

SOUTH AFRICA / JUDGMENT

WBHO Construction (Pty) Ltd v Fikile Construction (Pty) Ltd and Others (LM024Apr17) [2018] ZACT 80; [2018] 1 CPLR 350 (CT) (22 March 2018)

[2018] ZACT 80

COURT

Competition Tribunal

BEFORE

Yasmin Carrim, AW Wessels, Medi Mokuena

CASE / FILE NUMBER

LM024Apr17

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COMPETITION TRIBUNAL OF SOUTH AFRICA

Case No: LM024Apr17

In the matter between:

WBHO Construction (Pty) Ltd

Primary Acquiring Firm

and

Fikile Construction (Pty) Ltd

Edwin Construction (Pty) Ltd

Motheo Construction Group (Pty) Ltd

Primary Target Firms

Panel

: Yasmin Carrim (Presiding Member)

: AW Wessels (Tribunal Member)

: Medi Mokuena (Tribunal Member)

Heard on

: 14 February 2018

Last Submission Received : 19 February 2018

Order Issued on : 21 February 2018 Reasons Issued on : 22 March 2018

Reasons

for Decision

Approval

[1] On 21 February 2018, the Competition Tribunal ("Tribunal") conditionally approved the proposed transaction between WBHO

Construction (Pty) Ltd and Fikile Construction (Pty) Ltd, Edwin Construction (Pty) Ltd and Motheo Construction Group (Pty) Ltd.

[2] The reasons for approving the proposed transaction follow.

Parties to proposed transaction

Primary acquiring firm

[3] The primary acquiring firm is WBHO Construction (Pty) Ltd ("WBHO"), a company duly incorporated in accordance with the laws of the Republic of South Africa. WBHO is a wholly owned subsidiary of Wilson Bayly Holmes-Ovcon Limited ("WBHO Group"), which is a public company listed on the Johannesburg Stock Exchange. Its shares are widely held and it is not directly or indirectly controlled by any single entity.

[4] WBHO is a large construction company with a broad spectrum of expertise in respect of all sectors of the construction industry. WBHO controls a number of companies in South Africa and around Africa. WBHO mainly operates through the following divisions:

- a. Building and Construction - WBHO is involved in the building of inter alia office and commercial buildings, hospitals, shopping centers, residential developments and golf estates, hotels and resorts, casinos and stadiums.
- b. Roads and Earthworks - WBHO provides large-scale public and private projects across various infrastructural applications such as inter alia road construction and rehabilitation, bridges and structures, freeways and airports, harbours and railways.
- c. Civil Engineering - WBHO provides civil engineering services in a number of sectors including mining, energy, water, and effluent treatment and silos and towers.

Primary target firms

- [5] The primary target firms are Fikile Construction (Pty) Ltd ("Fikile"), Motheo Construction Group (Pty) Ltd ("Motheo"), and Edwin Construction (Pty) Ltd ("Edwin")- collectively referred to as the Emerging Contractors. The Emerging Contractors are all smaller construction companies that are more than 51% owned and controlled by historically disadvantaged persons ("HDPs").
- [6] Fikile is controlled by the RT Ndlovu Testamentary Trust, which holds the majority of Fikile's issued share capital. According to the B-BBEE certificate of Fikile, the entirety of Fikile's issued share capital is held by HDPs. Fikile does not directly or indirectly control any firm.
- [7] Fikile has its main focus in building works where it specialises in the building of multi- story residential and social housing as well as commercial property. Fikile also has a civil engineering division which it is in the process of upscaling.
- [8] Motheo is not controlled by any single firm. The majority of the directors of Motheo are HDPs and include black women. Motheo controls Motheo Infrastructure Contractor (Pty) Ltd.
- [9] Motheo offers a wide range of services in the construction industry including general building, with a focus on social housing. Motheo is also active in the civil engineering sector, focusing on road construction and rehabilitation, structural concrete construction, mining infrastructure, bulk earthworks, factory infrastructure and water treatment works. On a limited and selected basis, Motheo also provides certain Turnkey solutions such as overall project management and property development.
- [10] Edwin has three shareholders, the largest being WBHO with 49%. Until June 2017, Edwin was controlled by WBHO as to 57%. Edwin does not directly or indirectly control any firm.
- [11] Edwin is a multi-disciplinary construction company which provides a range of products and services in the construction industry. Edwin is a civil engineering contractor which supplies services and operations in the construction of roads and highways, bridges and interchanges, as well as dams and earthworks sectors.

Proposed transaction and rationale

- [12] The proposed transaction entails the formation of economic alliances between WBHO and the respective Emerging Contractors.
- [13] The merging parties submitted that it was intended that post-merger, the merging parties will operate as a single economic entity (i.e. the WBHO Alliance).
- [14] These alliances are the result of a settlement agreement concluded between a number of Construction Companies[1] and the Government of the Republic of South Africa (as represented by the Ministers of Rural Development and Land Reform, Economic Development, Public Works and Transport) on 11 October 2016 ("the Settlement Agreement").

- [15] WBHO submitted that in order to achieve the objects of the Settlement Agreement, it was essential for them and their respective Emerging Contractors to establish an alliance pursuant to which WBHO will acquire material influence over the direction, operation and competitiveness of the business of the Emerging Contractor. The WBHO Alliance, therefore gives rise to a merger in terms of section 12(2)(g) of the Competition Act, no. 89 of 1998 ("the Act").
- [16] The mentoring and development that WBHO has chosen to embark on, requires that the Emerging Contractors identified should acquire the necessary skill, quality and status as well as the quantity of work to generate and sustain a cumulative combined annual turnover equal to at least 25% of the annual construction works turnover of WBHO during the relevant period (7 years extendable to 10 years).
- [17] It is worth noting that if WBHO does not meet that turnover obligation within the relevant period, WBHO would incur substantial penalties in addition to the possibility of the Government instituting civil proceedings against WBHO for previously having colluded on certain Government projects. If WBHO fails to pay the penalty, it may even be blacklisted and disqualified from being awarded contracts from public enterprises for up to 12 months.
- [18] The Settlement Agreement prescribes that the development of the Emerging Contractors will be undertaken in terms of a formalized development and mentorship program proposed by WBHO in consultation with the Black Business Council.
- [19] As per the Settlement Agreement, the proposed transaction is due to terminate after a maximum period of 10 years from the date of its implementation. Following the termination, the alliance members are expected to return to their original positions where they will no longer operate as a single economic entity; they will be expected to be completely independent and vigorously compete with each other. The Commission acknowledged that the parties may by mutual agreement, choose to terminate the alliance prior to the lapse of the 10 year period.
- [20] The Commission noted that WBHO currently holds 49% in Edwin and has the ability to appoint 40% of the board of directors of Edwin. The Commission was concerned with the fact that one of the directors appointed to the board of Edwin by WBHO, also holds an executive position as the Managing Director of WBHO's Road and Earthworks division. The Commission was of the view that this may dilute the public interest benefits linked to ensuring that the Emerging Contractors are empowered to compete against the construction company, by creating dependency on WBHO's managerial influence.
- [21] However, the Commission accepted that the appointments preceded the Settlement Agreement as WBHO has historically had shareholding in Edwin. Further, the Commission noted that WBHO has elected to work with three Emerging Contractors, which will serve to ensure that the public interest benefit linked to the mentorship are at the very least achieved through the other Emerging Contractors in which WBHO will not have a shareholding.

- [22] The primary acquiring firm's rationale for the transaction was that pursuant to the Settlement Agreement, WBHO had undertaken to the Government that it would increase investment, promote innovation and create entrepreneurial opportunities in the construction industry, particularly for small to medium sized enterprises. In terms of those commitments, WBHO was required to identify enterprises which it would mentor and develop and obtain such competition authority approval as is required to pursue those initiatives. The Emerging Contractors are the HOP firms identified by WBHO for this purpose.
- [23] The primary target firm's rationale was that the program will (i) provide them with extensive support and access to skills and expertise to enable them to take on more projects of a large scale; and (ii) allow them to over time acquire a greater share of the construction industry and compete more effectively.

Impact on competition

- [24] The Commission identified horizontal overlaps in the following markets:
- The provision of services for civil engineering: road;
 - The provision of services for civil engineering: other;
 - The provision of services for general building: residential; and
 - The provision of services for general building: non-residential.
- [25] The Commission found that the proposed transaction will result in a post-merger market shares of less than 15% with minimal accretions in all markets (less than 5%). The Commission also identified a number of prominent rivals in the relevant markets such as Aveng, Group Five and Murray & Roberts among many other construction companies. The Commission concludes that the merged entity is unlikely to exercise market power given the presence of several viable alternatives who will be able to discipline the merged entity.
- [26] Further, the Commission identified a vertical overlap, in that WBHO manufactures/produces some upstream products used by the Emerging Contractors.[2]
- [27] The Commission found that the proposed transaction is unlikely to result in any input or customer foreclosure as the Emerging Contractors, individually and collectively, are not significant buyers of the upstream products produced by WBHO. With combined market shares in the downstream markets of less than 5%, the Emerging Contractors do not account for a sufficient portion of market demand so as to give rise to a possibility of substantial foreclosure.
- [28] Further, the Emerging Contractors' total procurement of the respective upstream products equated to less than 10% of WBHO's total sales of said products. Additionally, WBHO is just one in many manufacturers of these products. Therefore the Commission found there is no likelihood of foreclosure as a result of the proposed transaction.

Public interest

Employment and public interest benefits

[29] The merging parties submitted that there will be no adverse effect on employment, as no duplications arise as result of the mergers. Rather the Construction Companies will ensure that the transactions provide the Emerging Contractors with the support, skills and guidance to grow into successful independent firms in the market. As a result employees will need to be sourced and the target firms will create quality jobs and entrepreneurial opportunities in the industry. The Commission found there to be no likelihood of duplications or rationalisations as a result of the proposed transactions.

[30] The merging parties submitted that in line with section 12A(3)(c) the proposed transactions result in public interest benefits as it enables the Emerging Contractors (BEE and Historically Disadvantaged firms) to become competitive. The merging parties outline the following benefits:

- a. It will improve the development of skills among HDPs in critical areas in the industry;
- b. It encourages participation and ownership of SMEs and enterprises managed and owned by HDPs; and
- c. It provides for demonstrable and measurable expansion opportunities in the construction industry which promotes competition, innovation and growth in the market.

[31] The Commission agreed with this and found that the proposed transaction raises strong public interest benefits in terms of the Act. The proposed transaction ensures that small black-owned construction companies are able to grow their businesses to hopefully one day be able to compete directly with firms such as WBHO. Regarding the current level of transformation in the construction industry, the Commission found that most black-owned construction companies operate in the lower levels of the market (smaller projects). The WBHO alliance therefore presents an opportunity for the black-owned businesses to be developed into large and more competitive firms in line with the objectives of section 12A(3)(c) of the Act.

[32] The Commission was of the view that it is necessary to monitor the performance of the alliances in their attainment of these public

interest benefits. The Commission therefore required the merging parties to provide a report to the Commission on all the projects the merging parties would have participated in as part of the WBHO Alliance.

[33] The Commission was also concerned about the possibility of unfair treatment of the Emerging Contractors within the WBHO Alliance, given the disparity in size of the Emerging Contractors. The Commission was concerned that since the Settlement Agreement was silent on the apportionment of the 25% target and does not specify how the work is to be allocated, there may be a risk that WBHO may focus all its resources and training on one of

the Emerging Contractors and achieving the target through that one Emerging Contractor while the other receives no assistance and sees no growth.

- [34] The Commission engaged the Emerging Contractors regarding this concern, who indicated that the value of the alliance is in the skills and development that is on offer, the Emerging Contractors plan to exploit the opportunity and learn from WBHO to the fullest.
- [35] Further, the Emerging Contractors provided that they are largely specialized in different areas of the construction sectors, which suggests that there will not be reason to trade-off working with one Emerging Contractor for another. The Commission concludes that there is more incentive for WBHO to work with both Emerging Contractors in a fair and equal manner as opposed to the converse.
- [36] The Tribunal addressed this concern by suggesting that the Commission's condition relating to this issue be reworded to say that the Emerging Contractors are to be treated equally, in order to prevent any bias to one or the other in the allocation of work.[3] The merging parties and the Commission had no objection to this amendment.

The Fund

- [37] The Settlement Agreement made provision for the establishment of a Fund, the objective of which will be the development and enhancement of the Construction Industry and in particular, transformation objectives.
- [38] The Trustees of the Fund will comprise of representatives of all of the Construction Companies who are party to the Settlement Agreement, as well as representatives of the Government, as appointed by the relevant government departments.
- [39] The Commission was of the view that further measures were required to ensure that the Fund is not used as an information sharing platform by the construction companies.
- [40] The Commission was of the view that all the economic alliances should put into place the necessary safeguards to ensure that competitively

sensitive information does not flow from one economic alliance to other construction companies through the Fund.

- [41] In respect of the Fund, the Commission required that the alliance members ensure that all information submitted to the Fund is aggregated, and the members must ensure that the necessary measures are put in place to prevent the flow of competitively sensitive information from one alliance to another through the Fund or any other medium.
- [42] The Commission further required that the people selected by the Construction Companies for the mentorship and development of the Emerging Contractors should not be appointed as Trustees to represent them on the Fund.

[43] The merging parties submitted that such a condition would be restrictive and prejudicial to the alliances as it:

- a. Precluded all key executives and personnel of WBHO from being trustees on the Fund. The merging parties submitted that although only one person may primarily be appointed with overall responsibility for the day to day and ongoing mentoring and development of the Emerging Contractors, various secondees will be involved in operational and other development and mentoring activities and WBHO executives are likely to participate in, and have oversight over the development and mentoring activities; and
- b. This precluded persons from being trustees of the Fund who, through their general enterprise development activities and their activities and their involvement with the Emerging Contractors, have the best knowledge and expertise of what development, transformation and other initiatives are required by the industry, being the principal objective of the Fund. The merging parties submitted that the restriction is therefore detrimental both to the objective so the Fund and to the Alliance Construction Company's interests at the Fund.

[44] The Commission remained of the view that having the same people responsible for the monitoring and development, while sitting as

Trustees increases the likelihood of coordination between the construction companies.

[45] The merging parties re-iterated before the Tribunal that this condition was extremely broad, restrictive and unnecessary.[4] The merging parties maintained that other conditions placed upon them were sufficient to address any information sharing concerns.[5]

[46] The Commission indicated that the intention of the proposed condition was not to exclude everyone affected by the mentorship activities but rather just particular individuals with intimate knowledge of the mentorship program as they felt that kind of engagement could create a platform for the sharing of competitively sensitive information.[6]

[47] The Tribunal shared the Commission's concern regarding the potential for the Trust Fund to be used as a platform for information sharing and ultimately approved this transaction subject to the reworded condition in this regard, so as to afford the merging parties more flexibility in who they could appoint but also protect the Commission's concern. In this regard the parties were asked to engage with each other so as to preclude operational people from being appointed as trustees.[7]

[48] With regard to monitoring of the alliances, the merging parties must submit reports annually detailing the projects they have worked on during the joint venture. Further they must provide a report upon termination of the alliance.

Conclusion

[49] In light of the above, we concluded that the proposed transaction is unlikely to substantially prevent or lessen competition in any relevant market. Accordingly, we approved the proposed transaction subject to conditions. For convenience the set of conditions are "Annexure A".

Ms Yasmin Carrlm

Mr AW Wessels and Mrs Medi Mokuena concurring

22 March 2018

DATE

Case Manager:

Kameel Pancham

For the Merging Parties: Paul Coetser and Paul Cleland from Werksmans Attorneys

For the Commission: Busisiwe Ntshingila and Ratshidaho Maphwanya

[1] Aveng (Africa) (Pty) Ltd ("Avcng"), Basil Read Holdings (Pty) Ltd ("Basil Read"), Group Five Construction Limited ("Group Five"), Murray and Roberts Limited ("Murray and Roberts"), Raubex (Pty) Ltd, Stcfanutti Stocks (Pty) Ltd ("Stefanutti") and WBHO Construction ("WBHO").

[2] Road surfacing, bitumen, mesh and rebar.

[3] Transcript page 86, lines 1-3.

[4] Transcript page 59, lines 6-9.

[5] Transcript page 58, lines 13-14 & page 59, lines 1-9.

[6] Transcript page 66, lines 6-12.

[7] Transcript page 98, line 1-10.

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