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To:	South African Venture Capital and Private Equity Association (SAVCA)
	East African Venture Capital and Private Equity Association (EAVCA)
Subject:	Merger notifications – the requirement under COMESA Competition Regulations
Date:	7 May 2014

A. Introduction

This note gives an overview on COMESA merger obligations which market players operating in the COMESA region need to be abreast with when making investments and acquisitions.

It is important to set out from the outset that the COMESA Competition Regulations (the "**Regulations**") create a supranational merger regime which imposes a mandatory pre-merger filing for entities operating in the COMESA. Accordingly, dealmakers should, at an early stage of designing and planning any mergers and acquisitions, make an assessment to determine whether a COMESA filing is warranted.

It is recognized that there are surrounding uncertainties in the interpretation of the Regulations which has been scrutinized by market players. The COMESA Competition Commission (the "**Commission**") has announced that it shall be taking steps to address these ambiguities. While the Regulations are technically in force and will continue to be in force pending the changes announced, it is our view that the lack of clarity makes it difficult for the relevant provisions of Regulations to be effectively enforced.

B. Background

The Common Market for Eastern and Southern Africa (the "**COMESA**") was established by the COMESA Treaty (the "**Treaty**") which was signed on 5 November 1993 and ratified on 8 December 1994. The Treaty empowers the Council of Ministers of COMESA to make regulations to regulate competition within the member states[1]. Consequently, the Regulations were promulgated and ratified by the Council of Ministers on 17th December 2004.

The Regulations has established the Commission which began its operations in January 2013 and has as its main functions investigating anti-competitive practices between member states, reviewing regional competition policy, promoting national competition laws and co-operate with competition authorities of member states.

[1] Member states are: Burundi, Comoros, the Democratic Republic of Congo, Djibouti, Eritrea, Ethiopia, Kenya, Libya, Madagascar, Mauritius, Rwanda, Seychelles, Sudan, Swaziland, Uganda, Zambia, Zimbabwe and the Republics of the Egypt and Malawi.

The Treaty imposes on the member states the obligation to take the necessary steps and measures to secure the enactment of and the continuation of such legislation to give effect to the Treaty and to confer upon the COMESA the legal capacity and personality required for the performance of its functions. However, even if a member state has not enacted the Treaty into its domestic laws, the Treaty obligations are still binding on the signatory country within the COMESA; in the case of Polytol Paints & Adhesives Manufacturers v Republic of Mauritius[2], the COMESA Court of Justice issued a ruling about the applicability of the Treaty within member states (including those which have not adopted the Treaty as local laws into their jurisdictions).

C. Scope of the Regulations

The Regulations apply:

- to all economic activities whether conducted by private or public persons within, or having an effect within, the COMESA; or
- to conduct covering anti-competitive business practices and conduct, mergers and acquisitions, consumer protection, which have an appreciable effect on trade between member states and which restrict competition in the common market.

<u>Exclusions from Regulations:</u>

The Regulations do not apply to:

- arrangements for collective bargaining on behalf of employees and employers for the purpose of fixing terms and conditions of employment;
- activities of trade unions and associations directed at advancing the terms and conditions of employment of their members; or
- activities of professional associations designed to develop or enforce professional standards reasonably necessary for the protection of the public interest.

The Regulations do not derogate from the direct enjoyment of the privileges and protections conferred by the other laws protecting intellectual property but the Regulations apply to the use of such property in a manner as to cause anti-competitiveness effects prohibited herein.

D. Merger control

The Regulations have established a framework to prohibit anti-competitive practices and has introduced a merger control regime for transactions with a regional COMESA dimension.

The COMESA merger review regime is intended to be a one-stop shop for all COMESA members. The However certain competition authorities in member states however, do not accept that only a COMESA filing will supersede the need for filing at the domestic level and the domestic rules will still be applicable, hence, resulting in additional costs. Therefore, it is unclear as to whether the Commission is the only body to be notified for mergers meeting the criteria for notification under the Regulations.

a. General Considerations

Transactions meeting the criteria of notifiable merger as set out in the Regulations need to be

[2] Polytol Paints & Adhesives Manufacturers v Republic of Mauritius, ref. 1 of 2012, judgment of 31 August 2013.

notified to the Commission.

In order to improve transparency and predictability of the merger control regime, the Commission has issued draft merger assessment guidelines under the COMESA Competition Regulations ("**Draft Guidelines**") in April 2013. The Draft Guidelines are aimed only for general guidance and are not to be relied on as a statement of law relating to the Regulations. We have taken the Draft Guidelines into account when analyzing certain matters herein; however, we wish to highlight that these Draft Guidelines have not yet been adopted and are reported to be subject to further changes. Please refer to the "Developments" section below.

b. What gives rise to a merger notification under the COMESA merger regime?

Under the Regulations, for transactions to be caught under the merger control regime, a transaction would need to (1) fall into the definition of merger, and (2) have a regional element which requires operation in COMESA and fulfilling the applicable threshold.

1) A merger

The Regulations define merger as the direct and indirect acquisition or establishment of a controlling interest by one or more persons in the whole or part of the business of a competitor, supplier, customer or other person whether that controlling interest is achieved by way of purchase or lease of the shares or assets of or the amalgamation or combination with a competitor, supplier, customer or other person or any other means.

Further, controlling interest, in relation to:

- any undertaking, means any interest which enables the holder thereof to exercise, directly or indirectly, any control whatsoever over the activities or assets of the undertaking; and
- any asset, means any interest which enables the holder thereof to exercise, directly or indirectly, any control whatsoever over the asset.

What is control?
The Draft Guidelines aim to provide further clarity on "control". Control is constituted by rights, contracts or any other means which, either separately or in combination and having regard to the considerations of fact or law involved, confer the possibility of exercising decisive influence on an undertaking.

A list of circumstances in which the Commission will deem a person to be exercising control is provided in the Draft Guidelines, for instance beneficially owning more than one half of the issued share capital, entitlement to cast a majority of votes at a general meeting, ability to appoint or veto the appointment of a majority of the directors.

2) Regional element

(i) For the merger control regime to be applicable, both acquiring firm and target firm or either the acquiring firm or target firm operate in two or more member states[3].
Therefore this would mean in any given transaction, the operation of the parties would need to be examined. The Draft Guidelines provide examples, for instance:

[3] Article 23(3)(a) of the Regulations

- both the acquiring and target firms operate in two or more member states: Company A, the acquiring firm operates in Zambia and Malawi and Company B, the target firm operates in Zambia and Malawi; or Company A, the acquiring firm operates in Zambia and Malawi and Company B, the target firm operates in Ethiopia and Zambia,

- either the acquiring firm or the target firm operates in two or more COMESA member states: Company A, the acquiring firm, operates in Kenya and Seychelles and Company B, the target firm, has no operations in any COMESA Member States or vice versa.

The term "operate" is not defined in the Regulations; however through the Draft Guidelines it is proposed that this term be given a wide interpretation including being "directly domiciled in a member state", "derives turnover in two or more Member States", "have operations through exports, imports, subsidiaries etc. in a Member State".

(ii) the threshold of combined annual takeover or assets is exceeded.

The threshold is currently set at zero. This means that where any merging party meeting the above regional criteria have to file a merger notification. From our discussion with the Commission, we understand that the zero threshold is being re-visited. Please refer to the "developments" section below.

When assessing the merger situation, the "scope of application" section of the Regulations is also relevant – the Regulations apply to conduct covered by inter alia Part 4 (the Merger obligations) which have an "appreciable effect" on trade between member states and which restrict competition in the common market. "Appreciable effect" is not defined. However for any conduct to fall within the purview of the Regulations, it must have effects of a certain magnitude to have an impact on the common market. The Draft Guidelines, unfortunately, do not address this point which could possibly be used to address the non-applicability of the merger regime to mergers with no or minimal effect on competition in the region.

c. Non-notifiable merger

It should be noted that the Regulations make a distinction between notifiable and non-notifiable mergers. Notifiable merger is a merger or proposed merger with a regional dimension with a value at or above the prescribed threshold, whereas non-notifiable merger is a merger or proposed merger with a value below the prescribed threshold. Consequently at this stage, a notifiable merger will be only a merger or proposed merger with a regional dimension since the threshold requirement is not really applicable as it is currently zero. The Commission may require the parties of a non-notifiable merger to notify the merger if the Commission is of the view the merger is likely to substantially prevent or lessen competition or is likely to be contrary to public interest.

d. Notification and filing process

1) When are parties required to do the notification?

A party to a merger has to notify to the Commission the proposed merger in writing as soon as it is practicable but in no event later than 30 days of the parties' decision to merge. The Draft Guidelines defines the terms "decision to merge" to mean an established concurrence of wills between the merging parties in the pursuit of a merger objective.

2) How to notify a merger?

The merger notification requires the payment of a filing fee and a notification form which requires extensive information. The Draft Guidelines clarify that the Commission accepts joint notification and notification from either party.

The current fee is calculated at 0.5% or COM$ 500,000, or whichever is lower of the combined annual turnover or combined value of assets in the COMESA, whichever is the higher. Therefore, COM$500,000 is the maximum fee payable for merger notification.

3) Review by the Commission

The Commission examines the notification upon receipt of the complete set of information and makes a decision on the notification within 120 days after receiving the notification. However, if the notification is not complete, the review period starts on the day following receipt of complete information. Further, the Commission may extend the 120-day period and will inform the parties accordingly.

In determining whether a merger is likely substantially to prevent or lessen competition, the Commission takes into account a number of factors relating to characteristics of the market and including the particular situation of the parties such as:

- the actual and potential level of import competition in the market;
- the ease of entry into the market, including tariff and regulatory barriers;
- the level, trends of concentration and history of collusion in the market; the degree of countervailing power in the market;
- the likelihood that the acquisition would result in the merged parties having market power;
- the dynamic characteristics of the market including growth, innovation and product differentiation;
- the nature and extent of vertical integration in the market;
- whether the business or part of the business of a party to the merger or proposed merger has failed or likely to fail; and
- whether the merger will result in the removal of efficient competition.

If it appears to the Commission that there is a likely substantial lessening of competition, it would not de facto prohibit it but then it takes into account whether the merger will result in any technological efficiency or other pro-competitive gains sufficient to offset the effects of any prevention or lessening of competition arising out of the merger, or whether the merger may be justified on substantial public interest grounds.

The Draft Guidelines also provide that the Commission considers any substantiated efficiency claim in the competitive assessment of a proposed merger which may be in the form of consumer benefits arising in markets other than the market at issue, where the lessening of

competition is found but there are benefits to future consumers. The Draft Guidelines also provides that in order for the Commission to be satisfied that the efficiencies gained as a result of the merger outweigh any lessening of competition, the Commission must be satisfied that:

(a) the efficiencies benefit the consumer;
(b) the efficiencies are merger-specific; and
(c) the efficiencies are verifiable.

In addition to the above, the Draft Guidelines requires the Commission to conduct an entry analysis as part of the competitive assessment of a proposed merger and in this process, the Commission will examine whether entry is likely or whether potential entry is likely to constrain the behaviour of the merging firms post-merger.

4) Penalty

Failure to notify a notifiable merger may attract a penalty imposed by the Commission and when determining the appropriate penalty, the Commission takes into consideration the following factors: the nature, duration, gravity and extent of the contravention, any loss or damage suffered as a result of the contravention, the behavior of the parties concerned, the market circumstances, benefits and the degree to which the parties have co-operated with the Commission. According to the Regulations, a notifiable merger which has not been notified to the Commission will not have any legal effect in the common market and no rights and obligations of the parties in terms of the merger agreement are legally enforceable in the common market.

E. Developments

Whilst the introduction of a merger regime in the common market is a big step, there still remains a number of issues for dealmakers, for instance wide thresholds which can extend to foreign companies, high filing fees and long review periods.

The current turnover or asset threshold under the Regulations is set at zero, and the manner in which the thresholds are drafted in the Regulations indicate that even de minimis activities can trigger a notification requirement.

The Draft Guidelines have helped in clarifying certain ambiguities in the Regulations such as the procedural steps and substantive analysis in respect of merger assessment, however, a number of issues remain unresolved. For instance, the Draft Guidelines do not address the uncertainty over whether the requirement for a filing to the Commission precludes the need to make filings to any national competition authorities. Opinions differ on this issue in the COMESA member states. For example, in Mauritius the Competition Act has not been amended to include the Treaty provisions. In this respect, it is important to note that eight COMESA member states have competition authorities, being Mauritius, Malawi, Swaziland, Egypt, Seychelles, Kenya, Zambia and Zimbabwe. Hence the concept of “one-stop shop” for merger notification procedure as date remains unclear.

It is recognised that the Commission has been very open and transparent about the difficulties it has encountered in the application of the Regulations and that it is prepared to propose business friendly amendments to the rules. The Commission is looking into making the competition regime clearer and more business friendly for instance (i) raising the threshold, (ii) clarifying the

term “operate” (thus addressing the wide interpretation of same), (iii) aligning of filing fees with international practice, (iv) possibly looking into the 120-day review period, and (v) clarifying the terms “appreciable effect on trade between member states”. In our discussions with the Commission it also came to light that the Draft Guidelines are being reviewed and amended to take into consideration the need for the aforesaid clarifications and it is expected that the updated draft merger assessment guidelines will be made available by July 2014.

F. Conclusion

The enforcement of the Regulations is one of the greatest milestones in the regional integration agenda. The Regulations have established a one-stop-shop merger filing procedures across the COMESA region. However, due to ambiguities in COMESA Regulations, it has now essential for the Draft Guidelines to be in force and to address some additional issues so as to remove the current uncertainty over jurisdiction, to streamline the merger review process in the COMESA region and to avoid the risk of duplicative and conflicting merger reviews. Despite the uncertainties surrounding the merger regime, market players should not lose sight that there is a mandatory pre-merger filing which they need to assess prior to implementing any proposed merger.

The purpose of this note is to provide an overview of the merger filing obligations under the COMESA Regulations as at date. It does not contain a full analysis of the law and each party’s position should be assessed on a case by case basis and specific legal advice must be taken on any particular matter which concerns such party. If you require any advice or further information, please do not hesitate to contact us.

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