South Africa Small Merger Notifications:

The SACC joins the European Commission in expanding the application of small merger notifications to digital markets

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Introduction

The South African Competition Commission ("SACC") recently published amended draft guidelines for notification of small mergers in "digital markets" ("Digital Merger Guidelines").

The Digital Merger Guidelines seek to amend the SACC's existing guidelines on small merger notification and marks a significant change to the assessment of mergers in South Africa. Judging from past experiences, the Digital Merger Guidelines are unlikely to be changed significantly, before being made final.

Background to Digital Merger Guidelines

Competition discourse in recent years have been largely centered around the regulation of digital markets. Various agencies internationally have considered and introduced different mechanisms of dealing with the perceived dangers of digital markets. Similarly so, the SACC also recently shifted focus to the regulation of digital markets, starting with its informal study and report, titled "Competition in the Digital Economy" ("**Report**").

The Report, although informal and non-binding, now effectively serves as the SACC's framework for the future regulation of digital markets. In this regard, the Report identified various market characteristics which, the SACC believes, warrant deviation from the traditional approach to competition regulation in South Africa. For current purposes, this includes most notably:

- concentration arising from first-mover advantage, data accumulation and network

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- effects (so called "tipping markets"), which necessitates pro-active intervention; and
- merger notification thresholds which, currently, allow most mergers in digital markets to be implemented, without competition scrutiny, as they are primarily turnover or asset based, meaning that the acquisition of various small startups who, individually, are insignificant and do not trigger the thresholds, are collectively important ("creeping mergers").

This is also a stated objective in the Digital Merger Guidelines, which state that: "*There are concerns that these potentially anti-competitive acquisitions are escaping regulatory scrutiny due the acquisitions taking place at an early stage in the life of the target before they have generated sufficient turnover that would trigger merger notification as set by the turnover thresholds*".

The potentially harmful effects of 'creeping mergers' and 'killer acquisitions' are well documented. The SACC has, however, gone one step further to include, in its definition (informally), transactions which are significant internationally (such as Facebook's acquisition of WhatsApp), but which do not meet the thresholds in South Africa. In this regard, the SACC also cites the Google/Fitbit merger, which was not notifiable in South Africa, but which the SACC insisted must be notified.

It is necessary to note that the recent amendment to the Competition Act already introduced the concept of 'creeping mergers' into South African merger control. In this regard, the Competition Act, as amended, require the SACC to assess:

- the extent of ownership by a party to a merger in other firms in a related market;
- the extent to which a party to the merger is related to other firms in related markets, including through common members or directors; and
- any other mergers engaged in by a party to a merger for a period to be stipulated by the Commission.

While these provisions have not yet been fully put to the test, it seems evident that these provisions aid only in ensuring a 'holistic consideration' of the potential effects of a notifiable merger, they fall short in dealing with the identified concerns in the digital economy – being non-notifiable mergers.

Small Merger Notifications South Africa

Small merger notifications are not novel. Competition agencies, including the SACC, have in various forms, reserved the powers to assess transactions which do not meet the statutory merger thresholds. In South Africa, this was done through the publication of the SACC's Guidelines on the notification of small mergers ("**Guidelines**"). The Guidelines required that small mergers be notified, voluntarily, where a party to the proposed transaction was under investigation by the SACC or a respondent to complaint proceedings before the Competition Tribunal.

The intention and rationale were clear, where a party was under investigation (or prosecution) for having engaged in anti-competitive conduct, the proposed transaction had to be assessed to consider whether the proposed transaction may harm competition (or the pending case under investigation/prosecution). Put differently, there was a clear and pre-defined potential harm.

The Digital Merger Guidelines seek to extend the application of the Guidelines to require the notification of small mergers where a party to the transaction "*operate in one or more digital markets(s)*" and any of the following thresholds are met:

- the purchase consideration exceeds R190 million, provided the target has activities in South Africa;
- the purchase consideration is less than R190 million (e.g. the acquisition of 25% shareholding), but the target value (100% shareholding) exceeds R190 million, provided the target has activities in South Africa and the acquisition amounts to a merger (change of control);
- at least one of the parties to the transaction has a market share of 35% or more in at least one digital market; or
- the merger results in the merged entity being 'dominant' in the market (as defined in the Competition Act).

Small mergers are to be notified by way of a "letter" (as opposed to the statutory merger filing forms). Further in terms of the Digital Merger Guidelines, the letter must contain, "sufficient details" regarding: the parties; the proposed transaction; and the markets in which the parties operate.
Most notably, the transaction is not limited to the 'relevant market' for purposes of the competition assessment but may include related markets.

Small Mergers in the EU and Germany

The European Commission (EC) has also recently published guidance on the application of Article 22 of the European Merger Regulation (ECMR) in order to, *inter alia*, tackle mergers concerning digital markets, which fall short of the merger filing thresholds at both EU and Member States level. Article 22 of the ECMR allows for the referral of a transaction, which "threatens to significantly affect competition". In such cases, the EC may 'invite' Member States to request a referral of the merger from national level to the EC, resulting in a notification at EU level, even if the transaction does not fulfil neither the EU nor the respective national turnover thresholds. This may further result in an uncertainty for the undertakings concerned as to whether their proposed transaction is to be notified and assessed by the EC.

Interestingly, the guidance on the Application of Article 22 ECMR only includes a "reappraisal of the application", as the European Commission puts it, as the current wording of Article 22 ECMR already includes a referral mechanism for transactions not fulfilling the merger control thresholds in the respective Member State. This, however, did not play any role in the EC's referral practice up to date.
The EC's guidance now seeks to change its practice, particularly to aim at the prevention of so-called killer acquisitions in the digital economy – where potentially problematic transactions are not notified due to target thresholds not being met. The continued role and effectiveness of merger thresholds, particularly in relation to the digital economy, has long been debated in the EU. This is especially true, as the already mentioned Facebook/WhatsApp merger (used as a case in point by the SACC in its Report) was only notified with the EC after referral requests of some Member States based on Article 22 ECMR, as the merger fell short of the EU turnover thresholds, and most national thresholds.

To address this, some Member States, especially Germany and Austria introduced a "transaction value"-merger threshold, to ensure the notification of transactions involving a start-up 'unicorn' not (yet) achieving a substantial turnover. This threshold, *inter alia*, requires a filing based on the "consideration of the transaction", usually being the purchase price, exceeding a certain threshold. However, this novella in 2017 did not result in any significant increase in merger filings. In Germany, less than 10 (of roughly 2000) mergers per year were notified based on this new provision. Further, it remains unclear whether a threshold based on the target's purchase price is, indeed, better placed to evaluate the parties' market position. This is especially true when considering that none of the mergers notified under this provision entered the so-called 2nd phase, meaning that all such mergers were cleared (or withdrawn by the parties).

In light of the above, the EC guidance highlights a few important considerations relevant to the South Africa Digital Merger Guidelines:

1. the EC guidance notes that the 'transaction value' thresholds, which had been introduced in Germany and Austria, as said, do not appear to be effective; and
2. with the increased number of merger filings likely to follow under the new guidelines, it is necessary to ensure a balanced approach, through the implementation of measures to ensure the "simplification of merger procedures".

Conclusion

Small mergers are not mandatorily notifiable. The Competition Act does, however, provide that the SACC may, within six months after the transaction has been implemented, require the transaction to be notified.

This SACC's powers in terms of section 13(3) of the Act is discretionary. In this regard, the SACC may call for a merger to be notified where, in the view of the SACC, the merger may substantially prevent or lessen competition or cannot be justified on public interest grounds.

The inclusion of specific provisions in the Digital Merger Guidelines suggest, by necessary implication, that mergers in the digital market may substantially prevent or lessen competition or importantly, negatively impact public interest.

Defining the relevant competitive theory of harm in the digital economy is notoriously difficult. It is notably, however, that in terms of the Competition Act, as amended, public interest considerations (and by implication 'national interest') have been elevated to a separate and self-standing assessment. Public interest, in this context, includes most notably the "*ability of small and medium businesses or firms controlled by historically disadvantaged persons to effectively enter into, participate in or expand*". Accordingly, the South African merger control framework, as amended, provide the SACC with a unique ability to assess mergers in the digital market on grounds other than pure competition grounds.

In a separate but related issue, the SACC have initiated a market inquiry into the market dynamics in online intermediation platform – which is seen to be an 'emergent market' in South Africa and the SACC considers effective competition between these platforms to be key to digital expansion. In doing so, the SACC already signaled a clear intent to focus its assessment of digital markets on the less complex assessment of creating a space for small business to enter and operate. Furthermore, the insights which the SACC can gather through the less adversarial market inquiry, is likely to provide it with the valuable insights, which it may then apply to its merger assessments.

The SACC's unique ability to consider expanded 'public interest' consideration in merger control, coupled with the SACC's clear intention to require the notification of all mergers in the digital market, including small mergers, pose a significant risk to firms operating in the digital market.
Concerns regarding the SACC's Digital Merger Guidelines are exacerbated by the fact that these guidelines have failed to account for important issues, highlighted in the EC guidance (or addressed some of the perceived failures of the EC guidance). In this regard, it has failed to provide sufficient clarity regarding a simplified process to be followed in respect of such small mergers. Moreover, the Digital Merger Guidelines may add uncertainty to transacting parties, internationally, without any appreciable benefit to competition.

This risk in relation to the Digital Merger Guidelines is not unique to South Africa. Similar ambiguity already exists in the EU with the application of the "new" Article 22 ECMR. It may be safe to assume that any transaction filed in the EU on a 'cautionary basis', which may have a jurisdictional nexus to South Africa, ought similarly to be notified in South Africa, in terms of the Digital Merger Guidelines (once finalized).

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