Digesting the Commission's decision on Burger King deal

By Robert Wilson and Shawn van der Meulen

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For the first time in 20 years, a merger may be prohibited on public interest grounds alone. A ground-breaking recommendation by the Competition Commission (Commission) to the Competition Tribunal (Tribunal) to prohibit the proposed sale by Grand Parade Investments Limited (GPI) of its investment in Burger King (South Africa) to a US private equity firm will have severe consequences for the future of M&A transactions and investment into South Africa. The case also raises questions about whether competition law is the right tool to advance the country's transformation agenda.

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On 1 June 2021, the Commission recommended that the transaction whereby ECP Africa, a private equity fund, proposed to acquire Burger King (South Africa) and Grand Foods Meat Plant (Pty) Ltd (Grand Foods) from GPI be prohibited. The Commission found that the merger would significantly reduce the shareholding of historically disadvantaged persons (HDP) in the target firm, from more than 68% to 0%.

Public interest factors

When the Commission assesses proposed mergers, besides considering the impact of the transaction on competition, it must also consider certain public interest factors. One of these factors is whether a merger "promotes a greater spread of ownership, in particular to increase the levels of ownership by historically disadvantaged persons in firms". In recent years, several mergers have been approved, subject to conditions aimed at increasing HDP ownership in firms. For example, the PepsiCo / Pioneer merger was the first significant transaction in which promoting a greater spread of ownership in firms was a central issue. After extensive engagement with the competition authorities, the merger parties agreed to implement a B-BBEE ownership plan resulting in 12,000 workers being granted a stake in the merged entity.

Merger parties have typically engaged with the competition authorities and agreed on conditions to address the Commission's ownership concerns. In this merger, the parties did propose conditions such as investing no less than R500 million towards establishing new Burger King stores in South Africa and increasing the number of permanent employees employed by it in South Africa by no fewer than 1250 HDPs.

Although these proposed conditions would lead to other positive public effects in South Africa, the Commission appears to have taken an uncompromising stance on HDP ownership reduction due to the merger. The head of the Commission's mergers and acquisitions division, Tamara Paremoer is reported to have said that, regardless of the assessment on competition, the Competition Act requires that the authority also determine whether or not a merger can be justified on public interest grounds and that the Commission is simply doing what the law requires it to do. The Competition Commissioner, Tembinkosi Bonakele, has said that the Commission had no choice but to block the takeover and that it had done its job of enforcing the provisions of the Competition Act. The Commissioner indicated that it is up to the merger parties to challenge the Commission's interpretation of the law.

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Final decision

Since the transaction is a large merger, the Tribunal is mandated to have the final say on the outcome of this matter. In the past, the Tribunal has indicated that considerable caution must be applied when the competition authorities use public interest as a basis for their intervention, particularly when competition is unimpaired and when HDP investors, whose interests are directly affected, reject the Commission's interventions.

In the Shell SA / TepCo Petroleum case, the Tribunal said that constraining the options of firms owned by HDPs in this way may condemn these firms and HDPs to the margins of the economy. By limiting exiting HDP shareholders to a smaller group of potential purchasers and potentially discounted prices, exiting HDP shareholders could become less competitive over time as they are not able to realise the maximum value of their investments within the best possible time and to reapply the proceeds of such realisation to other investment opportunities. The Tribunal also noted that the Commission's role is to promote and protect competition and specified public interests and not second-guess commercial decisions of HDP shareholders wishing to exit an investment.

Potential knock-on effect

However well-meaning the Commission's objectives, this decision may create uncertainty which could have a potential chilling effect on merger activity, including foreign direct investment, especially in transactions where B-BBEE shareholding is decreased for legitimate commercial considerations. The tangible results of the prohibition were seen when, the day after the prohibition announcement, Grand Parade Investments' shares crashed by 17% before closing 10% lower. If the Tribunal prohibits the merger, the Commission's approach will potentially make it difficult for exiting HDP shareholders to obtain real value for their interests. The Commission is also likely to be encouraged to require significant positive commitments from merging parties to improve HDP and worker ownership levels.

While the competition authorities' efforts are understandably in line with the objectives of the Competition Act, such as creating a more inclusive and transformed economy and deconcentrating markets, the unintended consequences may outweigh the positive benefits of adopting a hard-line approach to specific public interest considerations.

We hope that as this matter progresses, the Tribunal will provide guidance on how the competition authorities should pursue their public interest mandate. Merger parties need certainty on deal making, and the authorities should not harm the very interests they are required to protect and arguably promote. Indeed, a more nuanced approach to that adopted by the Commission is necessary to balance the interests of HDP shareholders wishing to realise a return on their investments whilst also promoting the broader transformation of the economy and other positive public interest benefits such as increased employment. Dealmakers currently involved in transactions should await the Tribunal's final verdict before making any rash strategic decisions.

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