Submission in response to the Competition Amendment Bill, 2018 (as amended by the Portfolio Committee on Economic Development - B23B_2018)

A - Introduction

The Helen Suzman Foundation ("**HSF**") welcomes the opportunity to make submissions to the Select Committee on Economic and Business Development ("**the Select Committee**") on the Competition Amendment Bill, 2018 [B23B-2018] ("**the Bill**"). Should the opportunity arise, the HSF wishes to make oral presentations to the Select Committee.

The HSF is a non-governmental organisation whose main objective is to defend the values of our constitutional democracy in South Africa, with a focus on the rule of law, good governance and accountability.

The HSF endorses the objectives of the Bill, namely to address high levels of concentration and the skewed ownership profile of the economy, and encourages the promotion of administrative efficiency of the Competition Commission and Tribunal. We recognise the Constitutional imperative found in section 198 of the Constitution, which sets out the governing principles of national security in the Republic. Moreover, we recognise that national security is subject to the authority of both Parliament and the national executive.

We have previously commented on this Bill, and have appeared before the Portfolio Committee during the public hearing phase to expand on our recommendations. We are disappointed to note that none of our suggestions have been positively considered in the formation of this iteration of the Bill. Our concerns, therefore, remain the same and are compounded by the further amendments presented in this version of the Bill.

The Helen Suzman Foundation Trust
Trust No: 1455/93
NPO Reg. No. 036-281-NPO
www.hsf.org.za

Postnet Suite 130, Private Bag
x2600, Houghton 2041
Tel: +27 11 482 2872
Fax: +27 11 482 8468

6 Sherborne Road
Parktown
2193
Email:info@hsf.org.za

B – Scope of the Submission

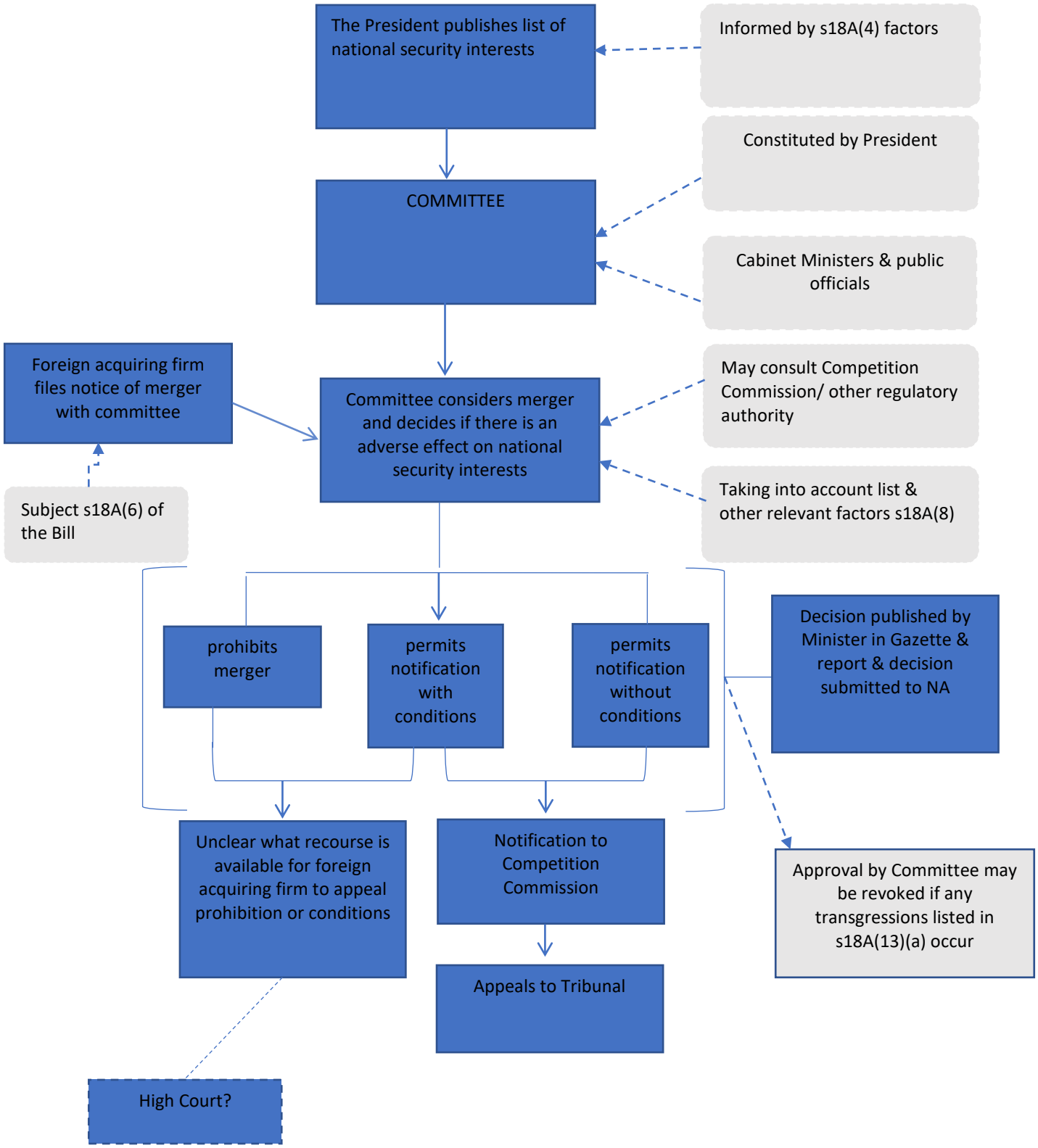
This submission is confined to comments relating to s 18A of the Bill. With experience in interdisciplinary research and policy work, the HSF is well placed to engage with an amendment of this nature as it relates to complex matters beyond the boundaries of economics and competition law.

The following concerns will be addressed in this submission:

1. The appropriateness of locating s 18A in the Competition Act.
2. The absence of certain definitions.
3. A lack of clarity with regards to the appeal and review processes.
4. The pre-decision engagement process.
5. List of factors in s 18A(4).
6. Notification requirements of intended merger.
7. The President may delegate determination in s 18A(15).
8. The appropriate balance between interests of national security and protection of an open investment policy.

C - The Structure to be established by S18A

The HSF understands the process of intervening in a merger by a foreign acquiring firm to take place in the following way:



This basic illustration provides a framework for identifying where section 18A lacks clarity and the consequential uncertainty.

D – Our Suggestions

1. Appropriateness of locating s 18A in the Competition Act

South Africa does not have an integrated national security policy. We caution the Committee against pursuing a national security strategy in the arena of competition law, in the absence of a coherent national security policy.

Other jurisdictions have taken care to either draft similar provisions into specific defence legislation or create dedicated Acts which set out the review and decision - making process. We believe that a similar approach can be adopted without compromising the objectives of this Bill. The legislative framework of South Africa's competition regime is ill-suited to the certainty and clarity required in interpreting national security interests. This is evident through the formation of the Committee which assumes almost all investigative and decision-making power. The diminished role of the Competition Commission and Tribunal, two bodies which should act as prime arbiters in adjudicating questions of Competition law, again evidence the inappropriateness of locating S18A within the Competition Act.

We consider three comparative examples: the United States, Australia and Canada.

The United States: The United States model can be found in s 721 of the Defense Production Act of 1950, also known as the "Exon-Florio Amendment". This section entitled "Authority to review certain mergers, acquisitions, and takeovers" effectively delegates the investigation of transactions to the Committee on Foreign Investment in the United States (CFIUS) while the President retains the authority to block or approve transactions.

The CFIUS enlists senior officials within their respective departments. These include the Secretary of Treasury, the Secretary of Homeland Security, the Secretary of Commerce, the Secretary of Defense, the Secretary of State, the Attorney General of the United States, the Secretary of Energy, the Secretary of Labor (non-voting, ex officio), and the Director of National Intelligence (non-voting, ex officio).

The President of the United States may also determine if it is appropriate to include the heads of any other executive department, agency or office generally or on a case-by-case basis.

The Exon-Florio Amendment defines "control" as having the meaning "given to such term in regulations which the Committee shall prescribe" and "covered transaction" as "any merger, acquisition, or takeover that is proposed or pending after August 23, 1988, by or with any foreign person which could result in foreign control of any person in interstate commerce in the United States."[1]

[1] Reform of CFIUS is currently being debated in the United States through the proposal of the 'The Foreign Investment Risk Review Modernization Act' which seeks to expand the definition of "covered transaction" beyond those that could result in control of a U.S. business by a foreign person. The HSF believes legislative reform of this nature is too far-reaching and overall will weaken competitiveness

Australia: In Australia, the decision to approve or deny a foreign investment application rests with the Treasurer of Australia - who consults with the Foreign Investment Review Board (FIRB). The legislative framework for foreign investment policy is a complex set of statute, regulations and policy geared at strengthening oversight and review mechanisms.

The Foreign Acquisitions and Takeovers Act 1975 defines "foreign entity" as an "entity that is not an Australian entity."

Canada: Canada enacted the Investment Canada Act which is administered by the Investment Review Division (IRD), a government department situate in the Ministry of Innovation, Science and Economic Development Canada (ISED). The IRD works together with the Minister of ISED, the Minister of Public Safety and Emergency Preparedness whereafter the proposed investment is referred to Cabinet (the Prime Minister and appointed Ministers) who may order a formal review to test for adverse national security risks. This Cabinet-ordered review process is an investigative process which involves Public Safety Canada - the security and intelligence agency of Canada. Other investigative bodies as set out in the National Security Review of Investments Regulations are also involved.

The Investment Canada Act defines "non-Canadian" as meaning "an individual, a government or an agency thereof or an entity that is not a Canadian; (non-Canadien)."

2. Definitional issues

a. 'a Committee' is not defined in the Act or the Bill. We suggest that the definition reads as follows:

"means the standing committee as constituted by the President of the Republic, tasked with determining the national security threat or interest occasioned by a merger involving a foreign acquiring firm";

The value of a standing committee as opposed to an *ad hoc* one is that it will ensure consistency in the way decisions are made and it will enable the committee to establish a streamlined administrative process of notification and correspondence. Allowance for external consultation is made in s 18A(9). This means that the permanence of the committee will not inhibit the ability to seek input from experts, the Competition Commission and other relevant institutions.

S 18A(2) of the Bill allows the President of the Republic of South Africa to appoint Cabinet members as well as "other public officials" to the Committee. Given the high-level determination sought to be made, the composition of the Committee should be stipulated to cater for officials in senior positions with the requisite expertise and experience, and from relevant departments or portfolios.

We specifically suggest that high-ranking senior officials from Economic Development, Trade and Industry, State Security, National Intelligence, Treasury and Policing be identified as necessary members of the Committee.

b. 'Foreign acquiring firm' includes the definition of a firm "whose place of effective management is outside the Republic". There is no provided definition of "effective management", leaving the term undesirably vague. This creates the possibility for an inconsistent application of which firms may be considered as "foreign acquiring".

We propose that the deficiency be remedied as follows:

> That "effective management" be clearly defined within the definitions to make the intention of the drafters clear, and to create certainty as to who the provision applies to.

c. The primary **'target firm'** insofar as s 18A is concerned is unclear. We propose that s 12(1) is amended to indicate that the section applies to mergers between a foreign acquiring firm and a South African target firm. The subsection should be amended to read as follows:

> "(1) The President must constitute a Committee which must be responsible for considering in terms of this section whether the implementation of a merger involving a *foreign acquiring firm* and a South African target firm, being a firm which carries out its business in South Africa, may have an adverse effect on the national security interests of the Republic."

The Bill cannot reasonably be interpreted to include a foreign-to-foreign transaction where the target firm merely derives revenue from South Africa but has no physical presence – it is highly unlikely that a transaction of this nature will raise national security concerns. Defining the target firm will avoid a situation where the parties to a foreign-to-foreign transaction unnecessarily commence the process of notifying the Committee in terms s 18A.

3. Appeal and review mechanisms

S 18A makes no provision for an aggrieved party to challenge a decision taken by the Committee established in terms of this section.

If the situation arises where the Committee decides to prohibit a merger in terms of s 18A and a foreign acquiring firm is unhappy with this outcome, what recourse is there? Without specification in the Bill, the foreign acquiring firm would have to approach the High Court of South Africa. The fact that the decision relates to national security interests presumably precludes the Competition Commission, Tribunal or Competition Appeal Court from adjudicating on the matter, on the grounds that they lack the relevant expertise.

Subsections (11), (12), (13) and (14) in this iteration of the Bill amplifies the need for a clear and detailed appeals process, as suggested below, since they impose new requirements and obligations on merging parties with no recourse for review or appeal. The absence of such mechanisms reinforces an unfair power dynamic between the Committee and the merging parties. It allows the Committee to exert its decision-making power without the provision of requisite checks and balances to ensure that such exercise is not arbitrary, unlawful or irrational. We envisage legal challenges from merging parties should the Select Committee fail to incorporate such mechanisms into the Bill.

External review/appeal mechanisms

The roles of the Competition Commission, Tribunal and Appeal Court must be made clear in the Bill as regards the review and appeals processes of decisions taken by the Committee. If they are precluded from adjudicating over a decision of the Committee or taking a decision on review, this must be specified and the appropriate forum, such as the courts, must be stipulated.

Internal review/appeal mechanisms

Review can occur internally, at the Committee stage. The HSF recommends the inclusion of an internal review mechanism whereby parties can challenge a decision of the Committee before seeking relief from a court. A good model of this can be found in s 41(4)(b)(iv) of the Promotion of Access to Information Act[2] (PAIA) whereby a requester of information may lodge an internal appeal or application with a court against the refusal of an application.

4. Pre-decision Engagement

The Bill does not make provision for parties to engage with the Committee prior to it taking a decision - either to mitigate or negotiate merger conditions that may lessen the risk of rejection on the grounds of national security concerns.

Models for effective pre-decision engagement or condition setting can be drawn from the USA, Canadian and Australian models.

- The United States includes provision in the Exon-Florio Amendment in Section 721 (l) for “Mitigation, Tracking, and Post Consummation Monitoring and Enforcement”, for the CFIUS to “negotiate, enter into or impose, and enforce any agreement or condition with any party to the covered transaction in order to mitigate any threat to the national security of the United States that arises as a result of the covered transaction.”

[2] Act 2 of 2000.

- In Canada, review of this nature may take place before or after the transaction. The Canadian government may impose terms or conditions or ask for undertakings to mitigate risks to national security interests, in a similar manner to the United States model.

- Australia invites foreign investors to engage with its Foreign Investment Review Board (FIRB) in order to explore options of structuring a transaction so that it has a higher chance of being approved.

The HSF strongly urges the inclusion of a provision in the Bill that allows the Committee to afford merging parties an opportunity to commit to conditions or take certain actions so as to satisfy the Committee that the merger will not adversely affect South Africa's national security interests.

The Act, once passed, should seek to encourage foreign investment by making it attractive for firms to enter and compete in the South African market. The positive impact this will have on economic growth and employment is obvious. This need not come at the expense of the development of our local industries and business. The State can still play a supportive role in growing and strengthening local markets while also incentivising foreign firms to do business in South Africa.

The Bill, particularly through the introduction of s 18A, does precisely the opposite. It over-bureaucratises this process through unilateral and burdensome administrative obstacles which risk acting as a disincentive for foreign firms.

5. List of factors in s 18A(4)

In determining what constitutes national security interests the President must consider all relevant factors. S 18A(4) elaborates on one of these factors being the potential impact of a merger transaction on, *inter alia,* the Republic's defence capabilities and interests; the economic and social stability and the Republic's international interests, including foreign relationships. The list of factors should serve as a guiding criterion which assist the President in drafting regulations defining national security interests, which are specific, clear and focussed. Instead, subsection 4 contains very broad and vague factors which drastically widen the scope of what constitutes a national security interest and is therefore open to potential abuse.

The HSF recommends amending this subsection to include narrower, more detailed factors relating to national security interests. An example of more limited factors for consideration appears in s 41(2) of PAIA.[3]

[3] These are factors which an information officer may rely on when refusing to disclose certain information on the grounds of defence, security and international relations of the Republic.

6. S 18A(6) and S 18A(11): Notification of intended merger

S 18A(6) places an obligation on the foreign acquiring firm to notify the Competition Commission of an intended merger in terms of s 13(1), and at the same time notify the Committee if such merger falls within the list of national security interests. However, s 18A(11) prohibits the Commission from considering any merger in terms of s 12A if the foreign acquiring firm failed to notify the Committee in terms of s 18A(6). This may be a drafting error since subsection 6 clearly refers to mergers in terms of s 13(1). Moreover, when it comes to the sequence of notification to the Competition Commission and the Committee, subsection 6 states "at the same time", however s 18A(11) makes it clear that the Committee must have been notified *prior* to the Commission. These two sections should be revised to make it clear what the notification requirements on the foreign acquiring firm are.

The preferred approach, we suggest, would be to dispense with the notification provisions as they are presently drafted altogether, and that they be redrafted to shift the onus of notifying the Committee to the Competition Commission.

It is unclear why the onus of notifying the Committee falls to the foreign acquiring firm. Not only does this requirement rely on the foreign acquiring firm being able to reliably identify whether the merger concerns a national security interest, it also assumes that any failure to notify the Committee will be done in bad faith and is thus deserving of penalties or revocation. We propose that shifting this onus to the Competition Commission will be a more cost-effective and efficient streamlining of the notification process. The Competition Commission, which already has the administrative infrastructure in place, can act as a filtering mechanism which flags merger applications which potentially relate to a national security interest for the Committee to then deliberate on and undertake the decision-making process.

The Competition Commission will have a better understanding as to whether there are issues of national security and is therefore better positioned to notify the Committee of the intended merger. A foreign acquiring firm may, in good faith, be of the opinion that the intended merger does not fall within the list national security interests and fail to notify the Committee. The punitive consequences that attach to such failure would therefore be unfair in the circumstances. This may also serve as a disincentive for foreign acquiring firms to consider acquisitions in South Africa.

7. S 18A(15): President may delegate determination

We are very concerned about the inclusion of s 18A(15). Given that the Bill goes to great lengths to mandate the President, the highest officer of the country, to publish what South Africa's national security interests are, it does not make sense that such a duty should then be allowed to be delegated. Such a provision creates uncertainty as to how South Africa's national security interests are determined. This will not bode well for investor confidence. Additionally, this hampers South Africa's ability to create a uniform and coherent national security policy.

8. Balancing the interests of national security against the protection of an open investment policy

> *"Significant growth of the economy requires accelerated inbound and outbound trade (in particular higher-value products) as well as attracting significant volumes of foreign direct investment."* - South African Defence Review, 2015

The Bill should identify national security as an interest of the state, while it should also making explicit South Africa's receptiveness to foreign investment. We propose the inclusion of the italicised text below in the preamble of the Bill:

",including making provision for National Executive intervention in respect of mergers that affect the national security interests of the Republic, balanced against the promotion of an open investment policy."

We further recommend the following clause be inserted after s 18A(9):

"The Committee in considering a merger in terms of s 18A must take into account such factors which may adversely affect the general economic welfare of South Africa if the merger is not approved."

E - Conclusion

What this submission has sought to do is two things:

First, we have identified legislative deficiencies that we believe if remedied, strengthen the Bill by doing away with vagueness, over-broad definitions and factors, and the potential for ambiguity in interpreting certain clauses. Additionally, there is a need to clarify the roles of various actors subject to the Bill, such as the Competition Commission, Tribunal and Appeal Court as well as the Committee. Our recommendations as to operations and mechanisms seek to optimise the internal working relationship between these bodies, as well as with merging parties.

Secondly, we have taken cognisance of the need to balance national security interests of South Africa with encouraging an economic environment that is open and receptive to foreign investment. We believe that the recommendations we suggest allow for these priorities to be considered in a way that benefits South Africa and all its people. As a developing economy, stunted by low growth and high unemployment, it is imperative that investor confidence is maintained through certainty and stability. The composition of this Committee is of paramount importance in instilling confidence in its ability to appropriately consider applications that come before it, striking the right balance between national security and economic development.

We urge the Select Committee to carefully consider the impact of s 18A on the independence, efficacy and functioning of the Competition Commission. The inclusion of this provision, in our view, will invite a slew of legal challenges occasioned by the lack of clarity, certainty and fairness in the drafting of these amendments. Our proposals for review and interaction will improve the rationality of the Committee's decisions.

This submission was prepared by Kimera Chetty, Mira Menell Briel, Charles Simkins, Anton van Dalsen and Francis Antonie

---