

Structure BEE deals with competition in mind

WHEN structuring corporate transactions, timely competition law advice can ensure clarity in regard to when parties' joint conduct can create additional obligations, and clarify possible exit strategies upfront.

Black economic empowerment (BEE) deals have largely been regarded as pro-competitive as they diversify ownership and may have positive public interest aspects. But what of the BEE shareholders who now wish to exit these structures?

The recent decision by the Competition Commission to recommend that the proposed acquisition by Network Healthcare Holdings (Netcare) of the Community Hospital Group, a black-owned firm, be prohibited, has highlighted a number of issues that are relevant to the initial structuring and the exit strategies available to investors in empowerment transactions, including an amplification of the meaning of control, as defined in the Competition Act.

The commission scrutinised the arrangements at three levels. Firstly, Netcare helped the founders of Community Hospital Group acquire five hospitals. Netcare acquired a 46,3% stake in the group after which, in 2003, it jointly negotiated tariffs



for itself and Community Hospital Group en-block. Then, in 2005 Pro Sano laid a complaint of alleged price-fixing against Netcare and Community Hospital Group as a result of such joint tariff negotiation. And finally, Community Hospital Group's black empowerment shareholders, sought to exit the company by selling their shares to Netcare.

A merger takes place when one or more companies, directly or indirectly, acquire or establish control over the whole, or part, of the business of another organisation.

Sections 12(2)(a)-(f) of the act set out the typical "bright lines of con-

trol", such as when a person beneficially owns more than half of the issued share capital, or is entitled to vote a majority of the votes at a general meeting, or is able to appoint or veto the appointment of a majority of directors of the company (with similar provisions in respect of trusts and close corporations).

Section 12(2)(g) is broader in scope and describes situations of de facto control. It provides that "a person controls a firm if it has the ability to materially influence the policy of the firm in a manner comparable to a person who, in the ordinary commercial practice, can exercise an element of control referred to in paragraphs (a) to (f)".

This is a catch-all that affects a number of arrangements entered into by firms, which parties are not always aware would trigger merger notification. Such de facto control typically exists where a minority shareholder retains the right to approve or veto strategic commercial decisions or is able to exert decisive influence over that entity. Decisive influence sufficient to constitute control in terms of the act typically includes the right to approve or veto budgets or business plans, appoint-

ing senior staff, business and/or commercial policy, substantial investments, the firm's competitive strategy or corporate planning.

During the commission's investigation, it found that Netcare had acquired decisive influence over Community Hospital Group in 2003, sufficient to constitute control as set out in section 12(2)(g) of the act.

Alternatively, if Netcare did not acquire control the parties may have engaged in collusive conduct, prohibited under the act, by virtue of the joint negotiation of tariffs. The commission found that the manner in which Netcare negotiated tariffs on behalf of itself and Community Hospital Group indicated that it had acquired such decisive control.

The parties agreed to pay a R6m administrative penalty, acknowledging that they should have notified the acquisition of joint control of Community Hospital Group by Netcare. The exit transaction, which constituted a change from joint control to sole control, was notified to the commission as required under the act. The commission determined that this transaction would substantially prevent or lessen com-

petition in the private hospital markets, which are already considered to be too concentrated, and where Netcare held substantial market share. It recommended to the tribunal that the merger be prohibited, effectively leaving Community Hospital Groups' black empowerment shareholders without an exit route.

The commission's assessment has highlighted two aspects that must be borne in mind when structuring transactions. In the first instance, where shareholders who are also competitors intend to engage in co-ordinated business practices, the intention to engage in such practices may be sufficient to constitute joint control and require merger notification to the Competition Commission. In the second instance, when black empowerment parties enter into equity funding arrangements with competitors, exit strategies available to the empowerment parties, and typical clauses that limit transfer of shares, may not be viable where the competitor already holds a significant share in the market.

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