DLA CLIFFE DEKKER HOFMEYR

COMPETITION

MATTERS

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IN THIS ISSUE

MINISTER OF ECONOMIC DEVELOPMENT APPOINTS COMPETITION COMMISSIONER

Cliffe Dekker Hofmeyr congratulates Mr Tembinkosi Bonakele on his appointment as the Competition Commissioner following his acting in this position for the past six months. Cliffe Dekker Hofmeyr wishes him a prosperous career in his new position.

TRIBUNAL DISMISSES CASE AGAINST SAB

On 24 March 2014, the Competition Tribunal (Tribunal) issued its reasons in respect of a matter concerning the distribution systems of South African Breweries Limited (SAB). SAB contracts with distributors for the distribution of its products on terms that grant these distributors exclusive territories for the distribution of SAB products at a distribution fee (in the form of a discount on the retail price).

The Competition Commission's (Commission) case was that SAB's conduct amounted to unlawful price discrimination in contravention of s9 of the Competition Act, No. 89 of 1998 (Act) to the extent that it charged a different price to its authorised distributors (being retail price minus a discount) than to other distributors (being the retail price), market division in contravention of s4(1)(b) of the Act as it agreed not to compete with its authorised distributors for the distribution of SAB products in the exclusive territories and, alternatively, a vertical restrictive practice in contravention of s5(1) by virtue of the territorial carve-outs being anti-competitive and not capable of justification.

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In respect of the market allocation charge the Tribunal noted that SAB, through enforcing exclusivity in respect of its authorised distributors, may have engaged in conduct that amounted to market allocation. No (formal or informal) agreement existed between the authorised distributors in respect of the exclusive territories, but SAB, allegedly, acted as the hub in a hub-and-spoke arrangement in respect of this market allocation arrangement. In addition, SAB, in performing certain of its distribution functions itself, was a competitor of its authorised distributors and stood in a horizontal relationship with them. The Tribunal, however, considered a characterisation argument in respect of the ostensible transgression of s4(1)(b) of the Act.

The Tribunal considered whether SAB and its authorised distributors are basic economic units independent of SAB. In the absence of guiding case law and precedent on how to identify the boundary between a single and basic economic unit, the Tribunal concluded that the authorised distributors are not sufficiently independent of SAB in the manner that would make them competitors of SAB in respect of the distribution of products. This reasoning was not based on a single economic entity theory, but rather on the characterisation of the relationship between SAB and its authorised distributors and a conclusion that this type of independent, yet highly interrelated (and controlled), conduct is not the type of conduct the Legislature intended to prohibit as *per se* collusive.

In respect of the vertical and horizontal restrictive practices complaint against SAB, which are analysed based on the rule of reason, the Tribunal concluded that the Commission could not successfully show that there was a substantial lessening or prevention of price competition, as it was shown that the current distribution system employed by SAB in fact leads to the cheapest possible prices to customers and that there was insufficient evidence to prove a lessening of non-price competition.

The Commission, further, brought a case that the differentiation by SAB between its authorised distributors and other distributors in granting discounts on the retail price as remuneration for distribution services amounted to prohibited price discrimination in terms of s9(1) of the Act. SAB's approach, in other words, is that most customers except its authorised distributors are treated as retail customers and are charged retail prices for its products. The Tribunal found that the transactions between SAB and authorised distributors, on the one hand, and independent distributors, on the other hand, were not functionally equivalent, to render these transactions equivalent and capable of scrutiny under s9 of the Act.

The Commission further brought a charge of resale price maintenance against SAB in respect of the obligatory use of a computer system that limited authorised distributors from setting their own price. The Tribunal found that there was no evidence to suggest that SAB intentionally imposed the computer system on its authorised distributors in order to enforce a system of resale price maintenance or penalised its authorised distributors for granting discounts and, hence, s5(2) of the Act was not transgressed.

Accordingly, the Tribunal dismissed all charges against SAB and its authorised distributors. This decision by the Tribunal is currently the subject of an appeal by the Commission to the Competition Appeal Court.

Leana Engelbrecht

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COMPETITION COMMISSION APPEALS THE TRIBUNAL DECISION DISMISSING CHARGES AGAINST SAB

On 24 March 2014, the Tribunal dismissed all charges against SAB and its authorised distributors in a matter that has been on-going for 10 years. The ruling by the Tribunal was a landmark decision relating to the relationship between suppliers and their distributors and instances where such a relationship, due to a lack of sufficient independence between the parties, cannot be characterised as the type of conduct, which the legislature intended to prohibit as collusive conduct in terms of s4(1)(b) of the Act. The Tribunal further dismissed charges against SAB and its authorised distributors relating to vertical restrictive practices, resale price maintenance and prohibited price discrimination.

On 14 April 2014 the Commission appealed this decision by the Tribunal to the Competition Appeal Court (CAC) on, amongst other, the following grounds:

(i) The Tribunal erred in its conclusion that SAB and its authorised distributors could not be understood to be competitors as contemplated in s4(1)(b) of the Act relating to per se prohibited horizontal restrictive practices;

(ii) S4(1) of the Act does not envisage or require an analysis of whether the firms are sufficiently independent to stand in a horizontal relationship and the only defence in this regard is a single economic entity defence in terms of s4(5), which the Tribunal acknowledged was not raised by the respondents and the respondents, in any event, do not satisfy;

(iii) That SAB and its authorised representatives, in fact, are competitors (or at least potential competitors) and the conduct engaged in constitutes market allocation in contravention of s4(1)(b)(ii) of the Act;

(iv) There was sufficient evidence to prove a substantial lessening or prevention of competition in respect of the complaint of vertical restrictive practices in terms of s5(1) of the Act, as the arrangements between SAB and its authorised distributors, amongst other reasons, are harmful to consumer welfare, limit competition between authorised distributors, and the exclusive territories granted in terms of the arrangement between SAB and its authorised distributors provide these authorised distributors with a captive consumer base and an opportunity to charge monopoly prices and to operate inefficiently;

(v) The transactions between SAB its authorised distributors and independent distributors are equivalent transactions and the Tribunal erred further considering the charge of prohibited price discrimination in contravention of s9(1) of the Act and should have concluded that SAB engaged in price discrimination with reference to its relationship with its authorised distributors and independent distributors;

(vi) For resale price maintenance to be proven, the presence of intention is irrelevant and the Tribunal should have concluded that SAB transgressed s5(2) of the Act by engaging in resale price maintenance, which the Commission argues it did intentionally.

The Commission seeks an administrative penalty against SAB in the total amount of R1,856,320,000 including certain behavioural remedies should its appeal in respect of all the charges against SAB succeed.

Leana Engelbrecht

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EXCLUSIVITY CLAUSES IN LEASE AGREEMENTS STILL SUBJECT TO SCRUTINY

After a lengthy investigation into long-term exclusive lease agreements between retail grocery anchors (such as Shoprite, Spar and Pick n Pay) and their landlords, the Competition Commission (Commission) decided not to refer the investigation to the Competition Tribunal. The Commission indicated that its investigation did not yield conclusive evidence to meet the legal hurdles in proving the anti-competitive effects of all exclusivity clauses in long-term lease agreements. Notwithstanding this, it appears that the Commission remains concerned about their potential anti-competitive effects and is intent on policing this on a case by case basis.

The Commission recently conditionally approved the acquisition by Arctozone Investments Proprietary Limited of the Lynnridge Mall. Although the transaction did not give rise to competition concerns, the Commission found that an exclusivity clause in the lease agreement between the landlord and one of the retail anchors gave rise to a potential public interest concern. As a result, the Commission approved the merger on condition that Arctozone, as the new landlord, undertake to negotiate with the anchor retailer in the utmost good faith to have the exclusivity clause removed within a stipulated time period following the Commission's decision. During its investigation, it was a common practice of the Commission to impose similar conditions in merger transactions. However, this is the first merger to be approved with such a condition since the Commission's non-referral in January 2014.

The Commission's general concerns relating to exclusivity clauses in favour of anchor retailers are that these clauses may prohibit the landlord from introducing competing grocery stores, bakeries, cafés, delicatessens, butcheries and other part-line stores into shopping centres, thus possibly increasing the barriers to entry faced by smaller independents in competing with anchor retailers. Ultimately, according to the Commission, this leads to consumers being denied the benefits of increased choice of product and price competition between retailers.

In its March 2014 newsletter, the Commission indicates that it aims to address these issues through advocacy engagements with key industry stakeholders. Its current position is as follows:

- In the case of new property developments, parties should refrain from entering into long-term exclusive agreements by default and the use of these clauses should be justified by the anchor retailer's investment in the particular shopping centre.
- The duration of the exclusivity granted should be related to the length of the financing agreements or the period required to recoup the initial investment that the anchor retailer makes in a particular shopping centre.

In conclusion, whilst the Commission was unable to refer for prosecution a blanket investigation against all retail exclusivity due to a lack of evidence, it remains intent on policing individual arrangements where it is of the view that any potential anti-competitive effects cannot be justified on the basis of the investment made or otherwise.

Nazeera Mia and Susan Meyer

THE COMPETITION TRIBUNAL ISSUES ITS REASONS FOR APPROVING ASPEN'S ACQUISITION OF PFIZER'S INFANT NUTRITION BUSINESS

In its reasons for approving Aspen Nutritionals, a division of Pharmacare Limited (Aspen) acquisition of Pfizer's infant nutrition business, issued on 2 April 2014, the Competition Tribunal (Tribunal) cautions the Department of Health regarding measures introduced to achieve the Department's policy objectives, which may inadvertently impact on competition.

Aspen Nutritional's acquisition of the Pfizer infant nutrition business followed an order by the Competition Tribunal that Nestlé, which acquired the worldwide infant nutrition business of Pfizer, divest itself of the infant nutrition business in South Africa through a rebranding remedy. This was the first such remedy in South Africa and flowed in part from the strong brand loyalty consumers of infant nutrition display.

According to the Tribunal consumer brand choice is heavily influenced by the recommendations of health care professionals, family and friends. Consumers carry this brand choice into retailers when purchasing infant nutrition.

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The infant nutrition market, and in particular the infant milk formula market, is highly regulated internationally. Specifically, the World Health Organisation (WHO) has adopted an international code of conduct that governs the marketing of breast milk substitutes to consumers. The rationale behind the code is to promote breastfeeding on the basis that it is superior to breast milk substitutes.

To give effect to this code, the Minister of Health published South African regulations in December 2013. The effect of these regulations is to prohibit infant milk formula manufacturers from communicating the benefits of their products to consumers.

The Tribunal expressed concern regarding the evidence before it that the regulations, although clear in terms of their rationale, may also have the unintended consequence of raising barriers to entry for new entrants into the infant milk formula market as these new entrants would struggle to raise awareness of their brands with consumers.

The Tribunal encouraged the Competition Commission to engage with the Department of Health to ensure that they balance their respective policy objectives.

Albert Aukema

FIRST ADDRESS BY THE PANEL OF THE PRIVATE HEALTHCARE INQUIRY

On 16 April 2014, the Panel of the Competition Commission's Private Healthcare Inquiry, through the presiding Chairperson, retired Chief Justice Sandile Ngcobo, addressed stakeholders in respect of matters relevant to the Private Healthcare Inquiry.

The Chairperson remarked that the purpose of the Private Healthcare Inquiry "…is to determine whether the process of competition is working well or can be improved effectively in a market as a whole. Market inquiries provide a framework for identifying, analysing and, where appropriate, remedying sector-wide or market-wide competition problems".

The Chairperson comforted stakeholders by indicating that the inquiry is not accusatorial in nature and nobody is accused of anti-competitive conduct, but rather the focus and aim of the inquiry is to analyse competition in the private healthcare market holistically while giving effect to the principles of fairness. Nevertheless, it is a reality that the market inquiry may lead to complaint initiations against certain firms or other relevant remedies allowed for in terms of the Competition Act, No 89 of 1998 (Act).

The Chairperson further indicated that rules of engagement (or administrative guidelines) that govern the conduct of the market inquiry are in the process of being developed and it is anticipated that these rules of engagement will be published by the end of May for comment by stakeholders and will ultimately be published on 1 August 2014. The administrative guidelines will determine the manner in which stakeholders engage with the Panel and will facilitate the gathering of information and the conduct of the market inquiry including, how confidential information is deal with, the conduct of public hearing, the submission of information to the Panel, administrative phases of the inquiry and the expected outcomes of the inquiry.

A further statement of issues will be published together with the administrative guidelines to set out what the anticipated scope of the investigation of the inquiry would be. The Chairperson stressed that stakeholder participation will be welcomed in settling the statement of issues and that the statement of issues may, from time to time, be revised.

It was further indicated that perceived theories of harm (being the perceived conduct that amounts to harmful competitive effects in the market for private healthcare) that have been identified to guide the Panel in its investigations during the inquiry include market power and market concentration, barrier to entry and expansion, imperfect information, the existing regulatory framework and vertical relationships.

The provisional timetable in respect of the main stages of the inquiry was announced as follows:

- 31 May 2014: Statement of issues and administrative guidelines issues for public comment;
- 30 June 2014: Panel to receive comments on the statement of issues and administrative guidelines;

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- 1 July 2014 – 31 July 2014: Panel to incorporate comments on statement of issues and administrative guidelines;
- 1 August 2014: Final statement of issues and administrative guidelines to be published;
- 1 August 2014: Call for submissions on subject matter of the Inquiry;
- 1 August 2014 – 30 October 2014: Submission on subject matter of the inquiry to be received;
- 1 November 2014 – 31 January 2015: Analysis of information;
- 1 March 2015 – 20 April 2015: Public hearings;
- 1 May 2014 – 31 July 2015: Analysis and targeted public hearings and information requests; and
- October 2015: Publishing provisional findings and recommendations.

The Chairperson urged stakeholders to participate in the inquiry as frank and comprehensive participation will lead to various perceived benefits to consumers, market participants, Regulators and Government.

Leana Engelbrecht

RESIN MERGER DOES NOT RESONATE WITH THE COMMISSION

The Competition Commission (Commission) has recommended that the merger between Ferro Industrial Products and Arkema Resins be prohibited. The Commission argues that the merger will remove the only competitor to Ferro in the provision of composite resin to the mining sector. Even in other sectors, the Commission contends that the combined market share of the parties will be around 64%, with only a small local supplier and some imports as a constraint. In recommending outright prohibition, the Commission was unwilling to consider alternative remedies, such as divestiture of Arkema's composite business or imposing a pricing formula

Large mergers are ultimately decided by the Competition Tribunal (Tribunal) as a matter of course, and the merging parties will have the opportunity to contest the Commission's findings. A lot may turn on, firstly, the barriers to expansion for the rest of the market (ie can the small local player and imports expand capacity to counter any price increases) and secondly, whether in the mining segment (where the Commission alleges a merger to monopoly) the countervailing powers of the large mines (in terms of price and the ability to facilitate entry) is sufficient to keep pricing at competitive levels.

The authorities have not always been so conservative. In 2004, the Tribunal unconditionally approved Murray and Roberts' acquisition of The Cementation Company, where substantial concerns about the effect of the merger on mining customers gave way to the realisation that as the mines are price takers in their own product market, they could not pass on any increases and moreover had an incentive to resist price increases, and the countervailing power to do so (being sophisticated purchasers making large purchases).

In 2006, in deciding the ferrochrome merger involving International Mineral Resources AG and Kermas South Africa, the Tribunal endorsed the view that the likelihood of non-competitive pricing is curtailed when sophisticated large buyers, making large purchases, are present. Admittedly, while both gave rise to substantial consolidation of important competitors, neither of these deals involved mergers to monopoly. In 2010 when Chlor-Alkali sought to acquire Botash, the Tribunal allowed the merger subject to conditions regarding maximum pricing and long term contracts

The lawyers for the merging parties will no doubt hearken to these decisions, but it may be that the authorities are no longer willing to play pricing regulator, or perhaps the downturn in the mining industry has made the regulator less bullish on the industry's ability to counter the pricing demands of suppliers.

With the mining industry in decline, one might welcome consolidation at the supplier level to cope with muted and uncertain demand and the merger is clearly an important one for the parties concerned. However, a balance needs to be drawn between the interests of suppliers and customers and in this instance and as usual, the Commission appears to be in the customers' corner.

Chris Charter

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COMMISSION CONCLUDES CONSENT ORDER WITH MARTINAIR CARGO IN RESPECT OF FUEL SURCHARGES PRICE FIXING COMPLAINT

In March 2006, the Competition Commission (Commission) initiated a complaint against Martinair Cargo, a division of Martinair Holland N.V (Martinair) and other airlines following the submission of a leniency application by Lufthansa Cargo AG under the Commission's Corporate Leniency Policy. The complaint related to alleged price fixing of fuel surcharges in the international market for the provision of air freight and/or cargo services, including such services into and from South Africa.

The Commission's investigation revealed that information exchanges between competitors, including Martinair, occurred on the subject of fuel surcharges, this being a component of the total price charged for the provision of cargo services. Put differently, in imposing fuel surcharge rates, the investigation indicated that Martinair did not act independently of its competitors. Accordingly, the Commission's investigation revealed that Martinair's conduct constituted a contravention of the Competition Act, No 89 of 1998 (Act).

Following the Commission's investigation, Martinair elected to settle the matter with the Commission, thereby entering into a settlement agreement, which was subsequently referred to the Tribunal to be confirmed as an order of the Competition Tribunal. The settlement agreement included an admission of having contravened the Competition Act as well as agreement to pay an administrative penalty of USD$ 533,517.38.

The settlement agreement also records Martinair's pre-existing competition law compliance programme, instituted in an effort to prevent further competition law violations. This recordal is a reminder to firms to pro-actively ensure that internal compliance programmes are put in place, as this may find favour with the authorities when considering sanctions to be imposed as a consequence of contraventions of the Competition Act.

Lerisha Naidu and Christelle Wood

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