12 AUGUST 2020

COMPETITION **ALERT**

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Excessive pricing during COVID-19 and beyond: Key considerations (Part 1)

Just three days after the declaration of a national state of disaster on 15 March 2020, the Minister of Trade and Industry published the Consumer and Customer Protection and National Disaster Management Regulations and Directions (Regulations).

Excessive pricing during COVID-19 and beyond: The cautionary tale of Babelegi and Dis-Chem (Part 2)

Part 2 will discuss the Competition Tribunal's seminal judgments of Babelegi and Dis-Chem, dealing with excessive pricing during COVID-19.

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Excessive pricing during COVID-19 and beyond: Key considerations (Part 1)

This article will explore the applicability of the Regulations, as recently discussed by the Competition Tribunal in the two COVID-19 excessive pricing contested cases to date.

Just three days after the declaration of a national state of disaster on 15 March 2020, the Minister of Trade and Industry published the Consumer and Customer Protection and National Disaster Management Regulations and Directions (Regulations). Regulation 4 provides a mechanism in terms of which the Competition Commission (Commission) is able to establish *prima facie* that a price is excessive or unfair, which in turn can lead to a finding that the excessive pricing provisions of the Competition Act 89 of 1998 (Act) have been contravened.

Since 19 March 2020, the Commission has investigated over 800 complaints of excessive pricing, successfully prosecuting two firms after contested hearings (which may still be subject to appeals) and reaching settlements with 32 companies. As at the date of this alert, this has resulted in fines in excess of R15.4 million being imposed, of which just short of R5.6 million has been donated to the Solidarity Fund. There have also been donations of essential goods to affected communities to the value of some R551,887. However, rather curiously, reliance on the Regulations in securing the prosecutions has been limited.

This article will explore the applicability of the Regulations, as recently discussed by the Competition Tribunal (Tribunal) in the two COVID-19 excessive pricing contested cases to date, namely *Babelegi Workwear Overall Manufacturers and Industrial Supplies CC (Babelegi)* and *Competition Commission and Dis-Chem Pharmacies Limited (Dis-Chem)*.

For the Regulations to be triggered, a dominant firm must apply a material price increase in relation to certain goods and services that fall within its ambit, namely "*basic food and consumer items; emergency products and services; medical and hygiene supplies; [and] emergency clean-up products and services*". The Regulations create a rebuttable presumption that a price increase is *prima facie* excessive or unfair if it "*does not correspond to or is not equivalent to the increase in the cost of providing that good or service; or increases the net margin or mark-up on that good or service above the average margin or mark-up for that good or service in the three-month period prior to 1 March 2020*" (the so-called 'Rebuttable Presumptions').

To date, the vast majority of the aforementioned settlement agreements and the two contested hearings have involved medical and hygiene supplies. There have, however, been three recent settlement agreements implicating basic food and consumer items, namely raw ginger, maize meal and eggs.

The Regulations self-proclaim to be of no force and effect when the COVID-19 outbreak is no longer declared a disaster. It is now confirmed that the Regulations also have no application to price increases which took place prior to the proclamation of the Regulations. First, the Tribunal in *Babelegi* held that, when assessing the merits of that case, it would have no regard to the Regulations on the basis that the complaint period preceded the publication of the Regulations. The Tribunal reinforced this approach in *Dis-Chem*, highlighting

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Firms are encouraged to remain vigilant, particularly in the light of the Tribunal's seminal and generous interpretation of key aspects of the Act in *Babelegi* and *Dis-Chem*, which will likely have a profound precedential value going forward, as detailed in Part 2 of this article.

that it is a fundamental principle of the rule of law that legislation, whether subordinate or not, cannot apply retrospectively. Based on this and the principle of fairness, the Tribunal confirmed that the courts would not lightly dispense with the presumption against retrospectivity.

This does not mean that dominant firms who implemented excessive price increases before 19 March, or who do so after the national state of disaster ends, acted or will act, with impunity. Notwithstanding the inapplicability of the Regulations to such conduct, price increases related to COVID-19 are now, based on the Tribunal's interpretation in the *Babelegi* and *Dis-Chem* cases, fairly easily caught under the excessive pricing provision in section 8(1)(a) of the Act, despite this prohibition having historically been rarely applied.

As confirmed in *Dis-Chem*, the inapplicability of the Regulations means there can be no application of the Rebuttable Presumptions in the Regulations. However, the severity of this consequence is tempered by the Tribunal's confirmation that, despite the Regulations being inapplicable, the economic tests underlying Regulation 4 can still establish a *prima facie* case of excessive pricing in terms of the Act. Simply put, one such test is whether prices increase significantly without any increases in costs. Further, in terms of recent amendments to the Act, there is now also a reverse onus in terms of which the evidential burden to show reasonableness of a price increase shifts to the dominant firm if a *prima facie* case of an excessive price has been shown. Viewed collectively, these developments render it significantly easier to prosecute an excessive pricing complaint.

During these unprecedented times, the excessive pricing provisions, whether in terms of the Act or the Regulations, remain an important consideration. Firms are encouraged to remain vigilant of their pricing conduct, particularly in the light of the Tribunal's seminal and generous interpretation of key aspects of the Act in *Babelegi* and *Dis-Chem*, which will likely have profound precedential value going forward in evaluating market power and dominance generally as well as excessive pricing complaints, as detailed in Part 2 of this article, below.

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CDH'S COVID-19
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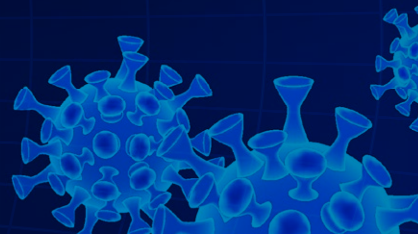

Excessive pricing during COVID-19 and beyond: The cautionary tale of Babelegi and Dis-Chem (Part 2)

Abuse of dominance cases generally used to commence with the same opening scene of defining the relevant market in which the antagonist was alleged to be dominant. However, following *Babelegi* and *Dis-Chem*, this script has been rewritten.

In Part 1 we addressed the practical means by which an excessive pricing complaint may be investigated in terms of the Consumer and Customer Protection and National Disaster Management Regulations and Directions (Regulations). It was emphasised that, despite the Regulations not applying to material price increases implemented by dominant firms prior to 19 March 2020, when the national state of disaster commenced, or after the state of disaster ends, this did/does not mean that such firms act without consequences in terms of the Competition Act 89 of 1998, as amended (Act).

This theme has been reinforced by the Competition Tribunal (Tribunal) in its recent decisions of *Competition Commission and Babelegi Workwear Overall Manufacturers and Industrial Supplies CC (Babelegi)* and *Competition Commission and Dis-Chem Pharmacies Limited (Dis-Chem)*, which found that the excessive pricing abuse of dominance provisions of the Act had been contravened.

In Babelegi, over the complaint period of 31 January to 5 March 2020, the respondent's average mark-up for masks was alleged to be in excess of 500%, with price increases alleged to be as high as 987%. Babelegi was alleged to have a market share of less than 5% for the sale of the relevant masks (with Babelegi submitting that even this approximation was grossly overstated).

Dis-Chem involved a JSE listed national pharmaceutical retailer who was alleged to have implemented price increases on its masks of some 47 - 261%. The Competition Commission (Commission) alleged that Babelegi and Dis-Chem's respective conduct amounted to an abuse of dominance in the form of excessive pricing. Pursuant to contested hearings, the Tribunal agreed with the Commission in finding both Babelegi and Dis-Chem had indeed contravened the Act, and levied respective administrative penalties of R76,040 and R1,200,000.

The decisions posit pertinent precedent with regard to the future interpretation of the Act. For example, abuse of dominance cases generally used to commence with the same opening scene of defining the relevant market in which the antagonist was alleged to be dominant (after all, firms cannot be dominant in a vacuum). However, following *Babelegi* and *Dis-Chem*, this script has been rewritten.

Despite the Regulations being found to be inapplicable in *Babelegi* and *Dis-Chem*, the economic test that was applied by the Tribunal to determine whether there was excessive pricing is markedly similar to the tests proposed by the Regulations. This is consistent with the Tribunal's statement in *Dis-Chem* that the economic tests contained in regulation 4 of the Regulations (as discussed in Part 1), while inapplicable to the facts of the case, nevertheless can still inform an excessive pricing analysis under section 8 of the Act.

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In concluding that Babelegi was a dominant firm for the purposes of the Act, the Commission and the Tribunal dispensed with the need to define a relevant market, having held that *"there is no compelling reason to engage in market delineation if other means exist to determine market power".*

Opening scene: Market definition, market power and dominance

The excessive pricing prohibition under section 8(1)(a) of the Act is only applicable to dominant firms (provided that annual turnover or asset value of the firm alleged to be dominant meets or exceeds R5 million).

In terms of the Act, firms with a market share of 45% or more are presumed to be dominant on an irrebuttable basis. If a firm has at least 35% but less than 45% of a relevant market, there is a rebuttable presumption of dominance, unless the firm can show that it does not have market power. A firm with less than 35% of a relevant market, is assumed not to be dominant, unless it can be shown to have market power. The concept of 'market power' is in turn defined in the Act as *"the power of a firm to control prices, to exclude competition or to behave to an appreciable extent independently of its competitors, customers or suppliers"*.

In concluding that Babelegi was a dominant firm for the purposes of the Act, the Commission and the Tribunal dispensed with the need to define a relevant market, having held that *"there is no compelling reason to engage in market delineation if other means exist to determine market power"*.

In *Dis-Chem*, the Commission similarly did not undertake a relevant market definition or market share analysis as its approach to establishing market power, and in turn dominance, was 'inferential' (i.e. inferred from Dis-Chem's conduct itself). *Dis-Chem* had argued that it is a requirement of the Act to define the relevant market in which it is alleged that there is an exertion of market power, as this is essential in determining whether a firm is dominant. The Tribunal conceded that market shares and defining the relevant market are usually the analytic tools deployed when assessing market power, but held that these are not the only tools and that, in some cases, direct evidence could be relied upon instead, such as price increases or the imposition of terms and conditions.

In seeking to establish market power, the Tribunal posited the question as follows: *"what advantages does this global health crisis confer on Dis-Chem, advantages that it would otherwise not enjoy in the counterfactual world of normal market conditions?"*

The Tribunal subsequently held, astonishingly so if considered through the lens of the case law preceding COVID-19, that: *"[a] store, by merely having PPE products in the context of such excess demand could enjoy market power. Multiple firms – even stores located in the same shopping mall – could conceivably exercise market power in the supply of PPE vis-à-vis their customers"*.

In *Dis-Chem*, the Tribunal further confirmed that *"at the level of principle, it cannot be refuted that market power can be inferred from a firm's economic behaviour"*. The successive price increases that were implemented on certain face

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It is clear that in both cases the Tribunal was at pains to emphasise the context of the COVID-19 outbreak, suggesting it would be in dereliction of its duty if it did not intervene in a timely manner in states of natural disasters or emergencies to protect vulnerable consumers.

masks, which allegedly resulted in a significant increase in Dis-Chem's margins, viewed alongside the increased demand for face masks, was in the Tribunal's view indicative that Dis-Chem both enjoyed and exerted market power. By virtue of this alone, Dis-Chem was held to be dominant for the purposes of the Act.

As always however, context is important. In Babelegi, the Tribunal emphasised that the market power enquiry cannot be divorced from the national socio-economic COVID-19 crisis, having held that the latter can confer market power on firms that ordinarily would never have enjoyed consideration as being dominant. In *Dis-Chem*, on the gateway issue of dominance and the relevant market, the Tribunal accentuated that material price increases of life essential items such as masks, even in the short run, in a health disaster such as the COVID-19 outbreak, warrants the Tribunal's intervention.

It is clear that in both cases the Tribunal was at pains to emphasise the context of the COVID-19 outbreak, suggesting it would be in dereliction of its duty if it did not intervene in a timely manner in states of natural disasters or emergencies to protect vulnerable consumers. This does beg the question as to whether, going forward, the Commission will be able to replicate its successful assertion of market power and dominance without defining a market, in cases where such extreme market conditions are absent.

The plot thickens: Economic test

In terms of setting the scene, the essence of the economic test in section 8 of the Act is to determine whether a price charged by a dominant firm is higher than a 'competitive price'. The Act provides for a non-exhaustive list of factors to be considered in an enquiry as to whether a price is higher than a competitive price. If a *prima facie* case of excessive pricing has been shown by the prosecutor (in the *Babelegi* and *Dis-Chem* cases, this character being the Commission), the evidential burden to prove the price increases were reasonable, shifts to the dominant firm. This reverse onus is a novel plot twist introduced by recent amendments to the Act.

In *Babelegi*, the Tribunal found that the successive nature of Babelegi's price increases and mark-ups and the significant levels thereof, together with an alleged failure to provide a credible justification was sufficient to prove a *prima facie* case of abuse of dominance in the form of excessive pricing. It then concluded that there was unreasonableness on the basis that the prices and mark-ups bore no reasonable relation to Babelegi's prices and mark-ups prior to the complaint period (as this was, in the Tribunal's view, the appropriate benchmark of what competitive prices and mark-ups would be under conditions of normal and effective competition).

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For the time being, and unless the story is retold on appeal, market power can be inferred from a firm's economic behaviour alone, and in the context of COVID-19, can even be temporary.

In *Dis-Chem*, the Tribunal confirmed that where a dominant firm, in the context of a health crisis, increases its prices significantly without any increases in costs, this alone could establish *prima facie* that its new prices are higher than the competitive benchmark, and that "*there is no need to quantify this benchmark more precisely*." The Tribunal reasoned that in the economic conditions of the COVID-19 outbreak, masks are as essential to consumers as water is in a drought, which in turn, conferred on Dis-Chem the ability to allegedly materially increase its prices for the masks, in a manner it could not have done in the counterfactual world of normal market conditions. The relevant comparator or "*competitive price*" used by the Tribunal in this exercise was Dis-Chem's own pricing or margins prior to its March increases which were under scrutiny. In the Tribunal's view, Dis-Chem was unable to discharge the burden of showing that its price increases were reasonable in the context of COVID-19.

In finding that Babelegi and Dis-Chem had both contravened sections 8 of the Act by charging excessive prices, it is interesting to note that the economic tests applied in both cases substantially echoed those provided for in the Regulations.

Conclusion

In terms of *Babelegi* and *Dis-Chem*, the abuse of dominance provisions of the Act cast a much wider net, potentially catching small firms, who may have previously disregarded these provisions in their compliance efforts. While the Regulations are only of force for a limited duration, the Tribunal's analysis in both *Babelegi* and *Dis-Chem* was in terms of the Act, such that the legacy of the Tribunal's prescripts may hold relative permanency. In terms of this cautionary tale, all firms, regardless of their size, are encouraged to remain cognisant of their pricing policies and practices.

For the time being, and unless the story is retold on appeal, market power can be inferred from a firm's economic behaviour alone, and in the context of COVID-19, such power can even be temporary.

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