbow Chicken Ltd and Astral Foods Ltd are active along the value chain in the poultry industry.

The Investigation

The complaint against Astral and Elite was lodged by Country bird (Pty) Ltd in February 2007. Country bird transferred all its assets to Supreme Poultry (Pty) Ltd in January 2007, and thus Supreme was also cited as a complainant in the matter. Supreme Poultry is also a fully integrated producer and processor of poultry and poultry products.

In the complaint, Country bird alleged that Astral and Elite were engaging in anti-competitive conduct, mainly through the operation of the joint venture and the terms under which it was formed. To this end, Country bird as one of the parties to



the joint venture, applied for and was granted conditional immunity under the Commission's Corporate Leniency Policy for their involvement in conduct which contravened the Act.

The Commission investigated the complaints and found that the Elite joint venture and the restrictions which flowed from it and the enforcement of its provisions by Astral and Elite has the effect of allocating markets and fixing trading conditions in contravention of Section 4 (1)(b)(i) and (ii) of the Act.

The Commission found that Astral is dominant in the poultry breeding market, which involves the provision of grandparent and parent stock and

abused its power by engaging in exclusionary conduct in contravention of Section 8(c) and (d)(i) of the Act.

The conduct involves various strategies, all of which are intended to protect Astral's dominance in the upstream breeding market and entrench its position in the downstream market through inhibiting effective competition in the market, in particular the market for the production of broilers. The exclusionary conduct had the effect of impeding Country Bird and Supreme from expanding within the market for the production and supply of broilers and from entering or expanding into the breeder market.

In recent months the Commission has been responsible for uncovering collusive behaviour in the bread, milling and dairy industries. The poultry industry has now been included, through the Commission's investigation, as another industry in the broad agriculture and agro—processing sector where anti-competitive practices exist. The conclusion of the investigation against Astral and Elite highlights once again the seemingly widespread nature of anti-competitive conduct in the food sector as well as the necessity for the extended investigation of food and agro-processing activities which is currently being carried out by a team within the Commission.

The Commission's investigation into alleged abuse of dominance in the forestry industry



By: Reena das Nair
(Policy & Research Division)

In June 2005, the Competition Commission ("the Commission") commenced an investigation into alleged anti-competitive behaviour in the forestry industry. This investigation was triggered by a complaint from New Scotland Sawmill ("NSS") against Komatiland Forests Limited ("KLF"), a dominant supplier of softwood sawlogs in the



By: Itumeleng Lesofe
(Enforcement & Exemptions Division)

northern regions of South Africa. NSS was a small non-long term contract sawmilling operation in Mpumalanga. Around December 2005, it closed down its operations mainly due to lack of supply of sawlogs.

NSS alleged that KLF abused its dominance by forcing small sawmillers in the region to pay high prices on the

spot or open market ("OM") compared to prices paid by larger buyers with long-term contracts ("LTCs") with KLF. Further, the complainant claimed that the price disparities between the OM sales and LTC sales resulted in price discrimination between the two groups. Such price discrimination was believed to have led to the exclusion of smaller mills. The complaint was accordingly lodged under Sections 5(1): Restrictive vertical practice; 8(a): Excessive pricing; 8(c): Exclusionary conduct; and 9(1) (a) to (c): Price discrimination of the Competition Act 89 of 1998, as amended, ("the Act").

The Commission found that the LTCs were indeed anti-competitive and resulted in excessive prices in the OM, which ultimately resulted in the exclusion of non-LTC holders. The LTCs further constituted a restrictive vertical practice between KLF and the LTC holders that has the effect of substantially preventing or lessening competition in the market for sawlogs, and consequently, in the market for sawn timber.

With regards to price discrimination however, the Commission found that the OM sales and LTCs sales were not equivalent transactions and therefore no case could be pursued under Section 9 of the Act.

The Commission's investigation in the identified contraventions revealed the following. KLF sells its softwood sawlogs through two main processes. The logs are first allocated to the ten millers with LTCs according to their contracted volumes as well as to KLF's own mill. The remaining logs are allocated in a second process to the OM buyers. The LTC holders are also allowed to participate in the OM sales to obtain further or 'top-up' volumes for their mills.

KLF's pricing system in these log allocation processes was found to force prices in the OM to levels that were not sustainable for those without LTCs. LTC holders, when participating in OM sales, tended to drive the OM price up as they could afford to bid higher prices for a small or top-up portion of their total volume requirements (as they secured most of their requirements through the LTC). The resulting higher price in the open market is further used as a benchmark for price increases that KLF puts forth to the LTC holders. However, because the LTC holders are large mills with considerable buyer power, they are able to contest these much higher prices through price-arbitrations.

The smaller open market players do not have this countervailing power and are forced to take these prices. Under the LTCs, the prices achieved as a result of this (by mutual agreement or if not, by arbitration) are much lower

than the OM prices (and lower than the seller, KLF, desires them to be). The pricing mechanism for the open market sales artificially sets prices above market clearing levels as it results in prices where the margin earned on sawmilling operations for the smaller millers covers variable costs, but not total costs. Those firms without substantial long-term agreements therefore are unable to become effective competitors and have expressed concern that they are being excluded from the market.



It was also found that KLF's vertical LTC agreements as part of the overall system served to lessen and prevent competition in the defined downstream market for sawn timber by creating an unlevel playing field for non-

LTC holders, which will lead to their exclusion as effective competitors from this market. Mills without these LTCs or substantial own plantations are unlikely to survive. Indeed the complainant itself was forced to exit. The resulting prices from the OM process are also excessive and attempting to use these prices as a benchmark to further raise LTC holders' prices as a means to eliminate the gap between the two further aggravates the situation.

The anticompetitive effect of such practices is twofold. It firstly leads to the exclusion of the non-LTC holding mills, including those that are efficient, and leaving sawn timber price determination in the downstream market in the hands of a few firms that dominate the market. Secondly, it leads to artificially inflated prices that will be passed onto the final consumers until import parity prices for sawn timber are reached.

The matter was referred to the Tribunal by the Commission but subsequently withdrawn in the first quarter of 2008 after the Commission was informed that KLF terminated the LTCs in September 2007 and that due notice of this termination was given to the LTC holders. The existence of the LTCs was the root cause of the contraventions of the Act identified and the remedy that the Commission would have sought as a successful outcome from the hearings at the Tribunal would have been the cancellation of these contracts. KLF's cancellation of the contracts achieved this desired remedy without prolonged litigation.

Telkom SA Limited against Competition Commission and Competition Tribunal

During May 2002 the South African Value Added Network Services Association (“SAVA”) and a number of other value added network services (“VANS”) providers filed a complaint with the Competition Commission (“the Commission”) regarding Telkom SA Limited’s (“Telkom”) alleged anti-competitive practices. In August 2002, Omnilink, a VANS provider, filed a complaint with the Commission against Telkom, alleging that Telkom had engaged in price discrimination in respect of the provision of VANS to Nampak. As both complaints involved similar allegations against the same respondent, they were consolidated into a single investigation in terms of the Commission’s rules.

The complaints against Telkom are that within the market for the provision of telephony services Telkom abused its dominance in contravention of the Competition Act by:

- refusing to provide backbone and access facilities to certain VANS providers to construct their VANS networks unless they provided confirmation to Telkom that they would use the facilities in accordance with Telkom’s interpretation of the Telecoms Act and their licenses as to the boundaries of VANS;
- refusing to peer with one of the complainant, AT&T, and also refusing to provide facilities that would enable Satellite Networks (Pty) Ltd to peer with AT&T;⁶
- refusing to lease access facilities to VANS providers directly and insisting on VANS providers acting as agents of their customers in leasing access facilities from it;

- charging more for telecommunication facilities, which connect to the network of other VANS providers, than it charges for the same facilities, which connect to its own competing VANS networks;
- charging other VANS providers and/or their customers for two sets of end connections,⁷ local leads and Dignet Ports for a Dignet circuit whilst it charges its customers for one set only; and
- bundling data conveyance, which the complainants contend falls within the scope of VANS, and voice services in terms of its PSTS⁸ licence, which it is contended creates a service that VANS providers cannot provide as they are prohibited from the carrying of voice until a date to be fixed by the Minister by notice in the Gazette (“the bundling complaint”).

The Commission has a Memorandum of Understanding (“MOU”) with the Independent Communications Authority of South Africa (“ICASA”) with respect to the exercise of jurisdiction in the telecommunications sector.⁹

High Court Review Application

On the 23 February 2004, the Commission referred a substantial portion of the consolidated complaint to the Competition Tribunal (“the Tribunal”) for adjudication.

Instead of responding to the Commission’s complaint referral, Telkom brought a review application in the Pretoria High Court¹⁰ to set aside the referral on the grounds that the Commission and the Tribunal did not have jurisdiction to deal with the issues that were the subject matter of



By: Ngoako Moropene
Legal Services Division

the referral, as only ICASA had such jurisdiction. Telkom further raised alternative arguments, in the event of it failing on its main argument, in the main to the effect that the Commission failed to follow proper procedures, including complying with the provisions of its MOU with ICASA, the Commission is biased and the Commission did not refer the complaint within the prescribed period in terms of the Act.

The Commission opposed the application and in doing so raised two main points *in limine*, namely that the decision to refer and the referral itself are not administrative acts subject to review, and that the forum to raise Telkom’s objections and review is the Tribunal and not the High Court.

High Court Judgment

On the 20 June 2008 the court ruled in favour of Telkom by setting aside the Commission’s decision to refer the complaints to the Tribunal. The judge

⁶ Peering entails a pooling of services so that each participant in the scheme can utilize the pooled facilities without charge.

⁷ End connections consist of network terminating units (“NTUS”) and Dignet Ports.

⁸ Public switched telecommunications services.

⁹ The MOU was clearly based on the concurrent jurisdiction between the Commission and ICASA. Jurisdiction over the conduct of Telkom is exercisable by the Commission in terms of section 3(1) of the Competition Act, as amended. Certain of the Commission’s jurisdiction over Telkom’s conduct is shared concurrently by ICASA. ICASA has jurisdiction over Telkom’s conduct in terms of Telecommunications Act of 1996, the regulations in terms thereof, and Telkom’s licence. Telkom’s conduct that is the subject of this complaint is primarily in the nature of abuse of dominance, and therefore falls within the jurisdiction of the Commission.

¹⁰ Transvaal Provincial Division of the High Court.



upheld the Commission's first point *in limine* and found that the decision to refer and the referral itself are not administrative acts subject to review. He dismissed the second point *in limine*.

On the merits the judge did not rule on the main issue, namely whether the Commission and the Tribunal has jurisdiction to deal with the complaint and the referral. He instead upheld most of Telkom's alternative submissions, namely that the Commission was biased in its decision to refer the matter as because it relied on external consultants whose objectivity was questionable. In what appears to be *obiter dicta*, the judge also held that the Commission did not properly extend the investigation period, in that not all complainants

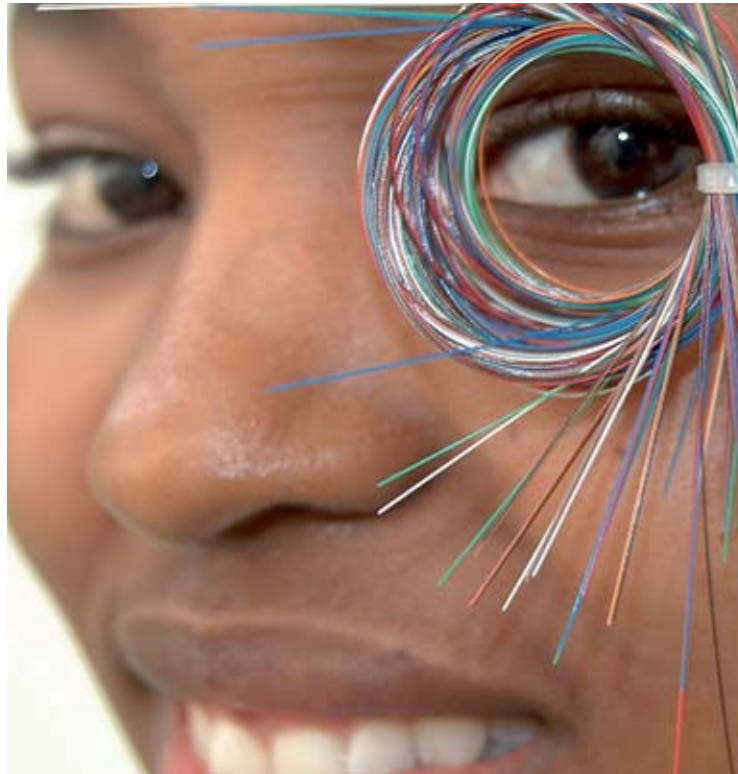
consented to the extension of the investigation period.

In a nutshell, the effect of this judgment is that a decision by the

Commission to refer a matter to the Tribunal is not an administrative act subject to review, unless such decision is vitiated by ill faith, oppression, vexation or the like. The words "the

like" may include bias. The Judge did not address the issue of the jurisdiction of the Commission or the Tribunal in respect of telecommunications matters. Further, the decision has created confusion regarding the manner and form in which the Commission should extend the investigation period provided for in terms of the Act.

The Commission has filed an application for leave to appeal the whole judgment. Subsequently, Telkom has filed an application for leave to cross-appeal. The case is ongoing.



Mergers and acquisitions – quarterly review of major cases

Electricity: Alstom and Current Electric

The merger involved an acquisition of Current Electric (Pty) Ltd by Alstom Electrical SA (Pty) Ltd. Alstom Electrical is 100% owned by Alstom SA (Pty) Ltd, whose major shareholders comprise various BEE partners including Tiso Electrical (Pty) Ltd (20%), Kagiso Power Services (Pty) Ltd (22.5%), Black Employee Trust (4.8%), and Sibilant Investment (Pty) Ltd (2.9%). Alstom intended to operate the Current Electric business as a separate entity.

The transaction resulted in a vertical integration between Alstom and Current Electric. Current Electric was the only manufacturer and supplier of medium current and voltage transformers in South Africa, which transformers are used in the manufacture of medium range switchgear where Alstom is active. The other users of medium current and voltage transformers are switchgear manufacturers such as Siemens, ABB and Schneider. Switchgear is mainly used by Eskom, the Municipalities and large energy intensive corporations such as Sasol and mines.

There was a likelihood of input foreclosure from the merger as the merged entity could foreclose other switchgear manufacturers by either raising their input costs or restricting supply of transformers. Whilst there was this likelihood, the Commission established that there was a potential entrant in the transformer market, whose entry would render the incentive of foreclosure ineffective. However, in order to guard against foreclosure that could occur before the new entrant becomes a fully-fledged medium transformer manufacturer, the Commission approved the merger subject to conditions requiring the



merged entity to continue supplying other switchgear manufacturers with transformers. The condition commenced on 21 May 2008 and runs for a period of 2 years.

Industrial Adhesives: Henkel and National Starch

This was an international transaction involving an acquisition of National Starch and Chemical, a division of Imperial Chemical Industries' ("ICI") by Henkel KGaA. The merger was approved in the European Union and United States. In South Africa there was an overlap in the activities of the parties in connection with the production and supply of industrial adhesives for use in bookbinding, packaging, flexible packaging, labelling, woodworking, construction and automotive.

The Commission found that the proposed transaction leads to very high combined market shares in the application of adhesives in bookbinding (55%), packaging (41.9%) and labelling (47.4%). With respect to the bookbinding market, the Commission found that the merging parties' R&D and international technical expertise for adhesive formulation makes

them close competitors such that the proposed transaction results in the removal of an effective competitor in bookbinding submarket. In packaging, the Commission found that the merging parties tend to target each other's product in determining their commercial strategies, for example, launching a new product; and as such the Commission was of the view that the proposed transaction results in the removal of an effective competitor in this submarket.

With respect to the market for labelling, interviews with market participants revealed that the merging firms are the two main suppliers of bottle labelling adhesives; and even if customers can switch to a different technology for adhesives, they are most likely to use the same suppliers (the merging firms). As such, the Commission concluded that irrespective of technology the merging parties are not only close competitors of each other but the main suppliers of labelling adhesives.

The Commission's investigation, however, found that customers generally engage in dual or multiple sourcing since having at least two or three sources is seen as a necessary

bargaining tool. In addition, customers were large companies with a degree of countervailing power. Therefore, the high market shares of the merging parties do not necessarily indicate the power to unilaterally raise prices since, post-merger, customers will likely qualify an additional supplier. Furthermore, it was established that there are many firms globally who are likely to enter the South African market if prices were to go up, and the only reason they have not entered was the perception that the market was too small and may be saturated.

The Commission approved the merger.

Motor Vehicles: Tata and Jaguar and Land Rover

The Commission recommended the unconditional approval of the large international transaction involving an acquisition by Tata Motors Limited ("Tata Motors") of Jaguar and Land Rover business ("JLR"). Tata Motors is based in India and manufactures and supplies passenger cars, commercial vehicles and buses. Tata Motors currently has no manufacturing activities in South Africa and supplies vehicles from its manufacturing facilities located in India.

JLR conducts its business in South Africa through Ford Motor Company South Africa. Jaguar and Land Rover are not manufactured in South Africa. The South African activities of Jaguar relates to the supply of premium saloons and sports cars. Land Rover supplies a range of sports utility vehicles.

The Commission found that the proposed transaction was unlikely to substantially prevent or lessen competition, as there was no overlap in the activities of the merging firms in the narrowly defined passenger vehicle market.

The merger was subsequently approved by the Tribunal.



Annual Conference on Competition Law, Economics and Policy



By: Molebogeng Taunyane
Compliance Division

The annual Competition Law, Economics and Policy Conference, co-hosted by the Competition Commission, Competition Tribunal and Mandela Institute took place on 6 June 2008 at Wits University. The conference brings together lawyers, economists, academics and regulators

in the competition law field to debate key issues, especially those arising from recent cases.

In opening the conference the Competition Tribunal Chairperson, David Lewis, acknowledged its importance given the intellectual agility and familiarity with current thinking in the field required of practitioners. Lewis also noted that the direction of the conference programme has changed from one that focused on the application to South Africa of ideas and legal conclusions developed elsewhere to the one that examines the interface between our economy and the application of our law.

“This is an intellectually dynamic field – where ideas and investigative techniques are rapidly evolving and are at the cutting edge of the disciplines that inform them. For this reason, engagement and debate between, on the one hand, the world of practitioners and, on the other hand, the world of

researchers and scholars is bound to be particularly fruitful, important and prevalent,” said Lewis.

Twenty-four papers were presented grouped under topics such as: telecommunications and regulation; pricing theories; mergers; dominance, price discrimination and administrative penalties; market definition; co-ordination and restrictions on competition; and competition policy and development.¹¹ These included four papers from the Competition Commission by Mfundo Ngobese, Damian Finlayson, Liberty Mncube and Andrew Swan. In general, the presentations were followed by robust debate among the conference delegates.

As part of expanding the profile of competition law and economics in South Africa, selected papers are being published in the South African Journal of Economic and Management Sciences, as was the case in 2007.

¹¹ See <http://web.wits.ac.za/NewsRoom/Conferences/CompetitionConference/PapersPresentations.htm>



International Competition Network 7th Annual Conference



By: Simon Roberts
Policy & Research Division

The International Competition Network (ICN) held its 7th Annual Conference in Kyoto, Japan, from 14-16 April 2008, hosted by the Japanese Fair Trade Commission. The International Competition Network (ICN) was established in October 2001 with the objective of facilitating procedural and substantive convergence in antitrust enforcement. It is an informal network of competition authorities from around the world, and has a membership of 102 competition authorities from 91 jurisdictions from around the world. Over 500 people from over 70 jurisdictions including representatives of competition authorities and non-governmental advisers such as attorneys at law who specialize in competition laws attended the 2008 Kyoto conference.

The ICN is a project-oriented organization without a permanent secretariat or executive office, and one of its major characteristics is that it provides a forum for discussion among not only member agencies, but also non-governmental advisors such as legal experts and economists. It is coordinated by a Steering Group responsible for decision-making. South Africa has played an important role in the ICN in recent years, hosting the annual conference in 2006, and with

the chair of the Competition Tribunal, David Lewis being an ICN Vice-Chair of Outreach.

The main activities of the ICN take place in four working groups that focus on mergers, competition policy implementation, cartels and unilateral conduct. In the annual conference the working groups report the results of their activities over the year and set an agenda for the year to come. The working groups deliberations include the development of ICN Recommended Practices, as part of promoting greater consistency of competition practices around the world in what is an increasingly international community of practice.

The relatively more advanced working groups are those on mergers and cartels, where Recommended Practices have been adopted.¹² Focuses in the 2008 conference included assessing efficiencies in merger evaluation and merger notification and procedures. With regard to cartels, the sessions addressed managing leniency programmes, settlements, fines and how to improve cooperation across jurisdictions in dealing with international cartels.

The unilateral conduct working group was set up two years ago, following interest expressed in it by several jurisdictions including South Africa. However, it is one of the areas on which there is most diversity across jurisdictions making discussions lively and less oriented to arriving at recommended practices. The main areas addressed in the 2008 conference were the tests for the assessment of dominance, issues related to state created monopolies, and the analysis of predatory pricing and exclusive dealing. Representations made by the South African authorities highlighted the greater importance of unilateral conduct, all else equal, in a small economy, with relatively high entry barriers and being

relatively isolated from other industrial economies. In addition, a history of state support for large firms in key industries implies entrenched dominant positions, the abuse of which can have significant negative economic implications. In addition, countries like South Africa with newer competition laws tend to have more closely defined standards for abusive conduct, which provides clear guidance to firms, and thus have more straightforward tests for dominance such as through the application of market share thresholds. Conversely, countries with less closely defined abuse tests are more concerned with having high hurdles for dominance.

In the competition policy implementation, South Africa played a leading role, in conducting a survey of ICN members on the usefulness of the ICN's outreach work, as well as in highlighting the Commission's own recent experience with strategic planning.

As the host nation, Japan selected the special session for the conference, on abuse of a superior bargaining position. Contributions from Japan, and other Asian countries, highlighted the importance of fair as well as free competition. In this regard, the negative effects on small firms from those with a stronger bargaining position, including where the superior position is on the buying side, is a key concern. It can mean weakened rivalry over time if smaller firms' ability to participate is harmed.

The conference demonstrated the strengths of the ICN in bringing competition authorities and practitioners together from around the world to share experiences in what is such a dynamic field of activity in law and economics. The deliberations highlighted the richness of these experiences and perspectives, as well as the diversity in practice, and provided a platform for the ongoing activities of the working groups over the year ahead.

¹² See www.internationalcompetitionnetwork.org

Meeting of the OECD Competition Committee in June 2008

South Africa has been an active participant in the Organisation for Economic Cooperation and Development's Global Competition forum since the competition authorities were established in 1999.

Since 1 January 2006 we have had observer status on the OECD's Competition Committee and participated in its meetings as well as those of Working Parties 2 and 3 ("WP2" and "WP3"). In addition, the OECD has assisted us with expertise and resources for numerous seminars, workshops and training programmes.¹³ The OECD brings together industrialised countries committed to democracy and a market economy. South Africa, while not a member, may participate under arrangements of 'enhanced engagement' with a view to possible membership in the future.

The OECD's Competition Committee has 3 meetings a year in February, June and October. This is a forum in which members and observers share their experiences with competition policy and law with each other. At this meeting selected jurisdictions are also subjected to a peer review which tests the selected jurisdiction's policies and their implementation.

Meeting in June 2008

Prior to each meeting, the Secretariat of the OECD requests written submissions on pre-determined topics of interest to the participating countries. These submissions are then presented or discussed at the roundtable discussions scheduled by each of WP 2

(Competition and Regulation), WP 3 (Co-operation and Enforcement) and the Competition Committee. In June 2008, the OECD held roundtable discussions on:

1. Competition issues in the construction industry;
2. Market studies; and
3. Bundled discounts and single product loyalty discounts.

WP 3 also had a short session on bid rigging in public procurement.

The Commission and Tribunal made joint written submissions to each of these roundtable discussions. The meeting also conducted an in-depth peer review of the Czech Republic as well as a review of competition amongst professions in Italy.



By: Nandi Mokoena
Commissioners Office

In general, the South African submission on competition issues in the construction industry covered the history of mergers in the construction industry as well as the prioritisation of infrastructure inputs, in line with the AsgiSA Government policy. The submission on market studies focused on the four main market studies the Commission has conducted with much emphasis on the lessons learnt from the Banking Enquiry. The South African jurisprudence gained in the South African Airways ("SAA") matter was the focus of our submission on bundled discounts and single product loyalty discounts. In this paper the South African competition authority set out the facts leading up to the SAA matter before the Competition Tribunal and detailed the factors which the Tribunal took into account in arriving at its finding that SAA had contravened the Competition Act.



¹³ See www.oecd.org/competition

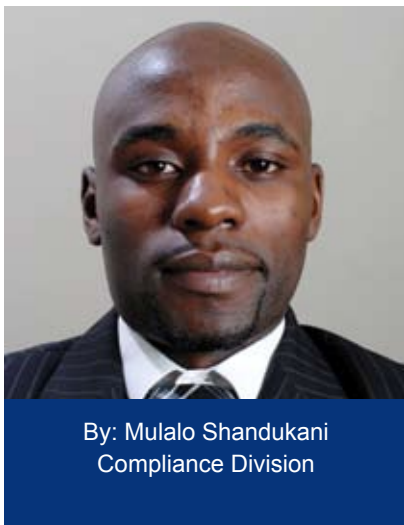


Each of the South African submissions were very well received. The OECD Secretariat requested a detailed presentation on our submission on bundled discounts and single product loyalty discounts and raised interesting questions regarding the competition issues in the South African construction industry.

Once again the competition authorities found the OECD meeting most useful and brought many of the lessons learnt home for further consideration and implementation. In this regard, Italy's experience with competition in professions was helpful in the Commission's own review of the legal profession. Moreover,

the Competition Assessment Toolkit developed by the OECD is also proving to be a practical tool for the drafting of guidelines for Government departments in their quest to detect anti-competitive behavior and to draft pro-competitive policies. The Commission has also recently improved staff's access to OECD materials for guidance in the Commission's day to day work.

Competition Commission signs a Memorandum of Understanding with the National Liquor Authority of South Africa



By: Mulalo Shandukani
Compliance Division

1. Introduction

The Competition Act 89 of 1998, as amended ("the Competition Act") is not an industry-specific legislation and as such its application extends to industries that are subject to regulation by specific regulators. Concurrent jurisdiction exists in regulatory environments wherein both the competition authorities and the industry-specific regulator have jurisdiction over competition matters.¹⁴

The Competition Commission ("the Commission") can enter into a Memorandum of Understanding ("MoU") with regulatory authorities to clarify how the concurrent jurisdiction where competition concerns overlap with regulatory responsibilities can best be handled.¹⁵ In this regard, the Commission recently concluded an MoU with the National Liquor Authority ("the NLA") covering the manner in which the two regulators will interact with each with regard to the consideration of liquor registration applications, evaluation of mergers and acquisitions, as well as anti-competitive complaints. The NLA, housed in the Consumer and Corporate Regulation Division of the dti, is responsible for the administration of the provisions of the Liquor Act No, 59 of 2003, as amended ("Liquor Act"). Primarily, the NLA regulates the macro-manufacturing and distribution tiers of the liquor industry by receiving, evaluating and recommending to the Minister of the dti ("the Minister") registrations for the national macro manufacturing and/or distribution of liquor.

Section 82(3) of the Competition Act provides that an MoU must, amongst others, promote co-operation between the regulatory authority and the Commission. The preamble to the Commission-NLA MoU clearly states that there is in fact no overlap in the respective jurisdictions of the two institutions. However, the Commission and the NLA have noted that there are areas of common interest and functions that require close working relations between them. Accordingly, this article is aimed at highlighting the manner in which the Commission and the NLA are going to cooperate under the recently concluded MoU.

2. Manner of cooperation between the Commission and the NLA

To start with, it should be noted that MoUs are one way in which the Commission interacts with other institutions, however, the Commission also has extensive interaction on specific matters where appropriate. On a literal interpretation of section 3(1A) of the Competition Act, one may hurriedly

¹⁴ Section 3(1A)(a) of the Competition Act.

¹⁵ To date the Commission has concluded MOUs with the Independent Communications Authority of South Africa, Postal Regulator and the National Energy Regulator of South Africa on the basis of Section 21(1)(h) read together with sections 3(1A) (a)-(b) and 82 (1)-(3) of the Competition Act. The three MOUs may be accessed from the Commission website: http://www.compcom.co.za/resources/publications_notices.asp?level=2&child=4.

conclude that the Commission is only statutorily entitled to enter into MoUs with industry-specific regulators¹⁶ when concurrent jurisdiction is to be exercised on prohibited practices (Chapter 2) and mergers (Chapter 3). However, a purposive interpretation of competition policy points to the fact that competition in a market may not only be affected when a prohibited practice is perpetrated or a merger is taking place but also through regulatory mechanisms of industry-specific regulators. On this basis, the Commission may conclude a MoU to create a platform for the execution of its advocacy role even in instances where there is no substantial overlap between its functions and that of the other industry-specific regulator with regard to prohibited practices and mergers. The NLA's functions vis-à-vis those of the Commission serve as an example in this case.

In summary, the following are the points on which the Commission and the NLA are going to interact when necessary:

2.1. Applications for registration in respect of the manufacturing and/or distribution of liquor

With the coming into operation of the Liquor Act also came the legal avenue enabling the NLA to work together with the Commission on specific matters. Sections 11, 12 and 13 of Chapter 3 of the Liquor Act provides for the process to be followed when a person is applying to the Minister to be registered as manufacturer or distributor of liquor, or both. As it is the jurisdictional mandate of the NLA, all applications for the proposed registration as a macro manufacturer and/or distributor of liquor must be lodged with the NLA in terms of the provisions of Chapter 3 of the Liquor Act.

Of particular relevance for purposes of the Commission-NLA MoU is section 13(2)(a) of the Liquor Act. Before proposing any conditions on

a registration, the Minister, in terms of section 13(2)(a) read with sections 13(1)(c) and 12(2)(a) of the Liquor Act, may consult with the Commission when considering the extent to which a proposed registration as a macro-manufacturer or distributor of liquor will materially restrict or promote

- New entrants to the liquor industry;
- Job creation within the liquor industry;
- Diversity of ownership within the liquor industry;
- Efficiency of operation within the liquor;
- Exports; and
- Competition within the liquor industry



Clearly, what these provisions require is a competition assessment of an application to register as a macro manufacturer or distributor, or both of liquor. The words may consult in section 13(2)(a) of the Liquor Act means that the NLA is not obliged to refer all registration applications for a

competition analysis by the Commission and that the former will exercise its discretionary referral power. In a case where the NLA requests a competition assessment of a liquor registration application from the Commission, the latter undertakes to provide advice/input within thirty (30) business days of receipt of such request. This time allowance is flexible depending on the complexity of the referral. The NLA shall exercise its discretion on how to use the Commission's advice when deciding whether or not to conditionally or unconditionally grant the liquor registration.

2.2. Merger Transactions and transfer applications of liquor licenses

Merger Transactions

Merger control provisions are contained in Chapter 3 of the Competition Act. In this regard, Section 12(1)(a) provides that a merger occurs when or more firms directly or indirectly acquire or establish direct or indirect control over the whole or part of the business of another firm. A merger may be achieved in any manner including through the purchase or lease of shares, an interest or assets of other firms or amalgamation or other combination with the firm.¹⁷ Therefore, any transaction that involves the transfer of control of a firm's business (in whole or part) to another and also meets the required statutory merger thresholds must be lodged with the Commission in the prescribed manner and form. The MoU provides for consultation between the Commission and the NLA in instances where the former deems it necessary to get the latter's non-binding input for purposes of analyzing a proposed merger transaction in the liquor industry.

Transfer of liquor licences

The procedure for transferring liquor license registrations is provided for in Section 15 of the Liquor Act. Accordingly, all transfer applications

¹⁶ Report prepared by the Advocacy Working Group, ICN's Conference Naples, Italy, 2002, p30.

¹⁷ Section 12(1)(b) of the Competition Act.



falling under section 15 of the Liquor Act must be lodged with the NLA. However, parties to a transfer application are also obliged to notify such transactions with the Commission to the extent that the liquor licence transfer

- entails the acquisition of control by a liquor registrant over another liquor registrant's business; and
- falls within the required Competition Act merger thresholds.¹⁸

If a liquor license transfer application does not meet the required merger thresholds, the NLA may consult the Commission for purposes of a competition assessment of such transfer application as provided for by section 13(2)(a) read together with section 15(2)(b) of the Liquor Act.

2.3. Complaints

With regards to investigations of complaints or alleged offences by the Commission and the NLA, the MoU encourages the regulator without jurisdiction over a complaint before it to advise/inform the concerned complainants to lodge the complaint with the other regulator if the complaint happens to fall within the provisions of the respective legislations of either regulator. Besides the provision for the regulators to consult each when necessary, each regulator

shall solely deal with complaints that fall within its legislative ambit and still make independent determinations. Therefore, all complaints relating to conduct, practices or agreements in terms of Chapter 2 of the Competition Act must be lodged with the Commission. Chapter 2 prohibitions include, amongst others, price fixing, market allocation, minimum resale price maintenance and abuse of a dominant position through exclusionary acts such as price discrimination, predatory pricing and exclusive dealing

3. Conclusion

In anticipation of liquor registrations that the NLA may refer to the Commission for a competition assessment, it was then necessary to

conclude a formal type of arrangement between the two regulators for the primary purpose of facilitating such referrals. To practically give effect to the MoU, a joint working committee constituted by no more than three representatives from each regulator is to be established. This Joint working committee will interact as and when matters of mutual interest in the liquor industry arise. It should be noted that the signing of this MoU does not in any way alter the legislative power of each regulator to make its independent decisions. It is nevertheless the intention of the regulators to ensure that our interaction through this MoU positively contribute to the competitiveness of the liquor industry. The MoU has still to be gazetted for public information.



The Benefits of an Effective Compliance Programme

Companies are increasingly recognising that competition law compliance is a central component of effective business practice and organizational integrity in South Africa. In recent years there have been important

developments in corporate compliance more broadly, with the King Report on Corporate Governance for South Africa, 2002 (King II) and the Codes of Corporate Practices and Conduct (the Codes). For example, regulation 47 of the Banks Act 90 of 1990, as amended

(Banks Act) in particular mandates for the establishment by a bank of a compliance function attending to all regulatory compliance issues. However, effective compliance with the Competition Act has only recently been getting the attention it deserves.

¹⁸ Certain types of Joint ventures contemplated in section 15(4) of the Liquor Act are not immune to notification with the Commission. A 5 Commission guideline on the application of the merger provisions of the competition Act to joint ventures may be accessed on: http://www.compcom.co.za/resources/publications_newsletters_practitioner.asp.



By: Sbusiso Madonsela
Compliance Division

While private companies continue to pursue profit, on behalf of their shareholders, the importance of good corporate governance as a board responsibility has been clearly set out. King II recommends that the compliance function should have direct access to the company's board and the programme should be understood by the entire staff complement with the Board and the Executive at the forefront. Regulation 47 of the Banks Act details the roles and responsibilities of the compliance function and places ultimate responsibility for it in the hands of the institutions' management. Having a compliance function has, thus, become a necessity than just a 'play safe mentality' by companies in all the sectors of the economy.

There must also be an understanding that central to compliance with the regulatory framework is appropriate human behaviour. In practice, it is the decisions of individuals that, if not detected and remedied, breaches the regulatory regime, exposes the institution to reputational risks, and leads to the institution's image being tainted. No one wants to be associated with an institution that does not adhere to the country's laws.

For any business enterprise to succeed and gain public respect in South Africa, it ought to understand, amongst a range of government policies, South Africa's Competition

Policy and comply with the country's Competition Law, the Competition Act 89 of 1998, as amended (the Act). Failure to comply with the Act has a potential of leading to serious repercussions. It is therefore important that companies commit themselves by voluntarily adopting and implementing effective competition law compliance programmes. Such programmes should, as suggested in other jurisdictions, encompass and include the declaration of the commitment to competition laws by a company's executives; the creation of a compliance function / appointment of a compliance officer; formulation and dissemination of a compliance manual; operation of education programs; establishment of a monitoring system; providing sanctions to be meted to individuals who violate competition-

related laws; and the establishment of document management system.

The importance of such programmes has been evident in recent years when companies who have failed to comply with the Act have been exposed, with most of them suffering reputational integrity, losing public trust and losing huge sums of money by being fined by the Competition Tribunal (the Tribunal). Ultimately the shareholders feel the loss occasioned by the negative effects emanating from failure to comply with the regulatory framework and top management end up having to accept the blame for failure to implement and monitor their institutions' compliance with applicable legislation.

The Competition Tribunal ("the Tribunal") has in the past confirmed





several consent orders entered into by the Competition Commission (the Commission) with the parties that have fallen foul of the provisions of the Act. Some of the companies that have entered into consent orders with the Commission include Adcock Ingram Critical Care¹⁹ New Reclamation Group²⁰, Tiger Consumer Brands²¹ and South African Airways²². In all the consent agreements entered into and endorsed by the tribunal, the parties have undertaken to devise, implement and submit to the Commission 'a Compliance Programme' that will be

communicated to their staff members so that they understand the need and importance of complying with the Act. This proves the importance and greater emphasis placed by the competition authorities on regulatory compliance and/or the need for companies to devise effective competition law compliance programmes.

One of the significant benefits of having an effective compliance programme that adopts the recommendations of King II is that it lowers the impact of reputational and regulatory risk. Companies

are encouraged to emphasize the need to enhance their institutional compliance frameworks to be in line with regulatory expectations. Besides the fact that this initiative will lower the impact of reputational and regulatory risk, it also has a potential of opening up space in the economy for a fair and efficient competition for all. Moreover, when companies devise effective compliance programmes, they are in a better position to detect violations of the Act which also afford them an opportunity to quickly apply for leniency through the Commission's Corporate Leniency Policy.

Notes on Minority Protections

The ubiquitous principle of "majority rule", albeit in a different form, also applies to decisions of a company, and depending on how voting rights are structured in the articles of association or a shareholders' agreement, the number of shares usually determines the number of votes. The shareholder owning the majority of shares is likely to have the majority of votes in a shareholders' meeting and thus determine the important affairs of the company such as the composition of the board. Section 12 (2) of the Competition Act No. 89 of 1998, as amended, contains an implicit recognition of majority rule. A shareholder with a minority of voting rights, notwithstanding the fact that s/he might have invested in the company, has to yield to resolutions taken by the majority. The common law and the Companies Act No. 61 of 1973, as amended, under very limited circumstances such as in the case of wrongdoing, affords few legal remedies to minorities to approach a court for appropriate relief e.g. sections 252 and 266 of the Companies Act. However, these limited common law and statutory legal remedies cannot be used by a minority shareholder

to circumvent and scuttle lawful decisions taken by the majority, even if the minority shareholder might not agree with those decisions. In practice, contractually created veto rights are increasingly used as a tool to protect the interests of minority shareholders and serve as a bridle on certain majority decisions.

Minority shareholders are often accorded the right to veto certain significant decisions of the company which may potentially affect their financial interests as investors in a company. The majority shareholder or a shareholder with the majority of voting rights in a company may then be required to first obtain the consent of the minority shareholder before taking and implementing such decisions. Generally, these minority protections serve as an assurance to minorities that substantial changes affecting the structure and solvency of the company ("the essence of the company") will not be taken without their consent. These decisions may include for instance changes in the issued share capital structure, amendment of the articles and memorandum of association, resolution to voluntarily wind up the company e.t.c. These minority



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protections are usually inserted in shareholders' agreements, although in some instances they may be grafted into the articles of association. In some cases, loan agreements may confer veto rights on the creditor which are analogous minority protections.

It is up to the shareholders to negotiate and agree on the nature and content of the veto rights. Some veto rights hardly present any problems, and it might not be difficult to ascertain whether they fall within the bounds of minority protections. However there may be veto rights which extend to or have a bearing on the strategic

²⁰ 37/CR/Apr08.

²¹ 15/CR/Feb07.

²² 83/CR/Oct04.

Towards a fair and efficient economy for all

Where to get hold of us

Visit the Competition Commission online at www.compcom.co.za for more information about the Commission and the Act, as well as the rules and amendments to the Act. You may also forward enquiries, comments and letters to:

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