

Issue 3
***The application of merger provisions of the Competition Act 89 of 1998,
as amended, to joint ventures***

Preface

1. The Competition Commission ("the Commission") prepares and disseminates Updates to inform and clarify the Commission's policies and adopted approaches to specific issues on any matter within its jurisdiction. These Updates are not binding on the Commission, the Competition Tribunalⁱ or the Competition Appeal Courtⁱⁱ in the exercise of their respective discretions, or their interpretations of the Competition Act.
2. While this Update is not binding on the Commission, it sets out the approach the Commission is likely to adopt in respect of certain transactions and may be updated from time to time to account for future developments.

1. Introduction

1. Since the Competition Act 89 of 1998ⁱⁱⁱ ("the Act"), came into operation on 1st September 1999, practitioners and company advisors have raised questions about the extent of the application of merger provisions contained in Chapter 3 of the Act to joint ventures.
2. Some have argued that since the definition of a merger in the Act does not expressly mention joint ventures, it would not be appropriate or fair to business to interpret the definition to include transactions that, in their view, the legislature did not intend to include in the Act.
3. Therefore, this document is an attempt to clarify how joint ventures fall within the ambit of Chapter 3 in order to assist business to comply with the requirements of the merger provisions of this Act. For more clarity, decided cases and approaches adopted in other international jurisdictions have been considered.

2. What does Chapter 3 of the Act entail

1. Firstly, it must be understood that section 3 of the Act provides that the Act applies to all economic activity within, or having an effect within, the Republic. Only those instances provided for in sections 3(1) (a)-(e) are excluded from the application of the Act. It is therefore clear from this provision that the Act is not only concerned with the geographic location of the activity in question, but is concerned with the effect of that activity within the Republic. The effect of such activities in the Republic may be determined, *inter alia*, through the firm's sales in or into the Republic, whether through distributors, subsidiaries or direct sales.
2. In light of this section, all joint ventures, in whatever form, which take place in the Republic, or outside the Republic with an effect in the Republic, clearly fall within the ambit of the Act. The question would therefore be whether such joint ventures constitute mergers in a manner contemplated in the Act.
3. Chapter 3 of the Act deals with mergers and the term "merger" is used to include amalgamations, takeovers and acquisitions. This chapter requires that all transactions entered into by firms, which falls within the definition of a merger and meet the thresholds determined in Notice 254 of 2001^{iv}, be notified to the Commission before they are implemented.
4. A merger is defined in section 12 as occurring when *one 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 firm is defined in section 1(ix) for the purpose of the Act to include a person, partnership or a trust. The words "*one or more*" firms in the definition clearly indicate that a merger may involve the acquisition of either *sole* or *joint control*. A merger contemplated in section 12 may be achieved in any manner including the following:

(a) purchase or lease of the shares, an interest or assets of the other firm in question; or

(b) amalgamation or other combination with the other firm in question^v.

5. Therefore, the manner in which a merger may occur is not limited to the instances mentioned above. Any acquisition of control by a firm through any means, not necessarily included in the definition, may constitute a merger. Although the definition of a merger does not specifically mention the types of transactions that are covered by the definition, it is clear that all transactions that result in the acquisition of control would constitute mergers.
6. In the application of the law, a generally applicable rule is that words, phrases and sentences of a statute are to be understood in their natural, ordinary or popular and grammatical meaning, unless such construction leads to an absurdity or the context or object of the statute suggest a different meaning^{vi}. It follows from this rule, therefore, that if the words of a statute are clear and unambiguous, then effect should be given to their ordinary, literal and grammatical meaning.
7. Therefore, the argument that the definition of a merger does not expressly mention joint ventures is not relevant as no other type of transaction is mentioned either. Therefore, the definition appears to be broad and abundantly clear and unambiguous.
8. In the premise, it is evident that for a merger to occur, there must be a change of control in the *firm* that is being acquired. Section 12(2) of the Act goes on to enumerate various formats that control may take^{vii}. It has been accepted that these enumerated forms of control do not attempt to exhaustively define the parameters of control that may be relevant for purposes of the application of Chapter 3 of the Act.
9. In **Bulmer SA & Seagram Africa (Pty) Ltd v. Distillers Corporations & others**, the Competition Tribunal ("the Tribunal")^{viii} held that acquisition of control is "event-based". Therefore for the purpose of section 12 the language of 12(1) must be interpreted and the instances of 12(2) must be seen as ancillary to but not determinative of that enquiry. This therefore outlines the broad nature of the application of the definition of the merger.
10. The reference to instances of control listed in section 12(2), though not necessarily determinative of how control must be conceived, indicates that mere cooperation between firms or parts thereof, does not suffice as acquisition of control. Though these comments

were made in relation to the notion of the application of the concept or the principle of “single economic entity”, the outline is helpful in understanding the broad nature of the definition.

11. A further point to note is that section 12 does not distinguish between permanent and short-term acquisition of control. Therefore, the duration of the joint venture does not appear to be relevant for the purpose of determining notifiability. Furthermore, control is based on the possibility of exercising decisive influence over a firm or business, which is determined by both legal and factual consideration.
12. For the purpose of notification, Chapter 3 categorizes mergers into small, intermediate and large on the basis of thresholds. A small merger need not be notified to the Commission. The Commission may require that such a merger be notified if it raises competition or public interest concerns. Both intermediate and large mergers must be notified to the Commission, but the Tribunal makes a decision with respect to large mergers after the Commission has made its recommendations.

3. How merger provisions apply to joint ventures

1. For purposes of determining the extent of application of the merger control provisions to joint ventures, it is important to consider the form that joint ventures may take. Various definitions, some elaborate and some restrictive, have been attached to the concept of a joint venture and the term is applied to a wide range of situations.
2. A joint venture is generally defined as a business arrangement in which two or more parties undertake a specific economic activity together. The joint undertaking can be achieved on a formal or informal basis. Engaging in or establishing a joint undertaking may enhance efficiencies and allow for economies of scale to be obtained and allow firms to enter markets, which are otherwise difficult to enter. Some firms use the ventures to turn under-utilised resources into profit or to create a new profit center. A joint venture is therefore usually created to perform a project that is beyond the capacity of a single entity.

3. The words joint venture and partnership are sometimes used interchangeably. A joint venture is similar to a partnership in that it must be created by an agreement between the parties to share in the losses and profits of the venture. It is different from a partnership in that the venture is normally for one specific project rather than a continuing relationship.
4. Under the European competition law, a joint venture has been defined as an undertaking which is jointly controlled by two or more other undertakings^{ix}. A distinction has been drawn between “concentrative” joint ventures and “cooperative” joint ventures. Concentrative joint ventures are described as those that bring about a lasting change in the structure of the undertakings concerned, while cooperative joint ventures are conceived for specific purpose, for instance, research and development, marketing, distribution, networking, and production.
5. In ***Inter-City Tire and Auto Center, Inc. v. Uniroyal, Inc^x***, the following were outlined as the basic element of a joint venture under the New Jersey or New York law:
 - (a) an agreement between the parties manifesting some intent to be associated as joint ventures;
 - (b) each party contribute money, property, effort, knowledge or some other asset to a common undertaking;
 - (c) a joint property interest in the subject matter of the joint venture;
 - (d) a right of mutual control or management of the enterprise; and
 - (e) an agreement to share in the profits or losses of the venture.
6. In ***Compact et al v. Metropolitan Govt. of Nashville & Davidson, TN^{xi}, Wiseman***, the **Chief Judge** held that banding together by parties, however benevolent the reason may be, does not make mere legal characterization of the transaction or conduct by the parties to it, a joint venture. Therefore, collusive mutual concessions by competitors are not necessarily joint ventures.
7. The ***Compact*** case contemplated that a joint venture is a transaction where parent firms each, have a 50% interest or substantial responsibility and decision-making authority. Furthermore, a joint venture was defined as a separate enterprise characterized by an

integration of operations between and subject to control by its parent firms which results in creation of significant new enterprise capability in terms of new productive capacity, new technology, a new product, or entry into a new market.

8. There is a view that sees a joint venture as any collaborative agreement between the actual or potential competitors, which falls between a cartel and a merger. There is, however, an appreciation of the fact that joint ventures may be between parties other than competitors. The specific reference to collaborative agreements between “actual or potential competitors” appears to be the only way in which the definition above sought to distinguish joint venture agreements from agreements such as concerted practices or collusions. A joint venture is further seen as an agreement that neither constitutes a merger in the strict sense of the word, nor conduct that falls squarely within the ambit of the restrictive practices.
9. The view that appears to be predominant limits the notion of a joint venture to agreements that create a new and separate business entity under the *joint control of independent* parent firms. The Chairman of the Federal Trade Commission, Robert Pitofsky, indicated during the hearing on the joint venture project in 1997 that joint ventures and other competitor collaborations are increasing in number, taking on new forms and often growing more complex. The growing complexity of these arrangements makes it difficult to formulate a blanket approach to them.
10. In light of the above definitions, a joint venture appears to be a separate business enterprise over which two or more independent parties exercise joint control, and is created for a specific purpose. Furthermore, joint ventures may be distinguished into various types according to their purposes, which include research & development, production, distribution, purchasing, advertising and promotion, and networking.
11. The distinction between mergers and other forms of corporate cooperation is often difficult to draw, making it difficult to determine if joint ventures result in a merger or a restrictive practice. As a way of establishing the distinction between restrictive practices and mergers, it has been reasoned that restrictive practices influence competitive conduct of firms by lessening or eliminating competition, but firms remain independent. Mergers on the other

hand bring about a lasting change in the structure of the merging firms resulting in merging firms giving up their economic independence.^{xii}.

12. In determining the applicability of merger provisions to joint ventures, it is also important to note that the analysis of whether or not a transaction is notifiable does not take into account whether or not the transaction is pro-competitive. The examination of competitive effects of a transaction is relevant in determining whether the transaction ought to be approved or rejected and not to whether a transaction is a merger or not.
13. As joint ventures take various forms, which may result in a merger or anticompetitive conduct by the parties involved, the merger control provisions should be understood to be applicable to joint venture transactions in the South African law. However, not all joint venture transactions will constitute a merger, as this will depend on how they are structured.
14. A joint venture that neither results in a change of control nor anticompetitive conduct, would not necessarily invoke the provisions of the Act. Since Chapter 3 is concerned with the change of control, only those joint ventures that result in a change of control and meet the threshold would be notifiable. However, those that do not result in a change of control *may be examinable under chapter 2 of the Act to determine any anticompetitive effects*.
15. To illustrate the notifiability of certain joint ventures, the following forms of joint venture transactions are examined to give some clarity:

(a) Where two or more firms jointly form a new entity for a specific purpose

In this case, parties would create a separate entity in which they jointly exercise control while remaining independent. The creation of such an entity on its own would not amount to a merger, as none of the parties would be acquiring any control over each other's business. There would be no change of control over any of the firms or businesses, as the creation of the venture would not affect their independence with respect to the control structure.

However, the situation would be different if the parties to the joint venture transfer assets or interests into the newly created entity. An example is where two independent companies,

Company A and Company B, who are competitors in manufacturing and distribution of certain products, decide to create a joint venture company, and transfer their respective distribution businesses into the said venture. In that case the assets that are transferred by the creating companies will constitute an acquisition by the joint venture, which is a separate entity, of control over the business, or a part thereof, of the creating companies.

In some instances, a special purpose vehicle company ("SPV") is created, which then acquires certain divisions or businesses of the said creating companies. The creating companies therefore cease to operate their independent businesses in respect of the transferred divisions and operate them through the newly created entity. This technically and factually results in the creating companies merging their divisions or businesses into one operation.

On the basis of the transfer of interests, assets or business into the venture, the transaction in question would clearly constitute a merger contemplated in section 12 of the Act. The joint venture company will be regarded as the acquiring firm while the specific assets or businesses being acquired would be the target firms.

(b) Where two or more firms acquire joint control over an existing firm or business thereof

Two or more companies may acquire joint control over an existing entity or any part of the business thereof in which none of them had control prior to the said transaction. Through the acquisition, the creating parties will control the business for the purpose of which the joint venture is proposed. This would constitute a merger as defined in the Act since control of the acquired entity will change.

In certain instances, the transaction may involve the issue of shares by the acquiring companies in consideration for the acquisition. Therefore, depending on the amount of shares issued, the share issue may result in a further notifiable merger. That may be the case if, for instance, the acquiring companies issue shares that confer control over their businesses or a part thereof to the seller.

An example of this is where Company A and Company B jointly acquire control over Company C in order to use it as a vehicle for a joint venture through a sale agreement. Instead of cash, the two companies each issue 50% shares to Company C in their respective businesses. Therefore, the shares issued may result in Company C acquiring control over the businesses of Company A and B respectively. This subsequent issue of shares by Company A and B may therefore constitute notifiable mergers if they meet the threshold. Therefore, one transaction may result in multiple mergers that may require notification.

In as far as two or more firms acquire control over a firm, the acquisition by each firm may constitute an independent and separate notifiable transaction. The Commission may, after analyzing a said transaction, prohibit one and approve the other. The fact that the transactions occur simultaneously and are contained in one agreement is not sufficient motivation for the transactions to be notified as one. The purpose of merger regulation is to ensure that each transaction is analyzed and evaluated for competition effects and its impact on the public interests.

However, where transactions are interdependent and indivisible, the Commission may decide to consider them as one transaction for the purpose of analysis. This is however the discretion of the Commission and such decision may be reversed if the Commission deems it appropriate to do so.

4. Approaches in other jurisdictions

1. Some jurisdictions distinguish or seek to distinguish joint ventures from mergers and in the process attempt to exempt joint ventures from merger control provisions.
2. In the US, there is an attempt to distinguish between strategic alliances and mergers. In the US they distinguish between competitive collaborations and mergers by their respective competitive effects and their duration. It is said that mergers by design end competition between the merging parties and are permanent, while competitor collaborations on the other hand do not end competition between the collaborating parties and are also of a limited duration.

3. On the other hand some jurisdictions do attempt to maintain a distinction between joint ventures and some other forms of collaboration strategic alliances. Canada is one other jurisdiction that attempts to maintain such distinction. The Canadian definition of a merger, like South Africa, is understood to be broad enough to encompass joint ventures. However unincorporated joint ventures, which are set for a specific project that is not likely realisable without the joint venture, are exempt from the Act^{xiii}. It would seem that the EC competition law takes a similar approach.
4. The European Union Article 3 of Council Regulation (EEC) No. 4064/89, as amended by Regulation (EC) 1310/97, is understood to include joint ventures performing, on a lasting basis, all the functions of an autonomous economic entity. Such a joint venture brings about the lasting change in the creating companies and is referred to as a "full function" joint venture while a "partial function" joint venture assumes limited functions within the parent companies' business activities, such as research and development, production and distribution joint ventures established for a short duration. There is a general prevailing trend to see a joint venture as full function and therefore subject to merger regulation, unless there is sufficient indication that the joint venture is partial function^{xiv}.
5. While pre-merger notifications are not a requirement in Australia, a number of joint ventures have been reviewed under merger regulations. Reference is made to the decision taken by the Australian Competition and Consumer Commission (ACCC) not to oppose a satellite infrastructure joint venture between ***Australis Media Limited (AML) and Optus Vision***^{xv}. The ACCC distinguished this case from a merger that was proposed between ***Australis and Foxtel***, which the ACCC rejected. Among the aspects that were said to be distinguishable were the following:
 - (a) the joint venture is an infrastructure sharing arrangement only;
 - (b) the joint venture does not lead to the disappearance of one of the three metropolitan pay TV operations;
 - (c) the joint venture has little or no impact on telephony;
6. Refining joint ventures between *Mobil Oil Australia Limited* and *Shell Australia Limited* and *BP* and *Caltex* were submitted to the ACCC in August and December 1998, respectively.

Therefore, it can be safely concluded that joint ventures are also subject to merger regulations in Australia.

7. It appears therefore from the above that while not all joint ventures fall under the definition of a merger, the authorities are concerned with those that result in a change of control or anticompetitive effects. Therefore, a joint venture in its basic form, i.e. which neither results in a merger nor collusion, appears to be exempt from merger regulations.

5. The Determination of threshold in joint venture transactions

1. Depending on how the transaction is structured, a joint venture entity can either be a target or an acquirer. For purposes of determining threshold, the term "target firm" has been changed to "transferred firm", which is defined in item 7 of Notice 930 of 2001 as:
 - (a) a firm, or a business or assets of a firm, that as a result of a transaction in any circumstance set out in section 12 of the Act, would become directly or indirectly controlled by an acquiring firm; and
 - (b) any other firm, or business or assets of a firm the whole or part of whose business is directly or indirectly controlled by a firm contemplated in (a).
2. Where a division, assets or a part of a business of a firm is acquired, actual assets, business or division that is acquired and not the whole business or firm will be considered for threshold calculation. Therefore, assets, units or divisions, whether legally incorporated or not, may be considered as the transferred firm.
3. Where a subsidiary of a particular company is being acquired, the subsidiary and all firms controlled by it will be the transferred firm. However, where the part(s) sold constitute the entire business of the selling firm, the whole firm and its subsidiaries, if any, will be considered as the transferred firm. The acquiring firm on the other hand includes the actual acquirer, its subsidiaries and its parent firms.
4. For the purpose of determining the threshold, where the joint venture entity is the acquiring firm, the calculation of the turnover and asset value(s) will include those of the parent

firm(s) whose business is being acquired by the joint venture entity, including those of the joint venture entity as the acquiring firms. This calculation will, however, exclude the turnover or asset values of the divisions, units or part of the business that is being acquired by the joint venture, as those will be included on the side of the target firm. This would ensure that values are not duplicated in the calculation.

5. Where the joint venture entity is a target in the manner contemplated in the Act, the calculation of annual turnover or asset values will be in terms of the normal procedure. This means that the arrangement may be such that the whole joint venture entity or a certain part of its business is targeted. The way in which the disposition of the joint venture entity or its business is structured will give the necessary indication as to whether the whole entity or part of its business is the target.
6. In most instances, an existing company that is acquired by the parties as a joint venture vehicle may be a dormant company with no assets or turnover. In such cases, the asset value and turnover of the company may be recorded as nil. Such a transaction would constitute a merger, but may not be notifiable to the Commission for approval as it falls below the required threshold.

6. Conclusion

1. It must be appreciated that the application of merger control provisions to joint venture transactions is not a straightforward matter. Furthermore, the growing complexity of these transactions makes it difficult for the competition authority to exempt them from the application of the Act.
2. While joint ventures are seen as enhancing efficiencies, depending on how they are structured, they may create a fertile ground for collusion between competitors and eliminate or lessen competition in the market. A joint venture that results in a merger may not only result in lessening or elimination of competition but more importantly, may result in elimination of an effective competitor and therefore reduction in the number of market players.
3. It is generally recognized that it may be necessary and beneficial for companies or corporate institutions, to enter into strategic alliances or form strategic co-operatives or joint ventures. However, it is important for the competition authorities to ensure that parties do not, in the way they structure such alliances, evade the provisions of the Act. *Therefore, Chapter 3 of the Act will apply to all those joint ventures or alliances that fall within the definition of a merger.*
4. As indicated above, while this paper attempts to clarify the approach of the Commission to joint ventures, it does not constitute a binding legal document. Parties may approach the Commission with regard to specific enquiries where they require further certainty as to whether a particular joint venture constitutes a merger contemplated in Chapter 3.

REFERENCES AND SUGGESTED FURTHER READINGS:

WEB SITES

1. <http://www.accc.gov.au/media/mr1996/media500.htm>.
2. <http://home.earthlink.net/~fpearce/Jointventure.html>
3. <http://www.ftc.gov/opp/jointvent/kolasky.htm>
4. <http://www.antitrust.org/law/EU/intlLaw.html>

BOOKS

1. Lennart Ritter et al (2000) European Competition Law: A practitioner's guide. 2nd edition. Kluwer Law International: The Hague - London - Boston
2. Frank L. Fine (1996) Mergers and joint ventures in Europe: The law and policy of the EEC, 2nd edition. Kluwer Law International

ARTICLES / PUBLICATIONS

1. William J. Kolasky, Jr. (1997) Antitrust enforcement guidelines for strategic alliances. Presented at the Federal Trade Commission's Hearing on Joint Ventures. July, 1997
2. Merger Control Law in the European Union: Commission Notice on the concept of full function joint ventures under Council Regulation (EEC) no 4064/89 on the control of concentrations between undertakings (98/c 66/01)
3. Competition Commission: South Africa, Annual Report (2000)

CASES

1. Compact, et al., v. The Metropolitan Government of Nashville & Davidson County, TN., et al No. 3-84-0853, United District Court, M.D. Tennessee, 1984
2. Intercity Tire and Auto Center, Inc., v. UniRoyal Inc., Civ. A. No. 85 –1797 United States District Court, New Jersey, 1988
3. Siegel Tire & Battery Corp. and Richard L. Siegel v. Morris Erbesch, Tina Erbesch & S Realty corp., Civ. A. no. 85 –1797 United District Court, New Jersey, 1988
4. W. Thomas McElhinney, M.D., v. The Medical Protective Company, et al. Civ. A. No. 78-8, US District Court, E.D. Kentucky, Pikeville division, 1982
5. Bulmer SA (Pty) & Seagram Africa (Pty) Ltd and Distillers Corporation (SA) Ltd & Stellenbosch Farmers Winery Group: Case No. 94/FN/Nov00, 101/FN/Dec00

ⁱ Established in terms of section 26 of the Competition Act 89 of 1998, as amended.

ⁱⁱ Established in terms of section 36 of the Competition Act 89 of 1998, as amended.

ⁱⁱⁱ As amended by the Competition Second Amendment Act 39 of 2000

^{iv} General Notice 254 of 2001: Determination of Threshold

^v See section 12(1) of the Competition Act 89 of 1998.

^{vi} Observations of Innes CJ in *Venter v R* 1907 TS 910 to 913)

^{vii} Section 12(2) (a)-(g) provides formats control may take, which includes the ownership of more than one half of the issued share capital, being entitled to vote a majority of the votes that may be cast at a general meeting of the firm, and the appointment of the majority of directors on the board.

^{viii} Case Nos: 94/FN/Nov00, 101/FN/Dec00

^{ix} See Commission Notice (98/C 66/01) p.101 para. 3 of the Introduction.

^x 701 F. Supp. 1120, 1989-2 Trade Cases P 68, 839

^{xi} 594 F. Supp. 1576, 53 USLW 2221, 1984-2 Trade Cases P 66, 289

^{xii} Lennart Ritter et al (2000) pp. 408

^{xiii} http://www.maccarthy.ca/pub_docs/cach3.htm "How does the Competition Act affect relationships with competitors" pp.5 and 11

^{xiv} Lennart Ritter et al (2000) pp. 408-426

^{xv} See <http://www.accc.gov.au/media/mr1996/media500.htm>, pp1-2, 2/12/01.