Submission to the Competition Policy Review

The South African Example: A Legislated Effects-Based Test and Efficiency Defence for Misuse of Market Power

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1 Introduction

1.1 This submission is made in respect of the Review Panel's consideration of the prohibition of misuse of market power in section 46 of the *Competition and Consumer Act 2010* (Cth) ('the CCA'), foreshadowed in paragraphs 5.8 to 5.10 of the Competition Policy Review Issues Paper. It is made for the limited purpose of summarizing the legislation in respect of unilateral anti-competitive conduct in the Republic of South Africa.

1.2 South Africa provides an example of a jurisdiction that has attempted to identify modern 'best practice' on unilateral anti-competitive conduct and to incorporate this practice in its legislation. In particular, the South African provisions in respect of unilateral anti-competitive conduct draw on both European Union law and United States law in this field, and expressly require the courts to weigh the anti-competitive effect of a dominant firm's conduct against any claimed efficiency gains arising from that conduct.

2 The Context of the South African Competition Act in Brief

2.1 The *Competition Act 1998* (South Africa) ('the Act') addresses those aspects of market structure and conduct commonly addressed in modern competition legislation, including mergers,[1] horizontal anti-competitive conduct,[2] vertical anti-competitive conduct,[3] and unilateral anti-competitive conduct.[4] These last three are known collectively as 'prohibited practices'.

2.2 The Competition Commission is generally the litigant of choice in proceedings under the Act,[5] including prohibited practice proceedings. However, the Act also makes provision for private enforcement.[6]

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[1] Chapter 3 of the Act.

[2] Section 4 of the Act relates to 'restrictive horizontal practices'.

[3] Section 5 of the Act relates to 'restrictive vertical practices'.

[4] Chapter 2 Part B of the Act.

[5] The Commission is also the decision-maker at first instance in small merger applications and exemption applications. Its other powers include the power to conduct market inquiries.

2.3 The Competition Tribunal is the adjudicative body of first instance in most proceedings under the Act. It is a specialist administrative tribunal with powers prescribed by the Act. The Competition Appeal Court is a specialist court, which hears appeals from, and applications for review of, certain Tribunal decisions.

3 Abuse of a Dominant Position

3.1 The Act prohibits unilateral anti-competitive conduct or 'abuse of a dominant position' in Chapter 2 Part B. This Part includes provisions addressing excessive pricing,[7] refusal of access to essential facilities,[8] and price discrimination.[9] However, it is the general prohibitions of unilateral exclusionary conduct in sections 8(c) and 8(d) which provide the closest analogy to section 46(1) of the CCA.

3.2 Sections 8(c) and 8(d) both prohibit certain 'exclusionary acts' by a dominant firm. Section 8(d) lists five specific types of conduct, which are deemed to constitute exclusionary acts. Section 8(c) concerns a residual category of exclusionary acts beyond those expressly identified.

3.3 Both provisions also require the complainant to prove that the act in question has an 'anti-competitive effect'. Both provisions permit the respondent to raise a defence on the basis that the conduct gives rise to 'technological, efficiency or other pro-competitive gains'. However, there are differences between the

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[6] If a person makes a complaint to the Commission, and the Commission, after investigation, declines to refer a complaint to the Competition Tribunal, that person can refer the complaint to the Tribunal directly: s 51(1). A private party may also bring an action for damages in a civil court upon a declaration by the Tribunal that a respondent has engaged in a prohibited practice: s 65(6).

[7] Section 8(a) follows the EU approach in prohibiting certain 'exploitative' (as opposed to exclusionary) conduct. The few excessive pricing cases to date have involved former state-, or state-sponsored, monopolies.

[8] Section 8(b).

[9] Section 9.

two provisions in respect of onus of proof and applicable penalties, as explained below.

4 Definition of a dominant position

4.1 As in most jurisdictions, the South African provisions only apply to firms that possess[10] a certain degree of market power: in particular, they only apply to 'dominant firms'.[11] This term is defined in section 7 of the Act.

4.2 Section 7 is unusual in that it specifies certain market share thresholds, above and below which statutory presumptions in respect of dominance are established. Thus there is an irrebuttable presumption that a firm with a market share of at least 45 percent is dominant in that market. A firm with a market share between 35 and 45 percent is presumed to be dominant, unless it can prove that it does not, in fact, possess market power. And a firm with a market share less than 35 percent is presumed not to be dominant, unless the complainant can prove that it does, in fact, possess market power.

4.3 'Market power' is defined in section 1(1) of 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'. This definition is literally an amalgam of the definitions of market power in the EU and the US.[12]

4.4 While other jurisdictions sometimes make reference to market share thresholds for dominance in the case law,[13] it is unusual to find such

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[10] Or are deemed to possess.

[11] The abuse of dominance provisions will only apply to dominant firms with South African assets or turnover, to paraphrase, valued at at least ZAR 5 million: section 6; GN 22025, 1 February 2001, as amended by GN 562 in GG 22128, 9 March 2001.

[12] See *United States v EI du Pont de Nemours Co* 351 US 377 (1956) 391-2; *United Brands Company v EC Commission* (C-27/76) [1978] ECR 207, par 65.

[13] See, eg, Alison Jones and Brenda Sufrin, *EU Competition Law: Text, Cases and Materials* (4th ed, Oxford University Press, 2011) 327-9, referring to the rebuttable presumption arising from EU case law that firms with a market share in excess of 50% are dominant; and Herbert Hovenkamp *Federal Antitrust Policy: The Law of Competition and its Practice* (4th ed,

thresholds specified in the legislation. In this respect, it appears that the South African legislature intended to provide firms with greater certainty about whether the abuse of dominance provisions would apply to them.[14]

4.5 This certainty comes at the expense of some accuracy and equity, particularly in respect of the irrebuttable presumption that a market share of at least 45 percent gives rise to market power. Respondents presumed to be dominant in this way may still escape liability if the complainant fails to prove anti-competitive effect, or if the respondent succeeds in an efficiency defence. In practice, most unilateral conduct proceedings have concerned respondents with market shares well in excess of 45 percent, and the Tribunal has generally found that such respondents possess market power based on a broader factual analysis.[15]

5 Specified exclusionary acts: section 8(d)

5.1 Section 8(d) flags five specific types of conduct that are deemed to be exclusionary acts for the purposes of the Act.[16] In this respect, it is similar to the EU and Canadian provisions regarding unilateral conduct, which also specify certain acts that are considered to come within the provisions.[17] Specifying such acts serves to highlight certain behavioural 'danger zones' for dominant firms, but it does not give rise to any per se illegality since plaintiffs are still required to prove the anti-competitive effect of the conduct.

Thomson Reuters, 2011) 293-4, referring to US case law that suggests that market shares in excess of 75% will be sufficient to demonstrate monopoly power (as opposed to the lower market shares necessary in cases of 'attempted monopolization').

[14] Such certainty is, of course, limited by the potential for some of the presumptions to be rebutted, and by the inherent uncertainty of defining a market (and therefore market share).

[15] See, eg, *Competition Commission v South African Airways (Pty) Ltd* 18/CR/Mar01 (market share over 65%); *Competition Commission v British American Tobacco South Africa (Pty) Ltd* 05/CR/Feb05 (market share over 85%); *Competition Commission v Senwes Ltd* 110/CR/Dec06 (market share over 80%).

[16] *Competition Commission v South African Airways (Pty) Ltd* 18/CR/Mar01 pars 101-5.

[17] See Art 102 *Treaty on the Functioning of the European Union*; *Competition Act*, RSC 1985, c C-34, s 78.

5.2 The exclusionary acts specified in section 8(d) can be summarized as:

- exclusive dealing, including inducement not to deal;
- refusal to supply scarce goods to a competitor;
- tying or bundling;
- predatory pricing; and
- buying up scarce resources.

It is convenient to paraphrase the listed acts in this way for present purposes, but it should be remembered that the actual wording of the provisions is much more specific.[18] For example, the predatory pricing provision adopts the wording of the well-known Areeda-Turner test for predatory pricing, even though it is acknowledged that predation may occur outside of these circumstances.

6 Residual exclusionary acts: section 8(c)

6.1 Section 8(c) addresses residual exclusionary conduct. It prohibits any exclusionary act by a dominant firm not listed in section 8(d), which gives rise to an anti-competitive effect that is not offset by any claimed efficiency gains. An 'exclusionary act' is an act that impedes or prevents a firm from entering into, or expanding within, a market.[19] That is, the act in question must be of an exclusionary nature, as opposed to conduct that directly exploits consumers, such as excessive pricing, or managerial slack in statutory monopolies.[20]

6.2 Conduct covered by section 8(c) may include:

- predatory pricing beyond the Areeda-Turner definition;
- non-price predation;
- margin squeezes;[21]
- refusal to supply goods or services to a firm other than a competitor;
- refusal to supply a service to a competitor; and

[18] See the full text of ss 7 and 8 in the Appendix to this submission.

[19] Section 1(1).

[20] See *Competition Commission v South African Airways (Pty) Ltd* 18/CR/Mar01 par 136.

[21] *Competition Commission v Senwes Ltd* 110/CR/Dec06.

- refusal to supply intellectual property rights.

This list is far from exhaustive. Again, the complainant is also required to prove that the exclusionary act had an anti-competitive effect.

6.3 Section 8(c) presents an open-ended category of exclusionary conduct, such that firms have less certainty in determining whether their conduct might fall foul of section 8(c), as compared with section 8(d). The legislature takes account of this fact, both in the difference in the onus of proof under the respective provisions,[22] and in the applicable penalties.[23]

7 Anti-competitive Effect

7.1 While the South African provisions refer to 'abuse of a dominant position', they do not require proof that the dominant firm used, or took advantage, of its market power. Rather, the complainant must show that the dominant firm engaged in exclusionary conduct, which gave rise to an 'anti-competitive effect'. The focus is not on the *means* adopted by the dominant firm, but on the substantive impact of its conduct on the competitive process in the relevant market.

7.2 The Act does not define anti-competitive effect, but the term has been explained in the case law. Three principles can be drawn from the authorities to date:

(a) harm to competitors alone is not sufficient to demonstrate an anti-competitive effect;[24]

(b) proof of actual harm to consumer welfare is sufficient to establish an anti-competitive effect;[25] but

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[22] Under s 8(d), the respondent bears the burden of proving that the claimed efficiency gains outweigh the anti-competitive effect of the conduct. For the broader prohibition in s 8(c), the legal burden remains with the complainant, who must show that the anti-competitive effect of the conduct outweighed any relevant gains in light of the evidence adduced by the respondent.

[23] See par 9 below.

[24] *Msomi v British American Tobacco South Africa (Pty) Ltd* 49/IR/Jul02 par 59.

[25] *Competition Commission v South African Airways (Pty) Ltd* 18/CR/Mar01 par 132.

(c) direct proof of consumer harm is not essential. An anti-competitive effect may be inferred where the exclusionary conduct 'is substantial or significant in terms of its effect in foreclosing the market to rivals'.[26]

7.3 In cases where a contravention of section 8(c) or 8(d) has been established, the necessary effect has generally fallen into this last category. Substantial or significant foreclosure may be found in the absence of total foreclosure of the market. It has even been found to exist where the market shares of rivals did not decrease in the relevant period, on the basis that the dominant firm (with a market share in excess of 60 percent) had impeded the growth of its rivals in the market.[27] But where the duration and extent of foreclosure is limited, and barriers to entry are low, the Tribunal has found that there is no anti-competitive effect.[28]

7.4 The requirement of anti-competitive effect presents no small evidentiary hurdle. In practice, parties to section 8 proceedings have produced extensive economic evidence and analysis in respect of the nature and effects of the conduct in question. Few cases under sections 8(c) and 8(d) have proceeded to a final hearing over the last 15 years, and anti-competitive effect has been proved in only a handful of cases.[29]

7.5 The complainant must show that, on the balance of probabilities, the dominant firm's exclusionary act caused the anti-competitive effect. The Tribunal has shown some inconsistency in its approach to considering potential alternative

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[26] Ibid pars 128-32.

[27] *Nationwide Airlines (Pty) Ltd v South African Airways (Pty) Ltd* 80/CR/Sep06. *Cf Competition Commission v British American Tobacco South Africa (Pty) Ltd* 05/CR/Feb05, in which the Tribunal held that, although the respondent's overwhelmingly dominant position was unlikely to be assailed in the near future, the conduct in question created no significant foreclosure.

[28] In *Mandla-Matla Publishing (Pty) Ltd v Independent Newspapers (Pty) Ltd* 48/CR/Jun04 pars 81-91, where less than 25% of the market was foreclosed for less than four months, the Tribunal found that there was no anti-competitive effect.

[29] See, eg, Simon Roberts, 'Effects-Based Tests for Abuse of Dominance in Practice: The Case of South Africa' (2012) Working Paper 4/2012, Centre for Competition Economics, University of Johannesburg, Table 1, citing eight final hearings on s 8(c) and (d) up to 2012; with five findings of contravention by the Tribunal, one of which was overturned on appeal.

causes of foreclosure,[30] but the general principle is that the complainant must show a causal link between the conduct and the anti-competitive effect.[31]

7.6 While the Act does not specify in which market the anti-competitive effect must occur, the Tribunal has confirmed that a dominant firm may commit an abuse of dominance even though the effect of its exclusionary act occurs in a different market to that in which it was committed.[32] Thus 'monopoly leveraging' is recognized as a potential abuse of dominance.

8 Technological, Efficiency or Other Pro-competitive Gains

8.1 Even if the complainant proves that the dominant firm has engaged in an exclusionary act which has an anti-competitive effect, the dominant firm will avoid liability if it proves that its conduct gave rise to 'technological, efficiency, or other pro-competitive, gains' that outweigh the anti-competitive effect. In this way, the dominant firm can argue that its conduct should be categorized as vigorous competition rather than anti-competitive exclusion.

8.2 The Act does not define 'technological, efficiency, or other pro-competitive, gains'. The wording would appear to encompass gains in allocative, productive and dynamic efficiency, but it seems unlikely that the Tribunal would find that productive efficiency gains, that are not passed on to consumers, are sufficient to outweigh any significant anti-competitive effect.[33]

8.3 The claimed efficiency gains must be directly related to, and dependent upon, the conduct in question, such that the gains could not otherwise be achieved.[34]

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[30] See *Competition Commission v South African Airways (Pty) Ltd* 18/CR/Mar01 pars 238-9; *cf Competition Commission v British American Tobacco South Africa (Pty) Ltd* 05/CR/Feb05 pars 110, 121.

[31] *Competition Commission v British American Tobacco South Africa (Pty) Ltd* 05/CR/Feb05 par 110.

[32] *Competition Commission v South African Airways (Pty) Ltd* 18/CR/Mar01 par 36.

[33] See *South African Raisins (Pty) Ltd v SAD Holdings Ltd* 04/IR/Oct/1999 10.

[34] *Patensie Sitrus Beherend Beperk v Competition Commission* [2003] 2 CPLR 247 (CAC) 265.

If the respondent could achieve the same efficiency gains without engaging in exclusionary conduct, its defence will fail for want of a sufficient connection between the gains and the exclusionary acts.[35]

8.4 The Act requires the Tribunal to weigh the claimed efficiency gains against the anti-competitive effect of the conduct. To date, the limited case law provides few examples of the Tribunal engaging in a fine balancing of efficiency gains against anti-competitive effects. Rather, it has tended to find either that the conduct had an anti-competitive effect and that the claimed gains were relatively trivial or unrelated to the exclusionary conduct,[36] or that the conduct had no anti-competitive effect but was in fact efficient conduct.[37]

9 Penalties

9.1 As noted earlier, the penalty for infringement varies depending on which abuse of dominance provision is contravened. If the dominant firm is found to have engaged in one of the specific acts listed in section 8(d), and the other elements of the contravention are established, the respondent may face an administrative penalty of up to 10 percent of its relevant turnover for a first-time contravention.[38] If, on the other hand, the conduct falls within the more open-ended category of exclusionary acts in section 8(c), the Tribunal may only impose such a penalty for a 'repeat offence'.[39]

9.2 On finding a contravention of either provision, the Tribunal may also impose an interdict (injunction) prohibiting the respondent from engaging in the

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[35] *Patensie Sitrus Beherend Beperk v Competition Commission* [2003] 2 CPLR 247 (CAC) 266; *Competition Commission v South African Airways (Pty) Ltd* 18/CR/Mar01 pars 245-53.

[36] Eg, *Competition Commission v South African Airways (Pty) Ltd* 18/CR/Mar01 par 250.

[37] See, eg, *Mandla-Matla Publishing (Pty) Ltd v Independent Newspapers (Pty) Ltd* 48/CR/Jun04 par 96.

[38] Section 59(1)(a) and (2).

[39] An administrative penalty may only be imposed for a prohibited practice in terms of s 8(c) 'if the conduct is substantially a repeat by the same firm of conduct previously found by the Competition Tribunal to be a prohibited practice': s 59(1)(b).

conduct;[40] declare an agreement void;[41] order the respondent to supply or distribute goods or services to another party;[42] or make an order for divestiture.[43] The Tribunal may also make a declaration that conduct of the respondent is a prohibited practice in terms of the Act, and a private party may rely on this declaration to bring an action to recover damages in a civil court.[44]

10 Conclusion

10.1 South Africa's adoption of an effects-based test for unilateral exclusionary conduct has permitted its competition authorities to take account of detailed economic evidence and analysis to assess the impact of such conduct on the markets in question. To date, this has resulted in relatively few final hearings of claims under sections 8(c) and 8(d), and even fewer successful claims.

10.2 Given that South Africa adopted modern competition legislation only 15 years ago, it is not surprising that there remain aspects of its unilateral conduct provisions that require further interpretation in the case law. However, the inclusion of broad concepts of anti-competitive effect and efficiency gains do provide the courts with an opportunity to adopt an 'economic and effects-based approach' to exclusionary conduct, as increasingly advocated in more mature antitrust jurisdictions.[45]

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[40] Section 58(1)(a)(ii).

[41] Section 58(1)(a)(vi).

[42] Section 58(1)(a)(ii).

[43] That is, an order directing a firm to sell any shares, interest or assets of the firm if it has contravened s 8, and the prohibited practice cannot adequately be remedied in terms of another provision of the Act or is substantially a repeat contravention: s 60(2).

[44] That is, the Magistrate's Court or the High Court: ss 58(1)(a)(v), 65(6)(b).

[45] See, eg, European Commission, 'Antitrust: Consumer Welfare at Heart of Commission Fight Against Abuses by Dominant Undertakings' (Press Release, IP/08/1877, 3 December 2008) <http://europa.eu/rapid/press-release_IP-08-1877_en.htm?locale=en> .

APPENDIX: RELEVANT PROVISIONS OF THE *COMPETITION ACT 1998* (SOUTH AFRICA)

7 **Dominant firms.** – A *firm* is dominant in a market if –

(a) it has at least 45% of that market;

(b) it has at least 35%, but less than 45%, of that market, unless it can show that it does not have *market power*; or

(c) it has less than 35% of that market, but has *market power*.

8 **Abuse of dominance prohibited.** – It is prohibited for a dominant *firm* to –

(a) charge an *excessive price* to the detriment of consumers;

(b) refuse to give a competitor access to an *essential facility* when it is economically feasible to do so;

(c) engage in an *exclusionary act*, other than an act listed in paragraph (d), if the anti-competitive effect of that act outweighs its technological, efficiency, or other pro-competitive gain; or

(d) engage in any of the following *exclusionary acts*, unless the *firm* concerned can show technological, efficiency or other pro-competitive, gains which outweigh the anti-competitive effect of its act:

(i) requiring or inducing a supplier or customer to not deal with a competitor;

(ii) refusing to supply scarce goods to a competitor when supplying those goods is economically feasible;

(iii) selling *goods or services* on condition that the buyer purchases separate *goods or services* unrelated to the object of a contract, or forcing a buyer to accept a condition unrelated to the object of a contract;

(iv) selling *goods or services* below their marginal or average variable cost; or

(v) buying-up a scarce supply of intermediate goods or resources required by a competitor.