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Investor Briefing 2: The Growth of M&A Regulation

This update is follow-up on our article "Investing in Kenya: M&A"

The number of M&A transactions in Kenya and the East African Community ("**EAC**") region generally continues to grow markedly, with predictors[1] painting an apparently rosy picture. In its first year of operation – 2012/2013, the Competition Authority of Kenya ("the **CAK**") reported having considered a total of 65 merger notifications, 17 restrictive trade practice cases, 3 exemption cases and 3 requests for advisory opinions.

Notably though, the scope of M&A regulation affecting transactions within Kenya, the EAC and the larger trading block - COMESA – has also grown steadily. Relevant regulations currently in force are the Competition Act of Kenya (the "**Act**") and the COMESA Competition laws. The looming entry into force of the EAC Competition laws portends the entry of the third applicable regulatory framework. While the growth of anti-trust laws in Kenya, COMESA and the EAC presents clarity, enhanced consumer protection and other benefits it also presents additional hurdles for potential investors.

What's new in Kenya?

The CAK in October, 2014 re-gazetted the merger filing fees as follows[2]:

Transaction thresholds (KES)	**Fees levied per proposed merger (KES)**
500 million – 1 billion (this threshold applies to the health sector only)	500,000
1 billion – 50 billion	1,000,000
Over 50 billion	2,000,000

This rhymes with the notification thresholds guidelines published by the CAK.

Although the CAK is yet to issue regulations, it has issued guidelines to clarify various aspects of the Act. The guidelines on exclusion thresholds provide clarity on the nature of transactions that may be excluded from prior approval by the CAK. The thresholds set below for exemption are pegged on the parties' cumulative assets or turnover and are also sectoral.

[1] Ernst and Young Attractiveness Survey, 2014 which ranked Kenya as the 3rd most attractive country in Africa to investors

[2] Gazette Notice No. 7406 dated 2nd October, 2014

Sector	Minimum Non-Excludable Threshold	Excludable Threshold
General undertakings	Combined threshold of KES 1 billion and turnover of target undertaking is more than KES 100 million	If combined turnover is between KES 100 million and KES 1 billion
Health care sector	Combined threshold of KES 500 million and turnover of target undertaking is more than KES 50 million	If combined turnover is between KES 50 million and KES 500 million
Carbon based mineral sector (includes oil, natural gas or coal but not their downstream retailing)	Value of reserves, rights and associated exploration assets to be held as a result of merger is more than KES 4 billion	If the value of reserves, rights and associated exploration assets is less than KES 4 billion
Oils Sector (where the merger involves pipelines and pipeline systems receiving oil and gas from fields belonging to & passing through the meters of the target	Value of reserves is below KES 4 billion	

Transaction appraisals consider whether the proposed transaction will result in substantial lessening of competition and apply the public interest test. Assessments of the likelihood of substantial lessening of competition primarily focus on possible market disruptions including strengthening of positions of dominance and the minimization of efficiency in production and distribution among others. Export mergers are likely to be under less scrutiny for this criterion.

The public interest test is essentially an assessment of what impact the proposed transaction will have on existing jobs vis-à-vis the likely efficiencies to be gained from the transaction. This is hardly surprising bearing in mind the proactive stance to job creation and protection globally.

CAK, CCC and ECA; three strikes?

M&A transactions within the COMESA block, as discussed in Part 1 of our investor briefing series, are subject to the jurisdiction of the COMESA Competition Commission (the "CCC"). The looming entry into force of the EAC Competition Act and the establishment of the EAC Competition Authority will create three parallel regulatory regimes to which M&A transactions are subject to in Kenya. The EAC Competition Act applies to all economic activities and sectors having a cross-border effect within the block as does the COMESA framework.

The COMESA Determination of Merger Notification Threshold Guidelines require merger notifications where either one or both the acquiring and target firms operate in two or

more member states. This position was clarified by the COMESA Merger Assessment Guidelines, 2014 which define operating as an undertaking having an annual turnover or value of assets in any member state exceeding US $ 5million. Additionally, the merger ought to have a regional dimension. If more than two-thirds of the annual turnover or value of assets of each of the merging parties is achieved within one and the same member state then such a merger is deemed not to have a regional dimension and is not notifiable. This clarification offers some relief with respect to the merger notification thresholds which were previously set at zero, effectively making all mergers notifiable.

The COMESA Assessment Guidelines also provide for pre-notification consultation either in person on phone or by any other appropriate means. Pre-notification consultation is an effective way for parties to get clarification from CCC as to whether the intended transaction is a notifiable merger and on any other matters. Parties may also request for comfort letters from CCC which categorises/distinguishes whether the intended transaction as a notifiable merger or not. Comfort letters are to be issued within 21 days of request. The clarifications on notification thresholds and the inclusion of pre-notification consultation and comfort letters by CCC are a welcome reprieve for investors as the process is considerably clearer and shorter for non-notifiable mergers. The possibility of losing US $ 500,000 on an unnecessary notification is also significantly lower.

The EAC Competition Act, similar to its counterparts, requires approval by the EAC Competition Authority (the "ECA") prior to the coming into effect of any proposed merger or acquisition. However, the ECA is yet to define its notification thresholds and has not defined a 'cross-border effect' which means that all mergers within the EAC member states have to be notified to the ECA.

The EAC – comprising Kenya, Tanzania, Uganda, Rwanda and Burundi – is geographically speaking, essentially a subset within the larger COMESA block. The COMESA framework describes itself as having primacy over domestic laws but does not grant the CCC exclusive jurisdiction to assess regional mergers. Essentially therefore approvals from all three regulatory bodies may have to be sought for transactions affecting two or more countries within EAC and COMESA. The approval application is naturally accompanied by the filing fees which vary in Kenya as tabulated above. The merger filing fees for EAC are yet to be determined while that for COMESA varies up to a maximum of COM$ 500,000 (the COM dollar being equivalent to the US dollar) Approval by the ECA is to be made within 45 days. The CAK issues its approval within 60 days and the CCC issues its approval within 120 days.

As it is, the cost of notifiable transactions with 'cross border' effect touching any two EAC countries will be significantly higher owing to the need, in certain cases, to get all three approvals. The procedure itself becomes unduly long as well. Paradoxically, if a domestic regulator approves a transaction with 'cross border' effect, the CCC or the ECA can decline to issue an approval.

The existence of these parallel regulatory regimes without a centralised co-ordination or referral mechanism will undoubtedly result in continued challenges to the applicability of the regional laws. The question fundamentally becomes one of supremacy of law. While both the COMESA and EAC regimes aspire to a form of supra-nation none have fully attained this status. In addition the question of the

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superiority of the COMESA and EAC frameworks and their enforcement is untested.

There is thus an urgent need for clarity in relation to the hierarchy of the approvals and the cohesion of the three regimes.

The Kenyan judiciary has adopted a purposive approach in resolving conflicts of hierarchy between domestic and international laws. In resolving the supremacy battle, the judiciary examines each instance as presented and has repeatedly upheld the supremacy of domestic legislation as an expression of the sovereignty of the people which is at the pinnacle of the hierarchy.[3] However this position is yet to be tested with respect to the face-off between domestic competition laws and the looming showdown between the EAC and COMESA frameworks.

On the flipside, the CCC naturally contends that the COMESA Regulations are superior to domestic laws and that any conflict ought to be adjudicated by the COMESA Court of Justice. Undoubtedly with the entry into force of the EAC framework, the lines will become even more blurred. One wonders what effect this will have on investor confidence.

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[3] See the reasoning in Beatrice Wanjiku & Another V Attorney General & Another [2012] eKLR, Diamond Trust Kenya Ltd v Daniel Mwema Mulwa Civil Case No. 70 of 2002 and followed in Republic v Permanent Secretary Office of the President Ministry of Internal Security & another Ex-Parte Nassir Mwandihi [2014] eKLR