BUSINESS HIGH-LEVEL SUBMISSION ON THE COMPETITION AMENDMENT BILL

SPECIAL MEETING OF THE TRADE AND INDUSTRY CHAMBER (TIC)

29 JANUARY 2018

INTRODUCTION

BUSA is committed to the achievement of inclusive growth and therefore supports interventions which will support achievement of this objective. As is the case in all legislation that seeks to constrain free market activity in the public interest, a careful balance needs to be maintained between using Competition Law to achieve public interest objectives and the pursuit of legitimate commercial interests.

Business agrees with the view expressed in the summary of the Bill that "the release of the Bill for public comment can be expected to result in significant public debate on economic concentration and is therefore disappointed that the almost half the time provided for public consultation was in the 2017/2018 holiday period, during which the Business constituency is not at full capacity. Sufficient time was therefore not available to do justice to these important amendments. As will be seen from the comments there are a number of areas in the Bill, which have given rise to significant concerns from Business and which require more detailed engagement to do them justice.

It is also noted "that, once the Bill is approved for public release by Cabinet, an extensive communication exercise would be conducted, led by the Minister and the expert panel". Business is not aware of the process being followed here and would appreciate it if notification of such opportunities could be made available.

In addition, business requests that the Socio-Economic Impact Assessment (SEIAS) conducted on the Bill be shared with Nedlac partners to enable a more comprehensive understanding of some of the effects of the proposed amendments.

Business intends to submit further, detailed comments on the Bill following this initial high-level input and clarification of the way forward, both in terms of the current Nedlac process and the broader public participation process.

GENERAL

There are a number of areas in the Bill, as identified in the detailed comments which require greater clarity:

Concentration

Business noted the presentation by the EDD to Nedlac in which reliance is placed on the HHI Index as a measure of concentration, and 10 sectors of the economy are cited as having high levels of concentration based on that Index. Consultations with members have revealed that they disagree with the results of the calculations included in the presentation in that their application of the HHI methodology to their sector data results in much lower levels of concentration. It would therefore be helpful to better understand the methodology used to arrive at the figures listed in the Bill. As it stands, "market share" can be interpreted in many ways. For example, it could refer to a firm's participation in certain product lines in a market, or its share in a market (e.g. a particular bank's share in the mortgage bond market or its overall share of the banking sector – itself distinct from the financial services sector). Secondly, the measure in itself is not an accurate level of concentration and competitive harm. The process of measuring changes in the HHI index is sometimes used as a filter measure to estimate a lessening of competition, in merger control matters. Reliance on this measure in merger control is also diminishing, across all major antitrust jurisdictions.

In the Background Note preceding the Bill, it is stated that evaluation of concentration requires a skilled and experienced regulator to create an evidence based considered foundation for interventions, and that the amendments recognise that the competition authorities have these skills and experience. It is known that one of the challenges of competition authorities around the globe is the knowledge and understanding of competition regulators and courts of specific markets, and public interest goals across a wide spectrum of industries. It is therefore recognised that it will be challenging for this to be addressed given the wide ambit of the market inquiry provisions. Further clarity on how this will be given effect is required. Furthermore, huge reliance is placed by the Commission on firms / business to assist the Commission with information on specific markets in mergers and enforcement (complaints), however, a new test is introduced to be applied for adverse effects, where the Commission may make unilateral decisions based on reasonable and practicable actions that will be binding.

The significant focus on and magnification of arguments on concentration borders on treating concentration as a problem *per se*, a position which has no sound basis in competition economics, law and policy, as concentrated markets could also be characterised by effective competition and welfare benefits. It is trite in economics and competition law that dominance on its own is not a problem and the Bill itself acknowledges that concentration may also be associated with economic benefits. There is therefore limited economics and policy basis for adopting such an approach. The pointed attempt to target concentration directly and remedying it e.g. through market inquiries may not be appropriate.

Concentration is itself is not a recognised economic malady. The governing test in these enquiries should remain as to whether a situation gives rise to a substantial lessening of competition, which is the benchmark economic enquiry in antitrust matters. The Bill introduces a new and undefined term in the form of "adverse effect on competition". This contemplates a lower standard than that set for other infringements of the Act, but the long-term consequences of a Market Inquiry can be drastic, including divestiture. In addition, here, binding decisions can be made by the Commission, whereas in the case of infringements of Sections 5,8 and 9, only the Tribunal can make a binding decision. The concept should be removed and replaced with the "substantial lessening of competition" concept, which is an accepted international economic benchmark.

The summary of the study does not, in fact, identify relevant markets but rather "average market shares" across broad sectors or industries. This is not in any way indicative of actual concentration levels in relevant markets as assessed in competition law and economic terms.
The study relied upon reflects a snapshot at the time each merger was assessed and as such may not reflect trends in concentration levels over time nor current concentration levels. It therefore does not reflect changes in concentration levels prior to and after the mergers. It is these trends that yield useful information regarding whether concentration has remained the same, increased or decreased. Where concentration levels are reducing over time, the rationale for the proposed amendments is less compelling.

Withdrawal of the Yellow Card Regime

This arises under sections 4(1)(a) (the general category of horizontal practices), 5(1) (the general category of vertical practices), 8(c) (the general category for abuse of dominance) and 9 (price discrimination) of the Act. Currently, an infringement of those sections must give rise to a substantial lessening of competition and can only be the subject of a penalty in the case of repeat conduct of the same conduct. These categories of infringements are generally known as the *non-per se* infringements, in comparison to hard core cartels (section 4(1)(b), minimum resale price maintenance (Section 5(1), and the specified categories of abuse of dominance listed under Section 8(d) of the Act.

There are good reasons for this regime and it is entirely in line with international precedent in other jurisdictions. These sections are broadly drafted to allow the appropriate levels of flexibility for the Tribunal and the Competition Appeal Court to develop appropriate case law over time, as to categories of behaviour which should be regarded as anti-competitive under the Act.

The Bill proposes to do away with this regime. The result is that any infringement of the act, however minor, and however unclear as to whether it falls inside or outside of the Act, falls to be subjected to a penalty for a first-time infringement.

Government's view is that the abolition of this "yellow card" dispensation is aimed at enhancing enforcement of the Act and to ensure greater compliance with it by firms. It is suggested that the "yellow card" dispensation was an appropriate penalty framework at the time of the Act's commencement but, given the greater certainty that has now been developed, it is appropriate to withdraw the "yellow card" at this time.

In business' view, this analysis of the "yellow card" situation is not correct. There are very few cases on the proper interpretation of section 4(1)(a), 5(1), 8(c) or 9. These sections were specifically designed to give the Competition Tribunal (Tribunal) and the Competition Appeal Court the opportunity to develop categories of prohibitions over time and through the development of the case law. At present, there is no "greater certainty" in the interpretation of these provisions, and it is submitted that the withdrawal of the "yellow card" dispensation is not appropriate.

There are several factors in this regard. The world economy and technologies are rapidly changing over time and one cannot prescribe for every situation in legislation. One must allow for flexibility in the introduction of new situations that will allow for fair treatment of parties.
Related to this is the potential chilling effect on innovation. Whilst dominant firms might come with their own sets of problems, in many respects they are highly innovative. The withdrawal of the "yellow card" dispensation and the effective removal of section 8(c) will blunt the innovative qualities of such firms.

The same point applies in relation to section 4(1)(a). The Act, rightly, targets the traditional hard-core cartel offences. At the same time, mutual collaboration between firms is often highly beneficial for the economy, particularly in a developing country such as South Africa, which has limited resources. By withdrawing the "yellow card" dispensation under section 4(1)(a), business is concerned that this will have a serious chilling effect on the establishment of pro-competitive joint venture arrangements and positive collaboration between firms. A focus of the draft Bill is the enhancement of small businesses. It is important that the Act allow for positive and pro-competitive collaboration with and between such small businesses.

Section 8(c) in its current form provides for a useful "catch all" to capture factual situations which are not specified under the Act. The effect of the deletion is that this "catch all" falls away and is replaced by the introduction of the word "including" in section 8(d). The significance of this is that the onus changes and becomes more onerous on respondents, which is also unfair.

Given that there is less legal certainty regarding conduct that is not clearly listed as being problematic (or potentially problematic) and it is therefore more difficult for a firm to assess whether it is possibly acting in contravention of section 8 in respect of unlisted conduct, it is more fair and reasonable to keep the onus in this regard on the Competition Commission in respect of conduct which is not clearly listed in section 8. Business accordingly submits that the existing section 8(c) should not be deleted or amended and that the word "including" which it is proposed be inserted at the end of section 8(d) be deleted.

An area of real concern will be in relation to the creation of joint ventures, which should be fundamental to the development of inclusive growth. Joint ventures between different types of competitors fall to be assessed under section 4(1)(a). So, if two or three competitors get into a joint venture and are adjudicated to fall on the wrong side of the line, under the current system, they would not pay a fine, but could adjust their arrangements to comply with the prohibition. Business is concerned that the change will chill the entrepreneurial instincts of firms to enter into joint ventures at all, and that does not help to grow the economy at all. The same applies to dominant firms such as Google and Microsoft, which are still highly innovative. The withdrawal of 8(c) and its yellow card cover, will discourage lawful innovation for those firms, for fear of picking up a fine for being on the wrong side of the law.

Joint Purchasing Agreements/ Buying clubs

Worldwide, these Joint Purchasing Agreements/ Buying clubs are regarded as being pro-competitive and beneficial to consumers. Section 4(1)(b) still prohibits “agreement on a purchase price” and has had the effect of making such arrangements per se unlawful in South Africa, exposing participants to a fine. If one is engaging in major changes of the Act, this is one critical amendment that should be made, by removing the words “or purchase price”. This does not mean that such an arrangement would be free of scrutiny, but it would just fall to be assessed under the non-per se umbrella of Section 4(1)(a).

This is an issue which has vexed businesses in South Africa since the inception of the Act. On an ordinary interpretation of this section, it means that joint purchasing arrangements or “buyers’ clubs” are per se prohibited under the Act. World-wide, it is recognised that these kinds of arrangements are pro-competitive and should be encouraged. In Europe, for example, where Article 101 is supplemented by binding guidelines, the guidelines on horizontal arrangements set out an effects-based (or “rule-of-reason”) analysis and specifically recognise that horizontal cooperation agreements, such as joint purchasing arrangements can lead to “substantial economic benefits”. This gap in our law should be recognised and the reference to purchase prices should be removed from section 4(1)(b).

On this basis, then, joint purchasing arrangements would fall to be judged under section 4(1)(a) which would still allow non-competitive arrangements to be penalised.

In relation to section 4(1)(a) please also see comment relating to the deletion of section 8(c) below.

Furthermore, business suggests that the drafters should look at amending section 4 of the Act to deal with the characterisation test decisively and to also deal with section 4 (2) the Act, which deals with a presumption of collusion. Business is of the view that section 4(2) has been ineffective and has not been successfully utilised by the competition authorities.

Business submits that there are pro-competitive gains that are derived, especially by small business, when it comes to joint procurement when dealing with big entities. It would be beneficial to entities to not be automatically found guilty when it comes to joint purchasing arrangements. As such arrangements, especially when dealing with international markets, can be pro-competitive for the consumers and the South African economy.

Business therefore propose a deletion of section 4 (2), (3), and (4). In addition, it is suggested that a new section 4 (2) dealing with characterisation be added. This section should be clear that where an agreement between competitors is found to exist and the intentions and outcomes of such agreement when properly characterised, are to the benefit of consumers, then such conduct, properly construed, does not fall within the ambit of the prohibitions in section 4(1). The onus to prove that the conduct does not fall within the ambit of section 4(1) should be with the respondents.

This proposed amendment can also deal with concerns regarding the prohibition in relation to the fixing of a purchase price.

Abuse of Dominance

The dangers of withdrawing the yellow card protection provided by Section 8 (c), have been referred to above. This approach should be reconsidered. Other changes to this Section include the introduction of a number of vague concepts such as "unreasonable condition" and "their relevant cost benchmark". It is not clear what those terms mean, and in the absence of a clear definition or elaboration, the section becomes extremely unfair for firms, given that conduct on the wrong side of the line exposes them to an immediate fine.

Merger Control

Having regard to subsection (3), the intention of the subsection appears to be that the competition authorities would have the power to prohibit the series of transactions that effectively accumulated into a merger? For example, if a firm acquires a non-controlling 15% shareholding in year 1, subsequently increases that shareholding to non-controlling 30% in year 2, and in year 3 to 51% - currently, only the latter would be notifiable as a merger. Currently, if the acquisition of the move from 30% to 51% was prohibited, then the 30% shareholding would continue to be held by the acquiring firm. The proposed amendment implies that if the move from 30% to 51% is prohibited – a firm may have to divest of its entire shareholding in the target firm, including the 30% non-controlling interest, because all three tranches would be one. Any divestment that is required may amount to an unlawful deprivation that does not accord with section 25 of the Constitution of the Republic of South Africa, 1996. Although the "series of transactions" may be regarded as occurring simultaneously for the purposes of a competitive assessment, it cannot be correct in law that a prohibition of the final merger in the series amounts to a prohibition of the entire series, and that divestiture may lawfully be ordered. In terms of section 60(1) of the Principal Act, divestiture in the context of mergers may only be ordered by the Tribunal if a merger is "implemented in contravention of Chapter 3". The possible effect of the proposed amendment is that a firm may be ordered to divest itself of shareholdings acquired lawfully. Wording should be included in the amendment that specifically excludes divestiture as a potential remedy, should the final transaction in the series be prohibited.

Business suggests that a merger should be determined in accordance with the market conditions prevailing at the time when the merger is concluded. The competition authorities should prohibit that one transaction that brings the merger into the competition authorities' scope.

It is in principle unclear what is sought to be safeguarded / regulated through this proposed amendment. There are well-established principles for the meaning of control. Placing non-controlling stakes within the purview of competition authorities' jurisdiction will create difficulties for investors and could serve to discourage or delay investment. The competition authorities should be able to clearly show that the acquisition of a minority shareholding – that would not normally be notifiable – poses a significant threat to competition in the relevant market to be empowered to scrutinise the acquisition.

For regulatory and market certainty, it is critical that a separate amendment be included to spell out in detail the process to be followed in engaging with the EDD, where the Minister has indicated that he wishes to participate in a particular merger. The process for assessment by the Commission is clearly set out in the Act, but the Act is completely silent on the processes for engagement with the EDD. There is no indication as to how long the EDD should have to assess the merger, how they should be engaged, and the status of their views when compared to the Commission, which also has independent powers to conduct public interest assessments. At present, this is entirely opaque to anyone involved in the merger process. Mergers are time sensitive, and Business strongly advocates that this situation be addressed in the Bill, to avoid unnecessary delays and arbitrage arising between the two regulatory agencies.

Market Inquiries

The Bill makes extensive amendments to the provisions of the Act dealing with Market Inquiries, with a particular focus of reducing issues of concentration in the South African economy.

Business is of the view that caution should be applied in the Commission using Market Inquiries as a back door to addressing situations they cannot effectively prosecute under Sections 5, 8 and 9, which appears to be the intention. Market Inquiries are very expensive and time consuming. Considerable extra resources and funding will need to be provided to the Commission to carry out this expanded role

Regarding the proposed changes to the market inquiry regime, a reasonable and objective jurisdictional threshold should be present before any such investigation is triggered.

Business welcomes the deletion of the complex monopoly provisions as these were, in business' view, unworkable as they may outlaw legitimate parallel conduct of market participants who have no ability to prevent falling foul of these provisions.

Regarding the consideration of mergers, the Bill proposes that when deciding whether a merger can be justified on public interest grounds, the Competition Authorities must consider the effects that the merger will have on the ability of small firms controlled or owned by historically disadvantaged individuals (HDIs) to effectively enter into, participate and expand within the market. However, clarity is required on how the Bill will promote broader public interest factors in merger analysis whilst balancing the primary purpose of competition law policy. Clarity is required on the substantive provisions on the public interest goals, considering that they have far-reaching impact, especially in respect of market inquiries.

<u>Need to address anti-competitive price discrimination</u>

Business appreciates and supports the Minister's objective behind the proposed amendments to this section to address the effects of anti-competitive price discrimination on Small, Medium and Micro Enterprises (SMMEs) and firms controlled by historically disadvantaged individuals (HDIs). However, the drastic shift in onus from the complainant to the respondent firm to show that differential pricing (as contemplated in sections 9(1)(b) and 9(1)(c)) "is not likely to have the effect of preventing or lessening competition" is extremely onerous. It is respectfully submitted that the shift in onus opens the door for potentially unsubstantiated, spurious and vexatious complaints against respondent firms, in circumstances where they do not have the wide-ranging investigative powers afforded to the Commission – including those aimed at gathering confidential market and firm-specific information from third parties. The incidence of price differences in the economy is vast and the proposed amendments are likely to give rise to an abuse of the section 9 process. Business' concerns are compounded by the move away from the existing test of establishing that the price discrimination is "likely to have the effect of substantially preventing or lessening competition" which is particularly onerous in circumstances where a contravention will now attract a penalty for a first-time offence.

<u>Role of the Minister</u>

With respect to the participation of the Minister in competition instruments and procedures, greater clarity and specifics are required to understand precisely how far this participation would apply.

Business is of the view that the scope of the Minister's involvement should continue to be limited to making representations on public interest grounds. To do otherwise, is to elevate the Minister to a quasi-competition regulator alongside the Commission, which undermines the independence of the Regulator.

Business proposes that the Minster may only lodge an appeal if he/she was a party to the original proceedings. As he/she would have no locus standi if they were not party to the original proceedings. Allowing appeals by the Commission and/or the Minister may lead to a lack of commercial certainty for merging parties – i.e. they could be caught up in litigation long after a merger is commercially viable, or a long-stop date expires. This may result in a constructive prohibition and a disincentive to invest by foreign (and, for that matter, local) buyers – especially in high-profile large mergers which already take significant time to be approved. If the section, as presented in the Draft Bill is maintained, the only feasible discipline could be the inclusion of cost orders for unsuccessful appeals by the Commission and/or the Minister.