
CHAIRPERSON: ...ladies and gentlemen, just before we start, a reminder about cell phones, please if we could all switch them off, not to put them on silent, they still interfere with the recording mechanism and then before we proceed we will have Standard Bank today to give us a presentation on amongst others, the issues, the legal issues which we asked them to look at and in that vein I would like to welcome Mr. Sinton together with the team which consists of Halvar Mathiesen, Barry Fergus, Donn Engelbrecht, James Hodge and lastly Jean Meijer. Thank you, you know we gave you so much work the last time you were here.

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MS NYASULU: Did we?

CHAIRPERSON: Thank you, Mr. Sinton?

MR SINTON: Thank you Mr. Chairman.

CHAIRPERSON: You are on the floor.

20 MR SINTON: Thank you, may I say that the..., we thought the easiest way to proceed today Mr. Chairman if it suits you, we would start with addressing the legal issues which you asked us particularly to raise at the last occasion.

*Pretoria
05 June 2007*

CHAIRPERSON: Right.

MR SINTON: Because..., and then we will proceed from there into the questioning which you wanted to have about the acquiring and issuing aspects of our submission.

CHAIRPERSON: Okay.

10 MR SINTON: And we did, I think there was time set aside for Diners Club to be present to do a presentation and they have requested a postponement of that. We still have not talked to but they were not happy today, just to let you know that if you would like to have a discussion about the three party model with us, we are quite happy to have that discussion with you. We just cannot talk about Diners in particular.

CHAIRPERSON: Okay that is fine. I think I did get a message that Diners Club will not be in a position to do their presentation today so I think the Enquiry Manager's communication with Diners to try and arrange another suitable date for everybody.

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MR SINTON: That is our understanding Mr. Chairman, thank you.

*Pretoria
05 June 2007*

MS MEIJER: This is a quite a lengthy presentation that covers quite a lot of material so that if you think it would be useful from your perspective to ask questions as we go along, please feel free to do that.

CHAIRPERSON: Okay.

MS MEIJER: Before I get into the detail of the presentation, I want to run through the basic principals of our Competition Act and the basic provisions that would govern *per se*..... the *per se* provision on price fixing, just in order to put in context the comparative law that we will look at. As you know the Competition Act is intended to promote and maintain competition and that is for the purposes of promoting the efficiency adaptability and development of our economy. It would clearly be contrary to the purposes of our Competition Act to prohibit conduct or mergers as the case may be that in fact has an efficiency enhancing or a pro competitive effect.

20 We believe that the very broader interpretation that has been given to Section 4(1)(b) and we will run you through that, in fact has that effect and has impacted on all kinds of ordinary arrangements between competitors which in fact are efficiency enhancing

Pretoria
05 June 2007

or pro competitive. And as we go through the foreign case law, you will see that many arrangements that would be prohibited under South African competition law, would in fact be allowed under that foreign law either in the first instance or by way of an exemption. And we do believe that there is scope to interpret our Competition Act in a manner which is consistent both with its purposes and also with the way in which these kind of matters are treated internationally. That is not to say that we suggest that as South Africa should slavishly follow the approach of any other jurisdiction but there certainly is, I think, some learning to be gained from the approach that has been taken.

The presentation is essentially divided into three sections. The first where we look at the South African approach that has been taken so far and secondly we look at the Comparative Law and there we have looked at the United States because that was really the origin of the *per se* provision. We were specifically requested to address you on Canada and Australia and we will do that and finally we look at the European Union.

Pretoria
05 June 2007

And then we go on to propose an approach which you as a panel can take to Section 4(1)(b) and we discussed the implications of that approach for the setting of inter bank fees like interchange fees. So very briefly and I will not go into the any detail because I know that this has been discussed in various presentations but our Section 4 of the Competition Act, prohibits agreements between competitors in two circumstances.

10 The first, and this is generally referred to as the rule of reason, is where the agreement is shown to substantially prevent or lessen competition and it is not shown to produce any efficiency or other pro competitive gains that outweighed that anticompetitive effect. So that is the rule of reason analyses and the second is what is generally referred to as the *per se* provision and it is the provision of price fixing, division of markets and collusive tendering.

20 I think it is important to highlight that just because an arrangement does not fall under the *per se* provision that does not mean that it escapes scrutiny, under the Competition Act. It would still fall to be analysed as an agreement between

Pretoria
05 June 2007

competitors under Section 4(1)(a). So that it would still be considered and could still potentially be prohibited.

The approach that is of concern to us with regard to Section 4 is and in particular with regard to Section 4(1)(b) is that the competition authorities have tended to take the view that all you have to prove in order to succeed in a complaint under Section 4, is that there is an agreement that it is between competitors or potential competitors and that it is an agreement as to a purchase or selling price.

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And if as a complainant you could produce an agreement which contains those three elements, you will succeed under Section 4(1)(b) and it is that that we really want to challenge through this presentation.

CHAIRPERSON: But is it not, do you say that we can ask questions?

MS MEIJER: Sorry?

CHAIRPERSON: Did you say we can ask questions as we are...

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MS MEIJER: Yes please.

Pretoria
05 June 2007

CHAIRPERSON: Yes is that not based on the interpretation of the section basically because it is only 1(a) which has got all the other provisions.

MS MEIJER: That is correct and we do not suggest that you should approach Section 4(1)(b) in the same way as Section 4(1)(a) but what we do say is that these terms price fixing dividing markets and collusive tendering have a particular meaning, a particular meaning which is restrictive of competition and that they could not have been intended and to have prohibited pro competitive or efficiency enhancing arrangement. So we therefore say that you need to take an approach to this section which ensures that it only impacts on those types of arrangements that was intended to prohibit.

CHAIRPERSON: But you are not going to find an agreement which says “we are now price fixing.”

MS MEIJER: No, but I think what you will find and it has occurred in South Africa is that there are some arrangements which plainly have no justification and a number of those arrangements have in fact been reported to the Competition Commission in term of the Corporate Leniency Policy and those firms who have no explanation for

*Pretoria
05 June 2007*

what they do have been very quick to settle. So we are not saying that the *per se* provision should not apply to the kind of conduct that it is intended to apply to.

We are just saying that the net in South Africa has been cast too wide and I will give an example in a minute of the kind of arrangement that I think is impacted by this interpretation and I think you will agree with me that it ought not to be.

ADV PETERSEN: Sorry to interrupt, when you say the “net has been cast too wide,” are you referring to the pre-Supreme Court of Appeal decision and ANSAC or you are including the Supreme Court of Appeal decision in your comment that the net has been cast too wide.

MS MEIJER: I think that the Supreme Court of Appeal gives us a glimmer of hope in terms of suggesting although not enforcing an approach that would be consistent with the purposes of the Act. So I will run through what I think that decision means for this Enquiry. Just before talking about examples of conduct that I think are impacted by the approach which has been taken certainly by the Commission, the Tribunal and the Competition Appeal Court to Section 4.

Pretoria
05 June 2007

It is important to remember the very narrowness of our exemption provisions and I am not going to run through each of them but there are extremely narrow grounds on which you can secure exemption in South Africa. It is not sufficient to say that a particular practice is in the public interest and therefore ought to be permitted. You have got to promote one of these very specific objectives. So turning then to the examples that I would likely you to think about, take for instance three bead workers who are making necklaces at the Durban Beach Front and a tourist approaches them one day and says you know and in fact they are competitors, the tourist approaches one of them and says “if you sold these beads at the Rosebank Market, you are selling them here for R50.00, you could get a R100.00 at the Rosebank Market.”

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And the woman sits and thinks about it and she talks to the woman who sell beads on either side of her and says “you know would it not be a good thing if we could get to Johannesburg and sell our beads,” and the one woman says “well I would never think of going to Johannesburg, I was mugged the last time I went there and I am not going back anytime soon.” The other says “I have got a child starting school, it is not a good time for me” but the third says “well I would be prepared to do it and if you

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*Pretoria
05 June 2007*

share my taxi fare which is a R130.00 each way, I will go up and see if I can sell the beads.”

And they agree that she will sell their necklaces for R80.00 each, irrespective of which of those woman made the necklace and she sets off to Johannesburg and on her first day at the Rosebank Market, she sells a 100 necklaces for R80.00 and that is more than all three of them would have sold in a week at the Durban Beach Front.

10 Now let us think about that arrangement. Intuitively I would say that that is a positive agreement. It is not something which strikes you intuitively as anticompetitive but if you analyse it, it is an agreement, it is between competitors. These three women do compete with each other selling their beads at the Durban Beach Front and it sets a price at which they will sell their products and technically it is *per se* prohibited under the Competition Act. Fortunately for those women that would be an arrangement that would probably qualify for exemption because they would be able to argue that it promoted the ability of small businesses, to become

20 competitive so they might escape scrutiny under the Act but let me give you a second example...

Pretoria
05 June 2007

ADV PETERSEN: But excuse me Ms Meijer. Maybe before you go to your next example and for purposes of this let us leave aside the exemption section, Section 10. Would the example of the bead makers and bead service not fall into the category of an economically integrated joint venture for purposes of serving the Rosebank Market? So that for that market and for purposes of that venture it could be considered a partnership and therefore a single firm, would that approach not take care of the dilemma that is raised by your example?

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MS MEIJER: I think it would take care of the dilemma and that is the kind of approach that we want to suggest is taken but bear in mind that in the ANSAC case, ANSAC is a fully integrated joint venture based in the US and it like the bead makers, sells through that joint venture at a single price into the South African market. And on the approach taken by the Commission, the Tribunal and the Competition Appeal Court, no evidence with regard to that joint venture and the nature purpose and effect of it was going to be permitted to be lead up until the ANSAC case.

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*Pretoria
05 June 2007*

So I think that what you posit Mr. Petersen is precisely where we would like to go, which is to say that if an arrangement is a joint arrangement which is likely to produce efficiency and which does not have as its sole purpose, the fixing of a price. It is not something that should fall within the ambit of Section 4(1)(b).

CHAIRPERSON: Are you suggesting a legislative amendment?

MS MEIJER: No I am suggesting that there is scope...

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CHAIRPERSON: For...

MS MEIJER: There is scope upon interpretation...

CHAIRPERSON: Interpretation...

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MS MEIJER: And in fact I am suggesting that this panel has significantly more freedom than might otherwise be the case because in fact no body in South Africa has yet determined the scope of the prohibition. So that you are free to take your own view unfettered by precedent set by any other of the bodies that govern competition law.

*Pretoria
05 June 2007*

CHAIRPERSON: I am raising this question in the conduct for the fact that the..., in the ANSAC case there is actually a legislative exemption for them to form this type of a joint venture?

MS MEIJER: In the US yes...

CHAIRPERSON: In the US in terms of the Sherman Act that is why I am asking you whether you are suggesting a legislative intervention in that regard.

10 MS MEIJER: No I believe that it is possible in South Africa to deal with this. If the appropriate approach is taken to Section 4, I believe that it is possible to deal with examples like ANSAC without saying how I think that or what I think the outcome would be in relation with ANSAC.

MR BODIBE: Thank you, good morning. Now in your example of beads, the question that I will ask is this..., are they the only suppliers at Rosebank or do they face competition from other suppliers?

20 MS MEIJER: There are not..., in my example numerous other people who sell beads at Rosebank, I think the reason that I was raising it is that in the approach that has

been taken by the competition authorities and I leave aside what was said in the ANSAC decision. And the approach taken by the competition authorities there would be no scope to introduce that evidence. There would be or all the complainant would have to prove that there was an agreement that was between competitors and that it fixed a price. So surrounding factors like who else was in the market, how small their market share was, would not be relevant to the inquiry and what I want to suggest is an approach that at a high level takes these factors into account but without blurring the distinction between Section 4(1)(a) and Section 4(1)(b).

MR BODIBE: So in this context therefore, if we had to analyse the relevant market, the Rosebank Market would be the relevant market and in that context you are saying therefore they should be regarded as a single entity. Is that the implication?

MS MEIJER: I am not sure that it would be correct to view them as a single entity but you would view them as competitors who had come together for an arguably efficiency producing, in order to save transport cost of each them traveling, pro competitive purpose in that there would now be one new competitor at the Rosebank Market. So that would be the way in which that kind of an arrangement would be

*Pretoria
05 June 2007*

approached and approached in that way, you would..., if you were permitted in terms of Section 4(1)(b) to lead evidence that demonstrated that we would say that that evidence would remove you from the ambit of Section 4(1)(b) because it would immediately be obvious that that is not the kind of naked restraint that ought to be *per se* prohibited without any consideration of its nature, purpose and effect.

MR BODIBE: Thank you.

10 ADV PETERSEN: Sorry I just need to, if I may to pursue this question with you because it may then simplify the rest of the analyses that we have to make. Let us go to the comparative jurisprudence for a minute. Now I know that the Sherman Act in the United States, Section 1 is not written in the same way as our Section 4 or any other section but nevertheless some of the guiding principles in the approach to *per se* prohibitions simply arise from common sense and from the notion of reasonableness and it is only in that context that I seek to raise a comparative example but let us take the recent case of Dagher, it is D A G H E R which involved
20 the Shell Oil Company and I think it was Texaco if I am not mistaken.

Pretoria
05 June 2007

Now Shell and Texaco had for purposes of petrol sales, gasoline sales in a certain part of the United States combined their activities and the joint venture then sold its gasoline in that area under the two distinct brand names and charged a uniform price and that was challenged as prohibited price fixing. Now when it..., I think the case was thrown out in the District Court.

10 When it got to the Court of Appeals in the non circuit, the bench divided three to one, two to one, I beg your pardon with a majority holding that it was a case of the joint venture going too far in fixing the terms of its business and declared it prohibited. It then went to the United States Supreme Court where a unanimous bench reversed the non circuit and concluded that because it was a fully integrated joint venture for purposes of that market, all that was being done is that the joint venture was setting its own price as a firm, to use my language rather than theirs, setting its own price as an integrated firm to the public but continuing to use two brand names for that purpose, held that that was perfectly legitimate and could not be treated as a case of

20 price fixing by competitors.

*Pretoria
05 June 2007*

10 So really I am..., what I am wanting to focus on here with reference to your example of the bead sellers, is whether the whole thing is not simply disposed of by a proper analyses of what it is that is going on there. That for purposes of the Rosebank Market have they not joined forces to create a single firm which is you know in the Competition Act is defined so as to include a partnership and to the extend that it is fully integrated for purposes of that market of its operations in that market, would we not have simply a case of that firm, of that integrated joint venture simply unilaterally setting its price for that market. So that Section 4(1)(b) simply does not..., Section 4 simply does not arise?

20 MS MEIJER: I think that that is the right approach but I also think that there are arrangements which would not constitute a full integration which also should fall outside of the net and I mean I can come back to that if you would like me to. I think the..., what I would like to impress upon you is that practices which take place in a market can either be anticompetitive or they can be efficiency enhancing or pro competitive and this is the case when one analyses restrictive practices as well as when one analyses mergers.

*Pretoria
05 June 2007*

And competition authorities in regulating a market would strive to want to avoid two types of errors at a very fundamental level and I am going to use a statistical term but it is one that has become fairly widely used. The first would be to make a type one error where they prohibit an efficiency enhancing or a pro competitive practice and in a sense has an analogy that would be like convicting an innocent person and sending him to jail.

10 They would also want to avoid a type two error which is equally important which is allowing an anticompetitive practice to slip through the net and that would be like letting the murderer go free. So both of those are errors which they would want to avoid and I think that there is always a trade-off in trying to reduce the possibilities of different errors.

20 So that if I give you an example in the legal context, if you increase the onus of proof to instead of being a balance of probabilities you increase the onus of proof to beyond a reasonable doubt, then you run a greater risk that guilty people might walk free but at the same time you are lessening the risk that innocent people will be convicted.

Now we say that both, in other words the type one error avoiding the type one error

*Pretoria
05 June 2007*

which is catching in the net something that ought not to be caught in the net is just as important as avoiding the type two error from a competition regulation perspective.

In other words the consequences for the market of allowing or of prohibiting a pro competitive arrangement can be just as serious as allowing an anticompetitive arrangement. So we would say that *per se* prohibitions should only apply in circumstances where there is a negligible or almost zero possibility that you will make a type one error. In other words that you will by applying the *per se* prohibition catch in the net something that ought not to be caught in the net. Very briefly going to the ANSAC case...

CHAIRPERSON: Before you get there, are you going to address us on the issue of the onus and the difference on the onus in both Section 41(a) and 4(1)(b) because there is argument to say the issue is more about the onus as to who is supposed to prove what.

MS MEIJER: Well I mean the onus of proof in both is proof on a balance of probabilities but in Section 4(1)(b) is obviously the preferable section for a competition authority to use because if it can prove the appropriate elements and

*Pretoria
05 June 2007*

obviously there is a difference in view as to what those should be but if it can prove the appropriate elements of price fixing it then secures a conviction.

The onus of proof on the competition authority under Section 4(1)(a) is very substantially higher because it first has to proof not just the lessening of the competition but a substantial lessening of competition and then the respondent has the opportunity to lead evidence of pro competitive gains or efficiencies.

- 10 So the onus under Section 4(1)(b) is much higher and if a competition authority can proceed under that section, it would obviously choose to do so as opposed to proceeding under Section 41(a) but because of the fact that the onus on the authority is lower, it would be much easier for it to catch in the net arrangements which ought not to be caught in the net.

CHAIRPERSON: Is that the main issue really?

MS MEIJER: That is the main issue...

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CHAIRPERSON: That is the main issue. The onus on 1(b) is lower on the competition authorities if you compare that with 4(1)(a).

MS MEIJER: And that is correct and it should be lower in relation to cartels, in relation to price fixing arrangements in the sort of proverbial “smoke filled room,” and the authorities should not bear a high onus. If parties have fixed a price and they can offer no explanation for why they did it, the competition authorities ought to be able to convict them there and then but what we are arguing in the context of for example interchange fees, is that that you know that those kind of arrangements which arguably if they have enormous efficiency gains or not to be summarily *per se* prohibited under Section 4(1)(b) but should rather because of the fact that they are quite possibly demonstrate and we say do demonstrate efficiencies and are in fact pro competitive because of the network effects they achieve.

That they ought to be subjected to the rule of reason analysis and the authority should have a far higher onus of proof in prohibiting those kind of arrangements than they would, you know an arrangement which did not demonstrate those kinds of efficiency benefits.

CHAIRPERSON: Okay you may proceed with your argument.

MS MEIJER: So I am not going to really talk about the facts and ANSAC but simply to explain how the appeal before the Supreme Court of Appeal came to be because it was not an appeal in relation to our finding of fact. What had happened is that Botash who is essentially ANSAC's only competitor had alleged that ANSAC was fixing prices for soda ash and the South African market and ANSAC said "if you let me lead evidence as to the nature, purpose and effect of what I do, I will show you that I..., this is a fully integrated joint venture and this is not an arrangement which is
10 anticompetitive and it is not the kind of arrangement that ought to be caught in the net of Section 4(1)(b)."

And there was a hearing to decide whether or not that evidence should be permitted and that is the type of evidence I think Mr. Bodibe that you were referring to, and the Tribunal and the Competition Appeal Court both said that no evidence as to the nature, purpose and effect is permissible and having shown that there is not an agreement between competitors that fixes the price, the competition authority has
20 done its work and it was that that was appealed to the Supreme Court of Appeal.

*Pretoria
05 June 2007*

And the Supreme Court of Appeal set aside a decision, saying that it had been premature and they said that firstly the Tribunal needs to determine the scope of Section 4(1)(b) and as I have said to you earlier, there has been no determination as to what its scope is and it is only then that it can move to an inquiry as to what conduct falls within the scope of that prohibition and the evidence that will be permitted, depends on what the scope of the prohibition is.

10 And the Supreme Court of Appeal said that it was by no means self-evident to it what the scope of the prohibition was intended to be. And I will take you through it just in two slides. It is a sort of key reasoning in the Supreme Court of Appeal decision as I saw it. The first was that they, the Supreme Court of Appeal conceded that price fixing does involve collusive or consensual price determination by competitors and that ought to be *per se* prohibited but it does not necessarily follow that price fixing has occurred whenever there is an arrangement between competitors that has the consequence that their goods reach the market at a uniform price. And they say “the

20 concept of price fixing may for example be limited to collusive conduct by competitors that is designed that has the purpose of avoiding competition as opposed to conduct that merely happens to have that effect.”

Pretoria
05 June 2007

ADV PETERSEN: Ms Meijer if you are in a position to do so, could you just give us the page references to the judgement each time you quote it.

MS MEIJER: Yes I will do.

CHAIRPERSON: Actually the judgement has got paragraphs. It might even be easier to refer to the paragraph.

10 MS MEIJER: I will refer to the paragraphs because I think there is..., this was refer to in paragraph 43, oh sorry 40...., 56 of the judgment.

CHAIRPERSON: 56 deals with admissibility of evidence. I think you are correct first when you said 48.

MS MEIJER: Okay...

20 CHAIRPERSON: "Price fixing necessarily contemplates collusion in some form between the competitors for the supply into the market of the respective goods within the design and in the competition."

MS MEIJER: Yes, sorry paragraph...

CHAIRPERSON: Yes it is 48.

MS MEIJER: 48.

MR SINTON: Sorry Mr. Chairman I might mention that in our written submission on card interchange fees much of this is quite at length and reference are there as well.

CHAIRPERSON: The references are there.

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ADV PETERSEN: Yes but to save a lot of back warding and forwarding between documents, could we just make sure, I am interested in particular in the phrase as supposed to conduct that merely has that incidental effect. I am not seeing that...

MS MEIJER: Oh...

ADV PETERSEN: Unless I am missing it.

MS MEIJER: Where is that...?

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ADV PETERSEN: In 48..., yes it is 49.

MS MEIJER: It is 49.

ADV PETERSEN: I think, yes.

MS MEIJER: Yes it is 49. I am sorry I had not actually prepared all of the notes of the references so that in some cases it might be easier if I can give them to you now, I will do so but otherwise afterwards.

ADV PETERSEN: That is fine, may I ask you in relation to that statement, and this goes wider than interchange but it may save time if you are able to deal with it now.

10 Would I be right in reading that, it says “the concept of price fixing both in the lay language and in the language that the Act uses, may for example,” as..., and you have got those words, “be limited to collusive conduct by competitors that is designed to avoid competition as opposed to conduct at merely has that incidentally effect.” If one envisages the hypothetical market situation where there are relatively few players, what might be termed an oligopoly or an oligopolistic market and the players instead of vigorously competing with each other, each individually decides that the better approach is to cautiously shadow each other but they never actually

20 collude. Sorry it is unilateral market behaviour without actual agreement or

*Pretoria
05 June 2007*

collusion. Would that amount to a concerted practice in your view under our Act as properly construed?

MS MEIJER: I think that there would have to be..., you would have to demonstrate that there was at least an understanding between them that they would all do that. It would not be sufficient that they had observed the market and considered it that each individually come to their own conclusion that it might be in their best interest to pursue that course of action.

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ADV PETERSEN: Thanks.

MS MEIJER: And what the Supreme Court of Appeal I think has signaled in its decision is that indirect price fixing of the kind that we have discussed and the bead maker example and in the construction company example that these present far greater complexity and I would argue that interchange falls into that kind of a category and that, you know, that these are all arrangements which serve a legitimate business purpose and that the fact that they may have the literal result or the result of literally fixing a price, does not bring them within the ambit of the *per se* prohibition.

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Pretoria
05 June 2007

So I think as I have said earlier that ANSAC suggests a possible approach to Section 4(1)(b) that would be workable and that would potentially avoid the making of the type one error or the catching in the net arrangements that ought not to be but this has yet to go back to the Tribunal and the Tribunal has yet to decide. So for the time being we have no decision as to what the scope of the section should be which is why I think that this kind of engagement is important.

10 Turning then to the comparative law and as Mr. Petersen has said earlier, the Sherman Act has a very broad prohibition on restraints of trade and in fact read literally it could be read to prohibit any contract because in theory every contract constitutes a restraint of some kind on the parties who engaged in that and for that reason the courts in the US have developed an approach which says that all that is meant to be prohibited is an unreasonable restraint of trade and they have further developed that and to say that in approaching this they are..., as a general principal the Sherman Act would be approached on a rule of reason basis but that there maybe

20 particular instances where conduct is *per se* prohibited because experience of the..., of the courts has shown that that kind of conduct almost never produces an efficiency enhancing or pro competitive outcome. And there certainly have been arrangements

Pretoria
05 June 2007

that have been *per se* prohibited in the US but in line with the approach that I think our Supreme Court of Appeal has suggested and in line with the approach that we propose, where agreements that set prices do not create naked restraints but ancillary to the main purpose of an agreement which quite conceivably produces efficiencies or pro competitive outcomes.

10 Then that..., the *per se* prohibition in the US is not mechanistically applied and those of kinds of arrangements are then subjected to a more searching rule of reason analyses to determine whether they ought to be prohibited or not.

MR BODIBE: Sorry, may I ask a question on your previous slide on bullet 3 can you give an example of those types of agreements that really produce pro competitive outcomes?

20 MS MEIJER: Well I think a normal, you know what we would all consider to be a cartel where three competitors have a weekly conference call to discuss how much they are going to produce and what they are going to charge for it, that is an arrangement which I think on any account of the world would be extremely difficult to justify and I think it is for that reason that in the cartel cases that have occurred in

*Pretoria
05 June 2007*

South Africa under the Corporate Leniency Policy, the firms involved have been extremely quick to settle and to pay their fines because they in fact do not, you know those kind of arrangements are the most egregious contraventions of the Competition Act and ought to be *per se* prohibited.

10 ADV PETERSEN: Just before you develop this, could I pursue or just raise with you and now deal with it whenever it suits you to do so, your presentation. The difficulties that I have in understanding the Supreme Court of Appeal's judgement in ANSAC, incidentally and it makes no difference to the merits of your argument but you were previously acting for ANSAC, is that still the case?

MS MEIJER: Yes.

20 ADV PETERSEN: Now the Sherman Act, Section 1 which you have covered, was so broadly worded that the courts could develop their own logical way based on experience of breaking down the problem of arrangements between competitors. Our Act has not been written in that way, you will be very familiar with the book on European Competition Law by Richard Wish. I have a copy of some pages from the 5th Edition in front of me. On page 112 where he is dealing with Article 81(1) of the

Pretoria
05 June 2007

European Treaty, he explains that the structure of that statutory provision can conveniently be thought of as dividing situations into two boxes and the one box is labeled “the object or purpose box” and the other box is labeled “the effects box.” So that a kind of primary classification goes on from a practical point of view and an agreement would fall into the object box if it has as its object the restriction of competition and an agreement would fall into the effects box if it has as its effect the restriction of competition and because the Treaty, I do not have the page open in front of me, Article 81(1) of the Treaty refers to agreements which have either as their purpose or effect the restriction of competition.

MS MEIJER: I put the provision now...

ADV PETERSEN: Whichever is the object or effect the prevention restriction or the distortion of competition and by the way that applies vertically as well as horizontally, is that right? He..., I understand him to explain and the European cases that I have been able to look at seemed to bear this out that your starting point is to say “what is the purpose of this agreement.” If it is to restrict competition then we do not need to go further and look at its effects because that is a much more complicated

*Pretoria
05 June 2007*

task. Now when one looks at the structure of our Section 4, it does rather look as though there is an “effects box.” This is the issue that I am trying to focus on with you. Section 4(1)(a) would prohibit an agreement between parties in a horizontal relationship or concerted practice. If the agreement has the effect of substantially preventing or lessening competition in the market unless a party to the agreement, I skipped some words, can prove that any technological efficiency or other pro competitive gain resulting from it outweighs that effect. So there is a balancing of effects that goes on in the test provided by Section 4(1)(a)...agreement ought to be considered but not in a case brought under 4(1)(a), in a case brought under 4(1)(b). Now when I read this Supreme Court of Appeal’s decision in ANSAC, I do not find clarity on this issue because in certain of the expressions there, it seems to open the door to an evaluation of effects even when you are undertaking the limited task of characterising the agreement for purposes of Section 4(1)(b). Is that not an open door into 4(1)(a) so that in fact it destroys the legislative distinction or boxes that have been created by the legislature in writing Section 4(1) and linked to that question, is the question whether in characterising as Bloemfontein has told us we have to do, in terms of characterising an agreement to see whether a *per se* prohibition applies to it

Pretoria
05 June 2007

under 4(1)(b). The question is, ought we not really to be concentrating on the purpose of the agreement there? In other words is this not..., is Section 4 not in substance, the setting up of two boxes along the lines that Richard Wish explained in the case of the European example?

MS MEIJER: I think that maybe one approach, I do not think that it is correct to say that ANSAC argued that all of the effects ought to be taken into account. The ANSAC position was to say, if you read Section 4(1)(b) you will see that there is various phrases in that section which suggest a type of conduct that is prohibited. It is restrictive conduct, it is conduct that fixes and fixes has certain connotations that are different to setting or agreeing you know dividing, collusive but that section is directed at that kind of conduct which is considered to be the most serious, you know contravention of competition legislation and that in fact attacks the central nervous system of an economy.

Now ANSAC said “you need to permit sufficient evidence of the nature, purpose and effect of this arrangement. You need to permit at a high level, some evidence of that, in order to decide whether this is conduct which falls within that category of the most

*Pretoria
05 June 2007*

serious kind of conduct which on the face of it almost never has a beneficial effect and should therefore be dealt with in this manner of without hearing any evidence really just prohibiting it or whether this limited evidence on nature, purpose and effect and ANSAC obviously believes that if you look at that limited evidence that you would see that in fact its arrangement should not be characterised as that worst kind of competition contravention but as to whether the Supreme Court of Appeal is anticipating our consideration and whether we should consider both object and effect is I think it is not something which is clear.

And I think almost because it is not clear, there is the freedom to look at nature object and effect at a higher level in order to decide whether the conduct is of the character that should be prohibited and courts over the time will have to decide in South Africa what level of evidence they will permit. Certainly we are not suggesting that it should be a full rule of reason analysis. It should be relatively high level evidence which shows that the parties intended that their arrangement should have a legitimate business purpose and that just showing that it was intended to have the legitimate business purpose and that that purpose maybe an efficiency enhancing, maybe adequate to get a party out of Section 4(1)(b).

*Pretoria
05 June 2007*

CHAIRPERSON: There is something which also bothers me about the ANSAC judgement. You made reference to paragraph 49 which is informed by if you read it. It is informed, those comments which were made, were informed by the judgement in Broadcast Music and Broadway which is also part of the interpretation of the Sherman Act. Now by its very nature the Sherman Act creates a criminal offence. You price fix, it is a felony and it is three years imprisonment which then brings in all sort of things like the balance..., the *onus* of proof which is a totally different test.

10 Are we not..., you know the argument has been raised that in looking at the Sherman Act then it creates all sorts of other safety measures because it is a criminal offence unlike the South African scenario where it is just subjected to civil penalties instead of going to jail for price fixing. What would you say to that view to say basically the Sherman Act it is..., it creates a criminal offence which then we will expect that there will be a lot of other..., a different approach to the entire price fixing issue as compared to the South African scenario which basically subjects civil

20 penalties?

MS MEIJER: And I think that the fact that there is a criminal offence and even in our laws if this was converted into a criminal offence and there is some talk that it

*Pretoria
05 June 2007*

might be, the normal standard would then be the much higher *onus* of proof of beyond a reasonable doubt but I am not sure in the context of a Competition Act that whether or not it is..., whether or not the penalty is criminal should really make a difference because the authority should be seeking to promote competition and maintain and promote competition and if it prohibits conduct that ought not be prohibited on a balance of probabilities even, I think that that is equally serious from the point of view of the purposes that the Act seeks to achieve as would be sending
10 someone to jail for a contravention. So I am not..., I mean I think if your question is that does the fact it is a criminal offence in the US mean that they have taken a different approach then should it be taken in South Africa where it is not a criminal offence, I think the answer should be that that does not necessarily create a difference and should not create a difference in approach.

CHAIRPERSON: Well that is the argument which was raised before me I am just raising it to see what would be our approach to that same argument.

20 MS MEIJER: And in Canada for example, it is a criminal offence and there have been very few cases under Canadian law because, you know, in economics I think it

*Pretoria
05 June 2007*

is quite difficult to prove something beyond a reasonable doubt and in fact I am not sure that our authorities in South Africa and perhaps this is a broader debate than we ought to be having today but I am not sure that it would serve the purposes of the Act to criminalise the statute because it would necessarily involve the much higher *onus* of proof of proving the contravention beyond a reasonable doubt. And in Canada there have been very, very few cases. The majority are settled because the authority is not certain that it will be able to prove the case beyond a reasonable doubt.

10

ADV PETERSEN: Ms Meijer I am not sure when it comes to Section 4(1)(b) that the Legislature intended much economics to come into that. You are nodding?

MS MEIJER: I agree.

20

ADV PETERSEN: But what the SCA does seem to have made clear or they have left a number of questions open in sending the matter back to the Competition Tribunal, what it does seem to have made clear is that to bring conduct under the 4(1)(b) prohibition, it must be properly characterised with reference to the meaning of the prohibition, the intended meaning of that prohibition. And so we can assume for the purposes of the next part of the exercise that all the necessary evidence is

Pretoria
05 June 2007

present for purposes of characterisation and even evidence beyond a reasonable doubt that does not..., as I think you are saying, matter fundamentally. The question is what is the proper characterisation or approach to characterisation. Now going back to the Richard Wish boxes idea, on page 113, I see you have the book there about a little less than half the way down, it says:

10 “The CFI,” that is the Court of First Instance, “do not refer European Night Services to agreements to limit output but they must also be allocated in the object box or purpose box on the basis that they obviously restrict competition.”

I will stop quoting there. I understand him to be explaining that some kinds of agreement are so plainly anticompetitive in their effect that they can only have had the purpose of restricting competition, the object of restricting competition. Does that...; does my interpretation of what he is explaining there makes sense to you?

MS MEIJER: Yes.

20 ADV PETERSEN: Okay if that is so, then one need not get into the weighing of pro and anti-competitive effects in characterising conduct for purposes of the object box

*Pretoria
05 June 2007*

or the purpose box or I would ask for the purposes of Section 4(1)(b) but one can look at well-known effects and obvious effects of an agreement in determining what the purpose of that agreement must be. Would that be satisfactory?

MS MEIJER: Can you just repeat that?

ADV PETERSEN: Yes, you see the dilemma with interpreting Section 4(1) is how to characterise conduct for purposes of the *per se* prohibition without opening the door to the kind of full inquiry into pro and anticompetitive effects which is envisaged for the Section 4(1)(a) prohibition. Any agreement between competitors which has predominantly anticompetitive effects can be tackled by the competition authorities under Section 4(1)(a) we seem to be ad idem on that. The problem is how to determine whether an agreement should be *per se* prohibited under 4(1)(b) without the defendant been able to open, the respondent being able to open the door to the full inquiry envisaged by Section 4(1)(a) bearing in mind that the prosecutor, the competition authorities bears the *onus* of proof.

20
Clearly it is intended under 4(1)(b), I would think to create a simpler category where plainly anticompetitive conduct can be prohibited without further ado. Now how

Pretoria
05 June 2007

does one bring effects into that characterisation without opening the door to the full scale inquiry and so I am raising with you whether Richard Wish does not give us a hint there that if the type of restriction is so obviously going to have an anticompetitive effect that it can only have had that purpose. Then one uses it where obvious effect to throw a light on purpose but the essential inquiry under 4(1)(b) might remain what is the purpose of this restriction.

10 MS MEIJER: I mean I would agree with that but I do not think that one can say simply because conduct limits output or divides markets or because a price is literally fixed that that is enough to determine that it was its object. You need to go somewhat further in considering whether the conduct has a reasonable explanation before prohibiting it and I mean perhaps a good example is, there is a case in the US of I think it was Polk Brothers..., it is Polk Brothers versus Forrest City Enterprises where two firms, you know one sold appliances and home furnishings and the other sold you know building materials and they had substantial chains operating

20 throughout the US. Polk Brothers who sold the appliances had a piece of land and they wanted to build a big warehouse on it and it contacted the other player Forest City and said “you know would you like to come into a joint venture, we will build

*Pretoria
05 June 2007*

this warehouse, we will have separate entrances and each use this facility. We will share the parking lot and it will provide for consumers a one-stop-shop where they can buy everything that they need for their home improvements at one place.”

10 And they agreed to this and they agreed to it on the basis that each agreed that they will only sell certain kinds of products in their shops and on the face of it that is a market division. You know Forest Brothers or Forest whatever the other one was called, Forest City Enterprises agreed that it would not sell any home appliances and then proceeded to do so and Polk Brothers tried to prevent it from doing that and the court said that had it not been for that restraint, they would never have entered into this agreement. So that although on the face of it, there was a division of markets. Competitors had clearly allocated between themselves what they would sell at that facility but that was not the purpose of what they have done.

20 They would never have cooperated at all. They would never have had the joint facility to the benefit of the public had it not been for those restraints. So I do not think it is enough to find purely the output limitation restraint or the like but I do

*Pretoria
05 June 2007*

agree that there is certain conduct where one may from the effects be able to deduce what the purpose was.

ADV PETERSEN: But now you are getting into the area of ancillary purposes.

MS MEIJER: Yes.

ADV PETERSEN: And presumably you are going to develop that?

10 MS MEIJER: Yes.

ADV PETERSEN: Yes.

MS MEIJER: Sir the way that the US has approached characterisation has been..., and I am going to quote from the Broadcast Music in the case which the Chair referred to a moment ago which I think deals with it extremely well. They acknowledge that some assessment of the intent behind and the effect of agreements is required and again that is not certainly specifically mandated in their legislation
20 and said that in characterising this conduct under the *per se* rule our inquiry must focus on whether the effect and here because it tends to show effect, the purpose of

the practice are to threaten the proper operation about predominantly free market economy.

That is whether the practice facially appears to be one that always or almost always tends to restrict competition and decrease output or in stead as one design to increase economic efficiency and render markets more rather than less competitive and I think that that is..., that in a sense sums up the kind of approach which we believe ought to be taken to Section 4(1)(b) and that although there would be some analysis of and I
10 think that there is no reason why there should not be some analyses of both purpose and effect, it is a higher level analysis than would be required under Section 4(1)(a).

In other words the parties would not; I do not believe lead detailed economic evidence as to the effects of their arrangements. They would on the face of it have to show that they had a legitimate business purpose in entering into the arrangement and that at least on the face of it. The effect has not been plainly and obviously
20 anticompetitive.

ADV PETERSEN: Sorry to keep stopping you but we have not..., sorry is this the BMI..., this quotation from the BMI case...

*Pretoria
05 June 2007*

MS MEIJER: Yes.

ADV PETERSEN: Okay it seems to and part of the formulation work from purpose towards effect is what I was raising from you previously works from obvious probable effect towards purpose. One of the things that we will have to deal with suggesting a construction for Section 4(1)(b), if we have to, will be..., we will have to grapple with the practical problem that the way this doctrine has developed in the United States and it is exemplified by the BMI case, from initially an idea of a quick
10 look you characterise by a quick look, then the experience that some agreements could not be characterised satisfactory by a quick look. It might require a more extended look, still in order to arrive at a characterisation of *per se* or not prohibition and so the distinction between the rule of reason analysis which is a full effects analyses, it seems to me our Section 41(a) is concentrating on that. The distinction between that and the supposedly easier job of characterisation is quite dramatically eroded and clearly there would be resistance to the idea that we could..., that we in
20 South Africa or that the legislature would have intended to allow the one exercise to become indistinguishable in the last analyses from the other. How does the Tribunal,

Pretoria
05 June 2007

to put it differently, how does the Tribunal or court know where to draw the line in the characterisation process?

MS MEIJER: I am not sure that I agree with you that there has been a substantially erosion and that there has been a blurring in the US. I think that that they have..., that the process of characterisation is now something that is quite well defined there where as I said earlier you look at it on the face of it, is this an agreement which is so unlikely to ever have a pro competitive benefits that we can prohibit outright. If not
10 then they do go into this process of characterisation and in my mind it is really a question of determining whether you know in that process of characterisation I do not believe that they go into a full effects kind of analysis. They do look at the purpose, they do look at the market in which the practice has taken place and for example in BMI they said that this was in a sense a new kind of product had been created by the arrangement that BMI had in place which enabled radio stations for example to buy a license, a blanket license.

20 So they look more broadly at market circumstances, they look at the purpose and perhaps to a limited extend to the effect but I do not think it is resulted in a complete

*Pretoria
05 June 2007*

blurring of the line and I accept though that this is not going to be an easy process and I accept also that it is important to maintain a distinction between Section 4(1)(b) and Section 4(1)(a).

CHAIRPERSON: I just want to..., do you by any chance have the page of the paragraph passage in the BMI case or paragraph? You can give it to me later. You can carry on with your..., yes.

10 MS MEIJER: Since BMI the US court have not condemned price fixing arrangements that are ancillary to the achievement of genuine efficiencies on a *per se* basis and I would not go into it in any detail because I am sure that you have looked at it but in the Nabanco case which was the case brought against Visa on the basis that Visa had engaged in price fixing. There the court took the view that this was not an arrangement that ought to be *per se* prohibited.

20 It then went on to do the full rule of reason analysis and ultimately to allow the arrangement and I think a large part, the reason that in characterising it, it did not *per se* prohibit the arrangement because that it did, it believed that the arrangement did exhibit some features of a joint venture and it acknowledged that this was a complex

Pretoria
05 June 2007

industry and that it would be very difficult for the courts in that case to say “this is the kind of practice which we can say by experience almost never has a pro competitive outcome and therefore should be *per se* prohibited. Turning...

MR BODIBE: Before you move on, sorry...

MS MEIJER: Yes?

10 MR BODIBE: Could you explain to me how the court determined that Visa was a..., or exhibited characteristics of a joint venture?

MS MEIJER: Perhaps I can read a paragraph and unfortunately I will have to give you the reference later because I did not make a note of it but what the court held there was that “the evidence demonstrated a complex relationship between cardholder and merchant demands for the Visa service suggestive of a joint enterprise. This joint enterprise is not subject to *per se* scrutiny because it is a necessary element in the creation of efficiency creating integration. Visa exhibits
20 characteristic of a joined venture even if it is not technically a joint venture.

**Pretoria
05 June 2007**

It is an entity that is partially integrated some functions such as the”...they refer to it as the “IRF” but we refer to it as the interchange fee, “to develop a product the Visa Card that none of its members could produce individually. The product then is truly greater than some of its parts. For a payment system like Visa to function, rules must govern the interchange of the cardholder’s receivable. The interchange fee represents one such rule establishing a necessary term without which the system would not function” and they said “the interchange is a mechanism by which Visa ensures the

10 universality of its card, not a price fixing device to squeeze out enterprises like NaBanco.”

So it was on that basis that they considered that it exhibited characteristics of a joint venture and it was not something which they ought to *per se* prohibit.

MR BODIBE: So it is not on the basis that the banks and Visa were in a relationship that could be described as joint venture?

20 MS MEIJER: They stop short of calling it a joint venture but they did acknowledge that it had some of those features.

Pretoria
05 June 2007

MR BODIBE: Thank you.

MS MEIJER: So just to sum up what the US approach has been that they have hesitated to prohibit *per se* until experience has shown that the type of restraint involved almost never produces a pro competitive outcome and if the price fixing arrangement is ancillary to the achievement of genuine efficiencies and the parties can demonstrate that they had an legitimate business purpose and that there is some prospects that those efficiencies might be achieved, then a process of characterisation
10 is undertaken and which limited evidence is permitted to determine whether the restraint should be *per se* prohibited.

And I think that what we really wanted, the point that we want to make about this, as we will about the other jurisdictions that we look at, is that this approach prevents the type one type error of catching in the net arrangements which are..., substantially reduces the risk of catching in the *per se* net arrangements that may well be pro
20 competitive.

Pretoria
05 June 2007

MR BODIBE: Okay, sorry Chair? Again sorry, you have used several times the concept of efficiency, now first I am not a lawyer, how do you inquire into what is efficient and what is not efficient?

MS MEIJER: I think efficiency enhancing is normally something that will result in products reaching the market at a lower price or you know it is I think more that kind of arrangements and...

10 (Caucus)

MS MEIJER: When it is generally..... we would say it is generally arrangements that result in the product reaching market or it result in the firms that engage in the venture incurring lower cost and hopefully that that consequently translate into lower prices but I think efficiency is more specifically firms achieving efficiencies in their own operation to lower their cost of production. Sorry or a bigger volume using the same base.

20 MR BODIBE: Okay so what happens in the situations.... I am not making any firm position on this, so in the example of this four party models that the arrangement on

*Pretoria
05 June 2007*

the one hand ensures increased volumes. So for example, acceptance of these cards and the fact that you balance the cost between, the theory goes, between the two sides that then what happens and I am not saying that it has not resulted in this but it could potentially result in not lowering the cost of production because the compensation that is given to one party may not necessarily, it can actual have the reverse outcome that it is not an incentive to innovate but to continue operating with the less efficient from a cost point of view mechanisms of producing the output because they have...,
10 their cost are reimbursed because of the scheme of arrangement but where the actual efficiency achieved is in achieving the volume efficiencies. So in that particular context, how do you balance between the two efficiencies?

MR FERGUS: I think two factors come into play. The first one is if you have no competition at the acquiring level, no competition at the issuing level. So no competition for collecting the transactions from the merchants and no competition in issuing the cards to the cardholders then the argument would stand firm once you
20 have that competition many efficiencies in the system will result in appropriate pricing to those two constituents. The second is that if you had a perfectly balanced market then you have the same risks. So if you had the issuer having the same share

*Pretoria
05 June 2007*

of the market as he has in the acquiring market and all the players in the market being in that position, then you have the risk. Once you have differentials in market share then you are not going to have those risks coming into play.

MR BODIBE: Currently have we seen any lowering of production cost in these four party models?

MR FERGUS: Yes over the last 30 years you have had the cost of processing a
10 transaction dropped by 75%.

MR BODIBE: Thank you.

ADV PETERSEN: Just before you go on from the United States and the NaBanco case, let me raise this with you and again deal with it at any stage if you wish to. Lets say for arguments sake that one comes to the conclusion that interchange as a concept or type of arrangement is not *per se* restrictive of competition and would not have been intended to be, can one entirely then leave out of further analysis for
20 purposes of Section 4(1)(b) or *per se* prohibition the level at which interchange happens to have been set.

Pretoria
05 June 2007

MS MEIJER: I think..., I mean Standard Bank's approach to this has been to acknowledge that although this is..., it is an arrangement that occurs in a market where there are enormous complexities, I think Standard Bank does acknowledge that there..., that it is..., you know that it does occur in a context where potentially that fee could be set too high but Standard Bank believes that in South Africa appropriate steps were taken by the banks and responsible steps were taken by the banks to ensure that that interchange were set in accordance with international best practice and that..., for that reason it has been set at an appropriate level and Standard Bank also is willing to submit, you know to further scrutiny in that regard. Does that answer your question?

ADV PETERSEN: Yes, I do not..., to some extent, I do not wish to be misunderstood as implying in my question any evaluation concerning the appropriateness or otherwise of the level of interchange that has been set in any payment stream. That is a separate question, what I am hoping to get further clarity on is the conceptual method that we should use here, okay? Now you just mentioned and in fact you will find it in the Standard Bank submission of 10 April 2007 on card

*Pretoria
05 June 2007*

interchange fees, page 33, paragraph 5.2.2 and Mr. Fergus himself said the very same thing the last time we had the pleasure of his company.

MR FERGUS: That was luck

ADV PETERSEN: That and I quote from the written submission “there exists the theoretical potential to use interchange in order to set the interchange fee above a competitive level.” Okay so dealing purely with the theoretical potential; let us
10 suppose that one agrees that interchange *per se*, existence of it set by all the parties together, set by the scheme however it maybe set, is itself not a candidate for prohibition under Section 4(1)(b), let us accept that for argument sake. The question then is, if theoretically interchange has been set by those parties at an inappropriate level, which involves some abuse either on the merchant side or on the cardholder side, if that is clear enough on the evidence could one not bring it under 4(1)(b)?

MS MEIJER: Would you not in order to determine that need an enormous amount of
20 evidence regarding what the appropriate level should be and I would not have thought that there was scope for that under Section 4(1)(b). So that having determined that on the face of it, it is an arrangement that had a legitimate business

Pretoria
05 June 2007

purpose and may well enhance efficiencies. You would then be forced, I think to shift that analysis into Section 4(1)(a) and go into this very detailed inquiry as to the appropriateness of the level.

ADV PETERSEN: Yes, but are you not now making the..., is the implication of your line of argument here, not one which makes the amount of evidence that is needed to characterise the conduct, the critical issue rather than whether one has to go into the pro or anticompetitive effects of the conduct.

10

MS MEIJER: Well I think to the extent that evidence is permitted under 4(1)(b), it is not a full blown inquiry and I think we all accept that. So that once you have come to the conclusion that this is not an arrangement which on the face of it should be *per se* prohibited, I think that at that moment the inquiry shifts into 4(1)(a).

ADV PETERSEN: Yes but are we not going round in circles there because we surely do not want an approach to interpretation of 4(1)(b) an approach to the characterisation problem which Bloemfontein left very much open to be filled in. We surely do not want an approach which leaves it up to how the Tribunal or the court feels on a particular day. It must have some adequately clear delineation that

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Pretoria
05 June 2007

everybody can work with the concept in naming where the boundary lines have prohibited and permissible behaviour between permissible behaviour lie so the quantum of evidence that might be needed to characterise this, to me a problem notion. Going back to the idea I raised with you earlier which may be right or wrong but perhaps 4(1)(b), one is essentially trying to determine the purpose of the agreement and you may need any amount of evidence to prove that purpose and if obvious effects help you, you can bring that in but you are not getting into an inquiry on the full effects of the..., I mean if that approach is correct then would I not be on good ground to say in relation to a particular element in an agreement between competitors that while as type it may not itself call for pro..., for *per se* prohibition because it would not necessarily have a restrictive purpose but in the way that it was being used it is as it were being used as a platform or a shelter for bringing into that agreement between competitors a deliberately restrictive element. In other words if this potential abuse as in fact carried into practice one could arrive at the conclusion about its purpose and therefore bring it under 4(1)(b).

MS MEIJER: And if we can just..., so that what you posit ..., is that not part of the whole characterisation exercise that I have been suggesting which is that you would

*Pretoria
05 June 2007*

look at the agreement to decide whether there was some prospect that it might have efficiency enhancing or for pro competitive outcomes but you would not need to prove conclusively that it did. And having shown that it might have..., I mean are you positing a situation where in fact you have already demonstrated some anticompetitive effect?

10 ADV PETERSEN: Well I think I am..., the difficulty I am raising with you, has for me had two elements. One is that it seems to me that NaBanco case addresses the problem conceptually at a very abstract level. I believe they had plenty of evidence in front of them but they did not go into the question of the appropriateness of the level at all because that was not the case that was put to the court. The case was whether interchange *per se* is against the law. Well they concluded it is not but that is the beginning of the inquiry. The other part of the inquiry is, let us suppose there is an element and an agreement between competitors which even in itself may well have a legitimate purpose but in the particular circumstances of the case and I am not

20 suggesting that that applies here. It is entirely a different question, in the circumstances the case, it provides a means by which the competitors can load onto the otherwise potentially legitimate agreement, elements which are in fact designed

Pretoria
05 June 2007

to restrict competition and have no legitimate purpose. And so what I am really raising is with interchange does the level not at which interchange is set, offer itself potentially as a matter for scrutiny also under 4(1)(b)?

MR FERGUS: I am definitely not a lawyer, so I maybe missing the point here but it is a self bouncing scheme in the four party model that if you set interchange to high, you artificially set it high the retailers will refuse to accept the cost and will exit the scheme. So way before it becomes a regulatory issue it would be a self-correcting issue because once the retailers do not accept the cost, you do not have a scheme.

ADV PETERSEN: Sure I hear you Mr. Fergus but what was raised and again I am not signaling any conclusion about this, what was raised in quite lengthy hearings on interchange, payment cards was the possibility and here I am noting your concession that there can be abuse with interchange, is the possibility that in a concerted way, cards and in particularly here perhaps credit cards, the take-up with credit cards and the use of credit cards can be made almost completely painless to the cardholder with a delayed network effect from the increased take-up with cards imprisoning the merchants so that their choice as to whether to go on accepting cards or not becomes

*Pretoria
05 June 2007*

an increasingly difficult choice for them to make because so much of their business is now card based. That the participants therefore in the scheme and this is purely hypothetical...

MR FERGUS: Yes?

ADV PETERSEN: That the participants in the scheme could by their combination and use of interchange have manipulated the elasticity or inelasticity of demand on the different sides of the market to produce a situation where they are able potentially uncompetitively to extract revenue...

MR FERGUS: ...I am trying to think of a situation where it would make business sense as opposed to the legal argument to do that because hypothetically, you know, you could have such a situation arise, I cannot understand how such a situation would arise in a four party situation with multiple issuers, multiple acquirers, different market shares and an independent assessment of the rates. So I am trying to actually put the practical comments onto a hypothetical legal interpretation of what could arise should it be in the interest of diverse group to do it because the group is too

*Pretoria
05 June 2007*

diverse and not actually sitting with the same objectives in the setting of interchange which is probably the biggest control.

10 MR HODGE: I mean maybe just to add from an economist perspective not from a legal perspective that as I understand the proposition is, can you infer from the level that there has been a definite harm and definite intent and I think looking at the submission in terms of 5(2)(1), the level itself does not necessarily indicate that that harm is taking place. The theoryss being put, fall in the literature and by the European Commission is that you are transferring revenues to another side of the market and one which is less competitive and it is only under those situations that there maybe profiteering but if the issuing side is a competitive market as well, then certainly that will be competed away and is not necessarily any harm. So the level itself does not necessarily lead to a conclusion of harm. It is in combination with other factors as well.

20 ADV PETERSEN: I hear you, my main difficulty with that argument is that where the revenue is extracted on the merchant side, the merchant in turn extracts it from the customer. Where the merchant..., where the revenue is extracted on the issuing

*Pretoria
05 June 2007*

side, it is clear to the cardholder what is being paid for the use of the card. If it has been extracted invisibly via the merchant, it is not clear and transparent to the cardholder and it seems to me that has potential competition implications. Again I am not expressing any..., even tentative conclusion about the appropriateness or otherwise of interchange or any particular level of it, I am just exploring whether it is potentially of 4(1)(b) issue.

10 MS MEIJER: If I can just add to that. I think that if you find that the arrangement may have a legitimate business purpose, it may result in, you know, the card being more universally accepted and achieved the kinds of scale efficiencies that we believe that it does achieve. The fact that you might see evidence that its level has been set too high, would not in my view be adequate for you to then prohibit it under 4(1)(b) because I think you would then run that same risk of making the type one error of prohibiting an arrangement that is pro competitive. So I think under those circumstances it would be a mistake for a competition authority to *per se* prohibit.

20 MR BODIBE: Can I make a follow-up to Mr. Fergus, you have so much faith in the self-correcting mechanism of a four party which in theory I can see but there are

Pretoria
05 June 2007

certain elements of the scheme or rules in the scheme that mitigate the self-correcting mechanism. One of those is the rules that in order to say for example to acquire, you must have an issuing base set at a particular level by both MasterCard and Visa. Do you not think that those rules sort of blunt the self-correcting mechanism of the fourth party mechanism especially in an economy where the extent to which you can grow the market is limited? So the extent to which a new bank or a new entrant can achieve the kind of volumes that are required on the issuing side is limited by that particular rule, would that not blunt the self-correcting instrument?

10

MR FERGUS: I cannot argue for Visa or MasterCard position in setting the rules, my interpretation of that would be that you grow this scheme, you grow the volume of activity, you increase the penetration by issuing cards and therefore you would want the participants in the scheme to be issuers as well as acquirers. Yes, and so if you have a mature market you then therefore want a bank to be committing to both issuing and acquiring. Where you have new markets, and we are entering many markets throughout Africa at the moment, the rules are being mitigated so that we can enter issuing and acquiring at the same time for exactly the same purpose of growing the scheme. We have numerous so and I can give you a written submission

20

*Pretoria
05 June 2007*

of which market we are doing that in the next 12 months if that helps. So the rules have been looked at and it has been concluded that the entering issuing and acquiring concurrently in a mature market makes sense for the future growth of the scheme and the use of the cards.

MR BODIBE: So you may think...

MR FERGUS: But I think it is more to..., the rules have more to do with mature
10 markets or maturing markets than they are to do with the brand new markets.

MR BODIBE: So how does that play itself out in a mature market?

MR FERGUS: Well in a mature market you have acceptance, pretty well ubiquitous
acceptance and so therefore someone coming in and entering the market, you grow
the market you want more cards in issue and therefore before you should be allowed
to acquire you need to issue. You know I mean we are in area where it is Visa or
MasterCard's rules that..., you know I can only give you my interpretation of the
20 rules and tell you what they have done in new markets.

*Pretoria
05 June 2007*

MR BODIBE: And what is the potential of those rules on inhibiting your self-correcting mechanisms?

MR FERGUS: I do not think it has any impact on inhibiting it. I mean the self-correcting factor that comes into play by the balance of issuing and the balance of acquiring that you have, not whether you are a participant in one side or other of the equation.

10 MR BODIBE: Well I would...

MR FERGUS: Because it is a flow from one side to the other so you have got a mismatch which you have got in every single bank in South Africa today.

MR BODIBE: But I will argue that if you have a rule that says “to be as an acquirer you must have an issuing base of so much percent” and in a mature market which means you are assuming that the scale of growth on the issuing side is quite limited, I would argue that in that circumstances you are self-correcting mechanisms are
20 blunted or cannot work perfectly because the share of the market have already been

*Pretoria
05 June 2007*

achieved and you, the potential for new entrants to enter is very limited to shake the position of the incumbents.

MR FERGUS: Your potential to entrant..... to enter is not limited in anyway shape or form by whether you are an acquirer. The two are not in anyway related. There are no..., it is four party scheme. Issuers that are issuing is totally independent business from acquiring, it is not linked.

10 MR BODIBE: I am referring you to a rule, correct me if I am wrong...

MR FERGUS: Yes?

MR BODIBE: That I am made to understand from Visa and MasterCard...

MR FERGUS: Yes?

MR BODIBE: That before you can enter the acquiring you must at least have an issuing base of about 15% or something like that, is that correct or not?

20 MR FERGUS: I think you have to be issuing, yes. I could not comment on the exact wording of the rules in the two associations but that has much more to do, with the

*Pretoria
05 June 2007*

need to show your commitment to grow the market and develop the market and increase the use of cards because that comes from issuing.

MR BODIBE: Okay we can pursue it some other time...

MR FERGUS: I think the question, you know, to getIt is very difficult for me to say why Visa have put the rule in place or why MasterCard has put their rule in place. I mean you know there is lots of economic reasons why they might. The
10 existing banks have actually grown the market and developed it and therefore a new one should increase the size of the market as part of their commitment to it. But I am guessing, it is really for them to answer that.

MR BODIBE: The reason I am asking this question is that in your response you put so much faith in the self-correcting mechanism which and you said for example multiple acquirers, multiple issuers and so forth and that that in itself can be a safeguard against abuse but I am just..., I was..., curiosity for me is that...

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*Pretoria
05 June 2007*

MR FERGUS: I would add an equal weighting in having independent experts understanding the cost study to set the level of interchange because I think that is equally as important in ensuring you do not have any abuse.

MR BODIBE: Okay thank you.

MR FERGUS: I mean there are many weights and balances in the process. Its a complex structure; or we would not be having the hearing would we?

10

CHAIRPERSON: Okay thank you, I know Ms Meijer is going to move into the Canadian Law, maybe this might be an ideal time to take the short break. We will come back after 30 minutes. What time is it now? Yes will come back at about quarter to...and then proceed to deal with the rest of the other research you have done.

(Adjourns)

20

On Resumption:

CHAIRPERSON: Ladies and gentlemen, welcome once again and our cell phones off once again. I have been made to understand that there are time constraints with

*Pretoria
05 June 2007*

regard to the Standard Bank team. So what we will do, we will..., Ms Meijer if you could adjourn your arguments to after lunch and then we can start with the other aspects so that the people that need to leave can leave at lunch time. I think that has been agreed and arranged with the Enquiry manager.

MR SINTON: That is correct Mr. Chairman.

CHAIRPERSON: Alright, so we will start with the issues relating to interchange
10 which we stood adjourned the last time we had the...

ADV PETERSEN: Issuing and acquiring...

CHAIRPERSON: And..., yes also issuing and acquiring. The last time we had the meeting. Right before I ask for all the others if they have any questions, alright let us..., Mr. Petersen do you have some questions?

ADV PETERSEN: I have got a few...

20 CHAIRPERSON: Got a few?

ADV PETERSEN: Do you want me to start?

CHAIRPERSON: Yes you start. Oh before I forget, your slides will be Exhibit XX, your slides. Right, you may proceed then.

ADV PETERSEN: Could not help noticing the body language here but we must do justice to your very considerable effort which we thank you. You did indicate the last time that you appeared in the hearings dealing with this subject matter and we have not had an opportunity to thoroughly study your submissions and it was subsequently reiterated last week that you favour a uniform approach to the setting of interchange across all the payment streams. Consistent across payment streams is the way that you put it and you include without distinction in that page 53 of your first submission of October last year, credit card, debit card, hybrid cards, EFT, EADO and NEADO, ATM, money transfers and agency arrangements, could you just clarify what you mean by agency arrangements?

MR SHUNMUGAM: Now Chair it is essentially where you act on behalf of another bank.

CHAIRPERSON: If you could just for the record, you are Mr. Shunmugam?

*Pretoria
05 June 2007*

MR FERGUS: The two examples we act for agents for Rennie's Bank and we act for ...agents for Post Bank.

ADV PETERSEN: And..., but getting back to the main thread on page 54, you repeat and I quote "it should be clear that the arguments made in the case of these payment streams should apply across payment streams in general." Am I right in thinking that it is still your approach as you sit here today?

10 MR FERGUS: Yes.

ADV PETERSEN: Well I just want to...

MR SINTON: Sorry Mr. Chair could we just pause there, that was subject obviously to our willingness to consider direct charging in the ATM world.

20 ADV PETERSEN: Fine, now we have separately debated ATM carriage and the merits of a direct charging model instead and thank you Mr. Sinton for drawing attention to that. In your consideration of that and it may not call for a definite response today but I would just ask you to grapple with this problem which strikes me. Where you treat ATM transactions as simply a payment stream, it seems to me

*Pretoria
05 June 2007*

that a vital distinction is being obscured by that analytical approach because in fact we are not dealing there with the processing by banks simply of a payment from one side of the market to the other but subsumed in it is a relationship or a transaction which is akin to a transaction when the merchant sells something.

10 In this case the bank on the acquiring side is not merely collecting on a payment instruction that is issued through its machine when the cardholder puts in the card but is in addition performing a service which at the moment it is been compensated by the issuing bank who in turn charges the cardholder. So what we are raising really with direct charging is the separation out of that element of the service so that it is charged from a side of the market on which it is delivered.

I just want to raise that for your consideration because obviously in an ATM transaction there is a payment instruction generated being processed through clearing. In the case of an “off-us” transaction and it necessitates in inter bank payment stream but there is something else going on as well which is conceptually independent or
20 could be independent of another bank.

*Pretoria
05 June 2007*

And so this is why we have raised and it may have a bearing on this afternoon's continued discussion, this is why we have raised the problem with ATM transactions that there the setting of interchange or carriage may not simply involve the issues to deal with whether that is legitimate price setting or legitimate price fixing but it may also involve customer allocation as raised by Section 4(1)(b) of the Act. I just want to raise that with you to ask you to consider and respond now by all means if you wish but it is not necessarily that you respond now to that distinction that I have tried to articulate.

10

MR SINTON: Yes thank you Mr. Petersen, I think because of the customer allocation element of it, we prefer to respond in due course, thank you.

ADV PETERSEN: Now in the further questions that I want to raise with you about interchange, I am going to assume without it indicating necessarily a decided view but I am going to assume that interchange in general in concept is necessary in the payment streams concerned and I would like to focus in particular on the four party model. Now you have been very forthcoming in proposing including with two options, a possible way of addressing the setting of interchange across payment

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*Pretoria
05 June 2007*

streams where interchange is necessary. And if it is possible for you to deal with this today so much the better otherwise it might again require further consideration on your part and perhaps some engagement with the Enquiry but if one is to..., if the Panel were to make recommendations along those lines, the most difficult area appears to be the identifying the appropriate methodology which the independent expert would then put into effect in terms of gathering costing and other information from the participating banks. You seemed to agree that some quite detailed

10 interrogation of the costs involved and providing these different services would be necessary. Mr. Fergus you are nodding, I understood that right?

MR FERGUS: Yes, I think that the cost study is a very complex and massive data gathering exercise.

ADV PETERSEN: Yes and you are prepared to entertain that in relation to each and every one of the payment streams to which..., in which interchange is appropriate.

20 MR FERGUS: Yes.

ADV PETERSEN: Despite...

MR FERGUS: I am only empowered to speak for cards so...

ADV PETERSEN: But you seem to be getting the power from your colleagues? So am I right in thinking that in the methodology there would have to be addressed the relative costs to the institutions on the issuing and acquiring sides in providing the payment services concerned?

MR FERGUS: Yes.

10 ADV PETERSEN: And also which it seems to me is a separate question, the relative demand elasticities?

MR FERGUS: Yes I mean...

ADV PETERSEN: As between cardholders and card..., or users and merchants.

MR FERGUS: Yes I mean it is historically it has been a factor in the interchange studies yes.

20 ADV PETERSEN: But is it...is it not in fact necessary in order to move from costing to pricing in that context?

MR FERGUS: And dependent on the maturity of the payment instruments in the market.

ADV PETERSEN: Fine because you do seem to accept and argue that there is a balancing exercise going on in this process.

MR FERGUS: Yes.

ADV PETERSEN: And that must be..., must involve the balancing of demand...

10

MR FERGUS: Yes.

ADV PETERSEN: In respect of the service at particular prices...

MR FERGUS: Yes.

ADV PETERSEN: On the two sides. Now in your 10th of April submission on..., I think it is on card interchange. can you remind me where it is where you deal with relative cost of cash on that page 34, yes it is in the volume on card interchange fees, page 34 paragraph 5.3.3 footnote 45? I understand no confidentiality has been claimed in respect of this document Mr. Sinton, is that right?

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*Pretoria
05 June 2007*

MR SINTON: Yes.

ADV PETERSEN: The interchange volume?

MR SINTON: Quite correct.

ADV PETERSEN: So I can proceed?

MR SINTON: Yes.

10 ADV PETERSEN: You note that and I quote “the use of payment card is a relatively more costly form of payment for merchants but not for society as a whole.” And you developed this point and subsequent if I may say so, very useful paragraphs. Now the difficulty that I have in relation to an argument like this which is raised where interchange is set as it is set today, where there is no proper public process or involvement as you are quite prepared to envisage, in fact you put forward is that here we have something being set by the competitors in the market which involves a decision that seems to follow from your logic to impose upon merchants that which

20 arguably and perhaps indeed does benefit society but is to merchants for higher cost.

*Pretoria
05 June 2007*

MR FERGUS: It potentially is high value as well. Because if it is generating incremental sales in the retail that would not get then the benefit is greater than the costs.

ADV PETERSEN: So it would be too one sided to...

MR FERGUS: Just take...

ADV PETERSEN: Only look at the cost differential.

10

MR FERGUS: Absolutely. And of course you know the arguments above are built on many jurisdictions where here in South Africa there are particular issues about the cost of cash, about the cost of cheques that do not necessarily prevail in other markets. So this is an economic rationale for interchange. The market conditions will differ from jurisdiction to jurisdiction. The balance between the costs of the various payment instruments will vary dramatically between different jurisdictions.

20

ADV PETERSEN: Now on the..., the next point tries to relate what we have just been talking about to the question of whether there is subsidising going on as between different classes of customer...from the merchant. If we limit the issue to

*Pretoria
05 June 2007*

the merchants relative costs, well of course it is the cost to the merchant not to society that is feeding through into the merchant's retail price. So if the cost of the merchant is higher in the case of accepting cards than in the case of cash, should we not conclude that in card transactions, the cash customer is indeed on your evidence subsidising card transactions as consumer. That maybe correct from the point of view of society as a whole but at..., if one limits it to that part of the analysis, would I be making a mistake if I concluded that?

10

MR FERGUS: Well I do not know of any evidence of where retailers who accept cards are charging more than retailers who do not accept cards for the same goods. I mean there is competition on all parts of the four party program of which cost is not the only consideration. So I am not aware of any evidence in South Africa or elsewhere that has shown that a charging passing interchange in the system results in higher prices and the merchantsthis is substantiated with the merchants who do not accept cards charging at a lower price for the same goods. So if the argument

20 was correct, you would find that differential and in many sectors there are examples of where cards are accepted and where they are not accepted for the same goods or service. So..., I mean if cards were the major driver in the pricing of goods then the

*Pretoria
05 June 2007*

assumption would be through because it is a component and a relatively small component in the retailer pricing.

ADV PETERSEN: Now coming back to the methodology where interchange is concerned, it may well be that a consensus develops about this which is why it seems to be important to pro...

MR FERGUS: Yes.

10 ADV PETERSEN: What would you say to the point that it is questionable to treat the credit card simply as a payment card and to treat interchange on credit transactions as an inter bank charge levied in respect of a payment stream full stop.

MR FERGUS: I am not sure I understand the question, maybe repeat the question...

ADV PETERSEN: Well I am trying to grapple with the methodology that has been used heitherto arrive at interchange on credit cards and the different methodology which from the beginning was applied in trying to arrive at interchange on debit
20 cards.

MR FERGUS: Right.

*Pretoria
05 June 2007*

ADV PETERSEN: The debit card being treated as a pure payment instrument.

Clearly there are associated account holding costs, you have made that point to us before and so the exercises seem to involve the full costing in regard to the debit card.

MR FERGUS: I think they are different. I mean debit card is an access medium to an account, a transacting account or a savings account to which there can be other access mediums. You know cash and cheque, whilst credit card is an account *per se*.

10

We should not have used that on the day when we were doing the exercise, to use account is not right. There is a credit card account, there is no debit card account and so there is going to be differences because the cre..., the debit card is a means of accessing an account whilst the credit card is the account and different factors come into play in working out the relevant of the costs.

ADV PETERSEN: But would you agree that to the extent of the credit card also plays the role of an instrument of payment?

20

MR FERGUS: Yes.

ADV PETERSEN: Okay that a rational methodology for arriving at interchange on credit cards...

MR FERGUS: Yes?

ADV PETERSEN: Should look into the costs involved there as well.

MR FERGUS: The cost of the account?

10 ADV PETERSEN: And of the processing of the payment instruction on the two sides of the market.

MR FERGUS: Well it does I think. I am not sure we have indicated that it does not.

ADV PETERSEN: Well my impression so far and it is drawn not simply from your submission, is that the exercise which has been in the past been performed in relation to credit cards, identifies some categories of costs...

MR FERGUS: Yes?

20

ADV PETERSEN: On the issuing side...

MR FERGUS: Yes?

ADV PETERSEN: Which are treated as a suitable proxy for the elasticity or inelasticity of merchant demand...?

MR FERGUS: Yes?

ADV PETERSEN: And they are to do with the provision of credit.

MR FERGUS: Yes that is largely...

10 ADV PETERSEN: Large..., very largely.

MR FERGUS: Yes.

ADV PETERSEN: The interest free period and so forth.

MR FERGUS: And fraud.

ADV PETERSEN: And fraud.

MR FERGUS: Yes.

20 ADV PETERSEN: Okay. Well where fraud is concerned that might be common or has elements common to other cards as well.

MR FERGUS: Well with different propensities but yes...

ADV PETERSEN: But very largely it appears to be..., to do with the cost of credit.

MR FERGUS: Yes, that is correct.

ADV PETERSEN: And I am not aware...

MR FERGUS: I mean...

10 ADV PETERSEN: Of any..., sorry?

MR FERGUS: I mean the major difference is that on a debit card you are accept..., accessing funds immediately on a credit card you..., it is deferred access to funds because there is an interest free period. So that is the reason why the funding comes into the equation.

20 ADV PETERSEN: No I can understand that but what I am trying to understand is and particularly moving forward where one is trying to workout and even make recommendations concerning an appropriate methodology.

MR FERGUS: Right.

*Pretoria
05 June 2007*

ADV PETERSEN: Let me put it this way. I can see that with debit cards what's the basis upon which it is set out upon the exercise...

MR FERGUS: Yes.

ADV PETERSEN: There is a costing on both sides and then there is an evaluation of demand on both sides...

MR FERGUS: Only fair, yes.

10

ADV PETERSEN: In order to achieve a point of balance. In relation to credit cards, why should one not start out with it as a payment instrument and then bring into account also additional features.

MR FERGUS: I think we are into nuances. I think that is exactly what is happening on credit cards. I mean it is more that factors of the credit card being an account are left out of the calculation rather than things were put in. So for example you know is the cost of the statementing a valid cost to be pulled into the interchange calculation because you are producing the statement as much for the transaction as you are for the borrowing and so, you know, it is..., what is a valid part of the transfer of value

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*Pretoria
05 June 2007*

for the transaction rather than what is related to the instrument of the account because in debit cards we do not take into account all the costs of running the transacting accounts and so it is what is reasonable to put into the interchange calculation. I do not think there is the difference or perhaps perceiving in the two calculations. The one difference is where it moves from purely transacting into value generated for the retailer by not having to provide credit and not take the cost of that credit and that fraud.

10

ADV PETERSEN: I note your answer and I will just indicate that I am not seeing anywhere any indication that there is a study of the relative costs of the credit card as a payment instrument in the setting of interchange up to this point and so my real question is, is it rational to require to be or to propose that it be introduced into the setting of interchange in the future.

20

MR FERGUS: Well can I come back and speak to the two associations, they have slightly different methodology. I do not want to put words in their mouth and come back to you with an answer.

ADV PETERSEN: Yes please.

*Pretoria
05 June 2007*

MR FERGUS: Yes.

ADV PETERSEN: Yes and likewise there appears to be an absence of any inquiry into the elasticity or inelasticity of demand on the cardholder side where credit cards are concerned.

MR FERGUS: I guess the elasticity of demand there is more to do with the pricing of the cards to the cardholder, the combination of interest rates, annual fees,
10 transactional fees that are applied and if they are reasonable for the benefit they are receiving from the relationship and carry on with the two high that elects this.

ADV PETERSEN: I hear you but you appreciate that what I am trying to address here is are the difficulties involved in moving to a transparent and objective approach to the setting of interchange and appreciate that the complex elements enter into business judgements or into business judgements are made...

MR FERGUS: I think...

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ADV PETERSEN: But if one has to investigate and draw conclusions...

MR FERGUS: Yes...

*Pretoria
05 June 2007*

ADV PETERSEN: how does one go about it?

MR FERGUS: The difficulty in the working out the elasticity of demand on the two sides is the sole price to the retailer is the merchant discount rates. The price to the cardholder is the combination of the interest rate, the annual fee, activity fees that go on in running the account and so getting that comparison is very difficult. It is not an easy assessment to make. It is on the cardholder side, it is a component and probably a relatively limited component compared to the annual fee, the need for credit, the cost of that credit which are much more drivers in taking the credit card accounts.

ADV PETERSEN: Just on a point of detail, in your 10th of April 2007 submission on page 32, paragraph 4.7.2 in the middle of the page, you indicated there was in the process that went on in 2002 some involvement of the SARB of the Reserve Bank. Would you have any or your colleagues be able to indicate to us what that involvement was?

MR FERGUS: We will come back under advisement. We believe it was discussions and description of the process that would be followed. I will go back and check because I was not here then.

*Pretoria
05 June 2007*

ADV PETERSEN: In your original submission of October last year, page 55 towards the foot of the page, the paragraph number for the record is 4.2.5.4.3.2 “Undermining of the Acquiring Model.” You are listing here adverse consequences of removing card interchange, if that were to be considered. You say “the single acquiring model is undermined as there is economic incentive for acquirers to remain in the market further intensifying the proliferation of sorting-at-source and multiple acquiring.” So it is acquiring would not be undermined, it is single acquiring that would be undermined, is that right because...

10

MR SINTON: That is correct Mr. Petersen...

ADV PETERSEN: Yes.

MR SINTON: Yes it is.

ADV PETERSEN: I am skipping over material to try to get to the essentials points in the available time. Let us go back to the ideas that you put forward for a uniform process of the setting of interchange and your option one..., let me just get the

20

right..., it is in the original submission page 64...towards the foot of the page 4.2.7.6,
are you with me?

MR FERGUS: Yes.

MR SINTON: Yes.

ADV PETERSEN: Alright I just want to make sure I am understanding you
correctly. It seems to me that your option one seeks to apply uniform lists of cost
10 components to the setting of interchange for all payment streams. Suppose I were to
accept that the principals would be the same...

MR FERGUS: Yes.

ADV PETERSEN: Assuming that interchange is necessary in the stream concerned,
why would the cost components also be the same or if I misunderstood your
paragraph.

20 MR SINTON: Sorry could you repeat the question, I was...

ADV PETERSEN: The way I read and you appreciate I am trying to be as short as I can here...

MR FERGUS: Yes.

ADV PETERSEN: The way I read your option one, it seems to go beyond saying that the principal should be uniform across the payment streams but even that the cost components would be the same and I have difficulty with my limited experience...

10 MR FERGUS: No, no it is not that. It is saying the relevant cost components for that payment stream. Sorry that would be the relevant...

ADV PETERSEN: No it may be that I misunderstood you. I just wanted to make sure that I do not. Okay now so far as the principles would be concerned, as I understand it, there would be no reason why that should not be known by the general public what this is seeking to achieve, it would have transparency in other words as well as objectivity.

20 MR FERGUS: Yes.

*Pretoria
05 June 2007*

ADV PETERSEN: You agree, is there any reason why in that process of arriving at the proper principles where matters of public interest, cost to society of cash, all these questions are coming in, why they should not be some participation perhaps on the part of consumer representatives or some other appropriately designated groups to have input into the debate...

MR FERGUS: Around the principles...

10 ADV PETERSEN: Around the principles, would you have any difficulty with that?

MR FERGUS: None at all, no.

ADV PETERSEN: Obviously then the implementation is an expert matter?

MR FERGUS: And obviously the details supplied by the individual banks are their cost structures and are highly confidential.

ADV PETERSEN: Yes.

20 MR SINTON: So Mr. Chairman as mentioned the banks find it difficult to agree amongst themselves on most issues. So consultation certainly, we have no objection

*Pretoria
05 June 2007*

to require consensus amongst all the participants envisaged here would be a very difficult thing to achieve. So we would suggest that we need principles generally agreed but at the end of the day the expert would have to set, we think,... would ultimately be the arbiter of what those principles and cost components would be. He would require input from the banks and civil society. We have no difficulty. But I think that we try and move away from is the requirement of consensus amongst ourselves about this.

10

ADV PETERSEN: But you made that point even as among the banks?

MR SINTON: Yes.

ADV PETERSEN: Is that correct?

MR SINTON: Yes.

ADV PETERSEN: Yes so exactly how it is done, you would need a deadlock breaking or a decision making power...

20

MR SINTON: Yes we see it...

ADV PETERSEN: At the end of the process of debate.

MR FERGUS: Yes absolutely...

MR SINTON: Yes we see that vested in the expert or perhaps the expert and the regulator, Yes..

MR FERGUS: Otherwise we will never get there.

10 ADV PETERSEN: Yes..., now it seems clear because both from the publicly available submissions by the card associations and by the oral submissions made by MasterCard here that this methodology of arriving at interchange which we have just been discussing, does not correspond in the last analysis with that currently undertaken by the card associations.

20 MR FERGUS: Well in the case of MasterCard, they have become a publicly traded company and have now moved in their submission to a unilateral calculation of interchange which is where they are saying they need to be, you can have multilateral which is what we were talking about in option one here between the banks with independent expert and supervision and we now bilateral between the banks which

*Pretoria
05 June 2007*

you never get to, this is just too complex to implement. MasterCard's view is a unilateral is the right answer.

ADV PETERSEN: Yes the..., I hear you, the difference that I am wanting to put my finger on is that in this approach which involves a costing and related study being undertaken at the present time that is based on a methodology or set of principles to use language that we were using a few minutes ago, determined by MasterCard.

10 MR FERGUS: Yes.

ADV PETERSEN: Right, then it is implemented. And then MasterCard exercises a business judgement to set the default interchange based upon the input that it has had.

MR FERGUS: This is a new process so it has not actually operated yet following MasterCard's I.P.O. And you are right they do reserve that right whether it will be taken is open to some debate and supposition. We are not there yet but that has just been collected, it is quite clear that they reserve the right to do that for market
20 development purposes and their own competitive purposes that it is not say they will

*Pretoria
05 June 2007*

do it. Or, where they do it they have to come up explicitly and say we are all differing from the rate that the independent expert calculated.

ADV PETERSEN: Certainly that I understand but in the methodology which...

MR FERGUS: We are proposing...

ADV PETERSEN: Is being proposed in your submission which we have been discussing...

10

MR FERGUS: thats taken away...

ADV PETERSEN: It is...

MR FERGUS: Absolutely taken away...

ADV PETERSEN: That is a different process.

MR FERGUS: We are saying...

20 ADV PETERSEN: Got some common elements but it is different process.

Pretoria
05 June 2007

MR FERGUS: Absolutely and that the interchange rate is across Visa or MasterCard.

ADV PETERSEN: Yes.

MR FERGUS: Yes so it is for the banking activities in South Africa rather than are vertically through MasterCard or Visa separately.

10 ADV PETERSEN: Now, could I ask you this, in order to bring such a methodology into operation, would it be necessary to have it adopted by statute or competent regulation in order to overcome the effect of the card association rules?

MR FERGUS: Local regulation supercedes card association rules and there are numerous examples globally to that effect.

20 ADV PETERSEN: And as you sit there now, would you be able to identify which particular regulatory or statutory framework would be the appropriate one for the introduction of a new methodology?

MR FERGUS: We would not take that under advisement (**laugh**)..., we probably have ten different views here so we probably should take it under advisement. I

*Pretoria
05 June 2007*

mean the banks position if the question is about who should regulate it, the view would be that that is best done through SARB so that is consistent with the other regulation that the banks are subject to. So if that..., if the question was around where should the regulation sit that would seem the most appropriate place.

ADV PETERSEN: Now if we think ourselves into that context of the new methodology like this in operation, would..., should any room be left for bilateral setting?

10

MR FERGUS: Well I mean on a global stage there has always been room for bilateral setting. To my knowledge it has never ever been implemented due to the complexity of doing it in the four party state..., program where you got so many issuers and so many acquirers actually managing the bilaterals within that process is incredibly complex and you know when I have looked at this previously in other jurisdictions, the only way we have ever found who is doing it is with retrospective rebates and you incur all kinds of overheads in managing that. So you know

20 logically you would say yes, practically it is very difficult to envisage how it would operate.

*Pretoria
05 June 2007*

ADV PETERSEN: You have set out very extensively the benefits of a multilateral approach or that would apply also to a uniform approach in this case...

MR FERGUS: Yes...

ADV PETERSEN: That we were discussing. In your submission of the 10th of April on card interchange fees, page 31 paragraph 4.6.6 you add that “bilateral setting of interchange would also tend to undermine the important honour all cards rule in that,” and you have..., might refer to footnote 39. I quote, “the acquiring bank would have different merchant service charges depending on the identity of the issuing bank.”

MR FERGUS: That is all part of the same practical implementation problems that you come to with bilaterals.

ADV PETERSEN: You also give details on pages 66 to 68 of the cumbersome process which you have just been referring to but you also deal with the significant values to new entrants which are raised by the bilateral approach.

MR FERGUS: Yes.

ADV PETERSEN: In fact that is a development of your original submission of October last year, page 62 paragraph 4.2.6.5.7 which is headed “Disadvantages to small players and discouragement of new entrants.” You indicated there that if new entrants and/or small players cannot rely on a standard level of interchange then they will be faced with high cost of participation than big players.

10 MR FERGUS: Yes well this is a..., I mean credit cards is a volume game and so you are running small volumes, you have higher costs. If you have low negotiating skills., power and you know this is all theoretical. There is not a single case where a market has moved to bilaterals to prove whether this is correct or it is a risk rather than a reality.

ADV PETERSEN: You do say in your option one again which was referred to earlier that individual banks would still have the option to bilaterally and negotiate an independent rate between themselves.

20 MR FERGUS: Below the ceiling?

ADV PETERSEN: Below the ceiling?

*Pretoria
05 June 2007*

MR FERGUS: Yes below the ceiling. Definitely below the ceiling and I think if we did not make it clear in here, we definitely made it clear in our presentation.... at the last one, sorry.

ADV PETERSEN: Could you just explain why it might be beneficial to even leave that opening rather than just allow for the uniform rate to be adjusted at frequent intervals?

10 MR FERGUS: I think if we are brutally honest, it was because the Competition Act said the rates should be set by bilateral.

ADV PETERSEN: So that is four (indistinct)...

MR FERGUS: So I probably will be in trouble now for being brutally honest.

ADV PETERSEN: But if we were to for argument sake recommend a uniform system, would you be at all perturbed if we also recommended that no room should be left for bilateral.

20

MR FERGUS: Not at all.

ADV PETERSEN: I am quickly moving on to the No Surcharge Rule, in your Submission on Card Interchange Fees of the 10th of April, paragraph 1.3.2 that is on page 2, you refer to the No Surcharge Rule and you say in brackets “more appropriately referred to as the no differentiation rule” and you also used that description in your original submission on page 67. Again I am wishing to get complete clarity here...

10

MR FERGUS: Yes.

ADV PETERSEN: So that we can weigh this up. Do you not agree that in terms of cards scheme rules merchants are to be precluded from charging a higher price than the normal price or the ticket price but are not prevented from giving a discount for cash below that price?

MR FERGUS: Is there a practical difference?

ADV PETERSEN: Well are you asking me a rhetorical question, must I answer it?

20

MR FERGUS: I mean I am not sure there is a difference. You know, I mean retailers can obviously discount and do, I mean you know the motor trade is the best

*Pretoria
05 June 2007*

example I mean retailers do discount in negotiations but there is a price that they cannot charge above.

ADV PETERSEN: Yes, but it was argued to us earlier in these hearings that the escape route that the merchant has if the cost of accepting cards becomes too high, is to allow cash discount that that is not prohibited by the card association rules and that that escape route, that is my term, provides one of the safeguards...

10 MR FERGUS: Yes...

ADV PETERSEN: Against the abuse of any power that the card associations and their members might otherwise have over merchants.

MR FERGUS: No at a personal level this is one of the examples of where legislation in local jurisdictions has been introduced that says surcharging is allowed. My experience of it has been that it has been abused where it has being allowed. So if one is going to argue that you want to allow price differential...a discount for cash is
20 a much more fair basis than a surcharge for credit cards.

*Pretoria
05 June 2007*

ADV PETERSEN: I am not permitted because of confidentiality to read any of your standard merchant agreement but would you care to go to it, it is annexure 1 to your submission on acquiring of the 10th of April.

MR FERGUS: I can hardly see you I cannot see the writing,(laugh) I cannot see both.

ADV PETERSEN: I very much doubt if anything confidential about this so you can
10 allow me to read out the clauses...

MR FERGUS: Yes.

ADV PETERSEN: So it is 4.2 on the first page that struck me.

MR FERGUS: Yes.

ADV PETERSEN: May I read that out?

MR FERGUS: Yes sure.

20

ADV PETERSEN: “The merchant must supply goods and/or services to a cardholder at prices not greater than the merchant’s normal price.” So that seems to

*Pretoria
05 June 2007*

me to accord with a no surcharge rule in about the sense explained to us by the card associations but it is not a no differentiation rule, am I right?

MR FERGUS: That clause is definitely right, yes and I am not a lawyer.

ADV PETERSEN: No but there is nothing to stop your merchants giving a cash discount for cash, is that right?

MR FERGUS: No not on that clause.

10

ADV PETERSEN: Mr. Sinton is also confirming that is that...

MR SINTON: That is our understanding.

MR FERGUS: Yes.

ADV PETERSEN: I do not believe this is a freedom widely advertised to merchants.

MR FERGUS: I am not sure it is an activity that would be widely implemented by merchants.

20

ADV PETERSEN: Now in relation to the honour of cards rule, stick with the Submission on Acquiring, page 6, paragraph 6. The question that you were asked in

*Pretoria
05 June 2007*

question 6 was “Do you impose the honour of cards rule or the honour all products rule, please explain your answer” and you answered in 6.1 that “Standard Bank does honour the honour of cards rule which provides that if a merchants accepts an association brand, it must accept all cards that bears that brand. In other words if a merchants accepts MasterCard brand it must accept cards that bear the brand irrespective of the identity of the bank that issued the card or the type of card.”

10

MR FERGUS: Yes.

ADV PETERSEN: Debit, credit or cheque card...

MR FERGUS: Yes.

20

ADV PETERSEN: And then I want to go on to 6.2 just so that I put my question in the right context, Standard Bank does honour the all products rule which provides that a merchant may not discriminate between cards on the one hand and cash or cheque on the other. In other words the merchants may not charge a premium on a card transaction. In practice some merchants do encourage the use of particular payment forms. Now so far as the second of those paragraphs implies that the

*Pretoria
05 June 2007*

merchant cannot charge a lower price for cash, we have cleared that up in the earlier exchange but it does seem to me that you are presenting the honour all cards rule as identical with an honour all products rule.

10 MR FERGUS: I do not think so because we go on to say the in practice merchants do encourage the use of particular payment forms. I mean there is a number of merchants in South Africa that do not accept cheques. Hence what we are saying is as far as our agreement with them for cards, they cannot disadvantage the cardholder against other forms of payments. If they decide that they do not want to accept cheques that is their business decision and is not part of our agreements around cards. So I think in a literal sense there is a difference between honour of cards and honour of products but the one is if you are going to accept cards, you must accept all cards branded with that product. The other is you cannot disadvantage card holders against other forms of payment. Is that..., have I made it clear?

20 ADV PETERSEN: That..., allow me to come at this from a slightly different angle because I am really just trying to make sure that when terminology is used, we understand exactly what you mean.

Pretoria
05 June 2007

MR FERGUS: Maybe we need a glossary so that you and I understand the same...

ADV PETERSEN: The sense that, speaking for myself, I have had from the information on the card associations and their rules, is that the Honour All Products Rule does not apply to different means of payment. It is just an extended form of the Honour All Cards Rule to this effect that if I am a card association and I have signed you up as a merchant, I may tomorrow bring in a premium card under my existing brand which is much more expensive to the merchant, okay and the merchant must
10 honour that card. So there is no freedom of the merchant to accept certain products of my scheme and not other products of my scheme.

MR FERGUS: The association cannot stick in a product priced differently without there being...the product in the market and a cost study. So they cannot just introduce a product to price it differently, they have no powers to do that.

ADV PETERSEN: We have heard a complaint, I think it was during the Cape Town
20 hearing and I..., my memory is not good enough to say it was exactly that raised it, that we,...or it may have been in some other occasion that this rule this extended

*Pretoria
05 June 2007*

form of the Honour all Cards Rule involves some kind of abuse. I am interpreting your answer to be that that is not so...

MR FERGUS: I have no knowledge of that abuse and you know if we can find out what it is, I will happily deal with the issue. From Standard Bank's perspective, there has been no abuse of this rule at all.

ADV PETERSEN: And is there in fact a higher merchant service charge on premium cards?

MR FERGUS: No.

ADV PETERSEN: There is not?

MR FERGUS: No, no.

ADV PETERSEN: So there is no instance, I have not found one but you can tell me, there is no instance one can point to where something called the Honour All Products Rule has given rise to abuse.

MR FERGUS: Not that I am aware of at all.

*Pretoria
05 June 2007*

(Caucus)

MR FERGUS: If where premium cards have been introduced into the market, the difference in pricing is been to the cardholder. You get these extra benefits, the price is this?

ADV PETERSEN: Yes.

10 MR FERGUS: Not to the retailer and the cardholder makes a choice whether to take that product or not.

ADV PETERSEN: Thank you. Right cash back at the point of sale, in your original submission of October, page 57 paragraph and I say this for the record, 4.2.5.6.1.2.3. You referred to card association rules prohibiting pure cash back that is to say cash back without an accompanying purchase. Okay you repeat the point in your 10th of April 2007 Submission on Acquiring, page 32 paragraphs 45. As you understand it, is this still the position as far as both Visa and MasterCard are concerned?

20 MR FERGUS: In the international rules yes, but certainly in the case of MasterCard have given Standard Bank dispensation because of the unique nature of the rural

*Pretoria
05 June 2007*

communities in South Africa and some of the other African markets to take cash back there.

ADV PETERSEN: Because you have dealt fully with the social benefits of pure cash back transaction.

MR FERGUS: I mean it is under test at the moment. I would hate to say that it is in massive roll out because it is a complex situation as you can imagine.

10 ADV PETERSEN: So the answer then to my next question is presumably that you do permit your merchants to provide pure cash back at the point of sale?

MR FERGUS: Yes we are in test with it right now in rural areas but it is for specific needs in those areas where it is beyond certain distance from the nearest ATM.

ADV PETERSEN: Oh but then do you retain the restriction in other areas?

20 MR FERGUS: Well as far as I know yes. It is to meet the Charter targets. There are great problems and retailers are not really happy with pure cash back because it highlights they have lots of cash on the premises. So it is not an obvious thing that retailers want.

*Pretoria
05 June 2007*

ADV PETERSEN: Yes I understand but it is nevertheless a restriction which is being imposed on them whether they want it or not.

MR FERGUS: Okay, you know...

ADV PETERSEN: If it were not for the card association rules, would you permit your merchants to provide pure cash back at the point of sale generally? You do not need to answer now but please do if you are ready.

10 MR FERGUS: I think we will advise I am not sure...

ADV PETERSEN: Sorry did I miss...

MR SINTON: Sorry Mr. Petersen, no we will rather revert you in due course in answering that question.

CHAIRPERSON: I have another question related to that particular point. Has the situation changed with regard to mini ATM's as far as Standard Bank is concerned
20 because in your submission of 5 April, I think there was an indication that you have not rolled out any mini ATM's.

*Pretoria
05 June 2007*

MR FERGUS: We are currently partly appointing 20 now to make sure they work before we go to a broader rollout. So our strategy is to roll them, we are currently testing 20 of the...

CHAIRPERSON: You are currently testing 20?

MR FERGUS: Yes.

10 CHAIRPERSON: Did the concerns that you raised in the other submission relating to the legislative framework relating to mini ATM's, has that been taken care of?

MR FERGUS: I will need to take that under advisement and get back to you. I think we got conflicts (indistinct)...

CHAIRPERSON: Not really legislative, it was more...

MR FERGUS: Of the Charter...

20 CHAIRPERSON: Yes not really legislative, it was more of a PCH agreement problem

MR SINTON: Yes the issue was under which PCH agreement should the...

CHAIRPERSON: Right...

MR SINTON: The mini ATM be governed and that we have a dispute between Standard Bank and First National Bank on that issue.

CHAIRPERSON: So it has not been resolved?

MR SINTON: It has not been resolved, no.

10 CHAIRPERSON: Oh okay I just want to double check because when I was going through my notes, I picked up that there was that issue still outstanding.

MR FERGUS: I have an update on the current position...

MR SHUNMUGAM: Sorry Chair I think that was in dispute, the current intent in the industry is that a position has been taken, and they are busy investigating into what payment clearing house agreement that it would fall. So there are steps being taken in the industry, I think that there has been a strategic intent agreed and the
20 banks are now implementing.

MR FERGUS: Not fully resolved...

MR SHUNMUGAM: So it is not fully resolved.

CHAIRPERSON: It is not full resolved, okay.

ADV PETERSEN: Maestro debit cards, MasterCard debit card, in your submission on issuing part one of 10thn of April 2007 page 4, paragraph 4.2.1 you say that uniquely there is a per card fee paid on Maestro Cards to MasterCard. You say the same in your submission on acquiring, page 8 paragraphs 9.4. Now let me ask my question in two parts because the one...your answer may cancel out one of the other questions. If that is correct, do you know the reason for the fee which it seems to me would tend to discourage the issuing of debit cards as a per card fee but the second part of my question is, are you sure you do mean a per transaction fee instead of a tiered fee? I have to there refer you to the confidential volume, Volume 2 of issuing which you would be pleased to know I have actually worked through if I can find it..., you have part two with you?

20 MR SINTON: Is it an annexure?

*Pretoria
05 June 2007*

ADV PETERSEN: That is the annexure 5A which is..., I can tell you what it is. It is the MasterCard Consolidated Billing System for the SAMEA region of October 2005 and if you go to page 2-102 and there is a similar thing on page 2-107. You see in the middle, it is confidential this volume so I be careful how I put it to you. First of all I have not been able to find in this volume a reference to a per card fee. It may be that I read it too quickly. On the other hand I do find reference to “a per transaction fee” and I just wonder whether you are sure of the way you..., now in retrospect sure
10 of the way you put it earlier.

MR FERGUS: No there is a card fee that is paid quarterly for Maestro and in going back into the midst of time to when the Maestro scheme was established in the late 80's or early 90's, it was to develop and expand the acceptance and the knowledge of the brand and that is why it was uniquely added for the Maestro products but it is very small. It is not a material figure. We will tell you under advisement what the figure is but it is not in anyway material.

20 ADV PETERSEN: Could you just fill-in that little gab for us...

MR FERGUS: Will do.

*Pretoria
05 June 2007*

ADV PETERSEN: I will appreciate it.

MR FERGUS: It is tiny.

ADV PETERSEN: And then could you just go to..., just for completeness, could you go to annexure 5B which is bound in Volume 1. That is the Visa equivalent issuing Volume 1 paragraph 2.1.3...

MR SINTON: Sorry which page is it?

10

ADV PETERSEN: My pages are not numbered but it is paragraph 2.1.3.

MR FERGUS: The prints are getting smaller and smaller the deeper we get into the questions.

ADV PETERSEN: I read there that in a particular instance there is a per card fee.

MR FERGUS: Yes.

20

ADV PETERSEN: Correct?

MR FERGUS: Yes.

*Pretoria
05 June 2007*

ADV PETERSEN: So your general answer should be supplement, it is not entirely unique then in the case of the...

MR FERGUS: Well it is unique to MasterCard.

ADV PETERSEN: Well this is Visa.

MR FERGUS: Yes..., yes.

10 ADV PETERSEN: But on debit cards it is unique to MasterCard?

MR FERGUS: Yes.

ADV PETERSEN: White labeled cards, Issuing Part I, page 10 paragraph 15.1, you give a definition which I just quote if I may because it is helpful, “a white labeled card is a piece of plastic that is issued by a bank or a non-bank in this inter-operable in certain respects that is not association brand,” association being Visa or MasterCard in this context. Now in the rest of paragraph 15, part of which is
20 confidential, you seemed to say that the reason you do not issue white labeled cards is the restriction in terms of the debit and credit card PCH agreements, have I misunderstood you?

*Pretoria
05 June 2007*

MR FERGUS: That is not the reason that is a limitation. The reason we do not issue them is economic. If you issue cards you have got the same costs in running the account. If you issue cards with very limited acceptance which you have got in white labeled schemes, you do not get the activity, you do not get the revenues but you have got the same costs. So it is an economic decision, not one that is restricted by the regulations.

10

ADV PETERSEN: But if in.... it would seem to be an unlikely event given what you are saying, the economic cost benefit analysis were to be different for a particular institution. They would be precluded from issuing white labeled cards by the restriction in the PCH agreements, is that right?

20

MR FERGUS: Okay do you want to give the answer? Okay the advice I am being given is to the restriction is to ensure the proper rules and regulations are in place and to manage disputes, charge backs, disagreements between the parties and once that is done then agreement would be given to the scheme going ahead.

ADV PETERSEN: But that is..., it would seem if I am understanding correctly that that is being managed by way of a compulsory membership of the card association.

*Pretoria
05 June 2007*

MR FERGUS: No, no that a local association can be formed that once there is acceptance that there are proper rules and regulations in place to govern the scheme and to protect the merchant and cardholder in the transaction.

ADV PETERSEN: Would that require a new PCH?

MR FERGUS: More than likely. I mean there are examples of this, I will use RCS as an example of a closed scheme or labeled scheme that has gone through the
10 process.

ADV PETERSEN: Okay very deeper into the fine print, it is in your acquiring submission, 10th of April page 35. Now there is a table there which is confidential, I just want to get your assistance interpreting the categories.

MR FERGUS: Yes?

ADV PETERSEN: It maybe safer if I can just give the column headings. The table
20 is about the value of transactions, then divided into on-us and off-us and then there is a total. I would imagine that on us would be the same figures whether one has approaching it from an issuing or acquiring perspective?

*Pretoria
05 June 2007*

MR FERGUS: Yes it is our card and our merchants...

ADV PETERSEN: Fine but the “off-us” figures being given here...

MR FERGUS: Yes?

ADV PETERSEN: Am I right in thinking that the values here are given from an acquiring perspective...

10 MR FERGUS: No, no our cards used..., no sorry these are..., this is not our cards and our merchants.

ADV PETERSEN: So it is “of-us” from an acquiring perspective?

MR FERGUS: Yes.

ADV PETERSEN: I know you used a more complicated terminology for “off-us” but it is okay if I...

20 MR FERGUS: Yes.

ADV PETERSEN: It is from an acquiring perspective.

MR FERGUS: Yes.

MR SINTON: Yes.

ADV PETERSEN: And accordingly the totals would be as well then. On page 36 of the same document the next page, answer to question 52. Again a confidential table, is the column heading “gross commission,” the same as gross revenue from merchant service charges, is that what it mean? Gross commission is...

10

MR FERGUS: Yes...

MR ENGELBRECHT: Sorry Mr. Petersen just the page?

ADV PETERSEN: Okay page 36...

MR ENGELBRECHT: Okay.

ADV PETERSEN: Acquiring volume, there is a table at the foot of the page...

20

MR ENGELBRECHT: It is a combination of the “on-us” and not on-us.

ADV PETERSEN: Yes?

MR FERGUS: It relates to the merchant's discounts...

MR SINTON: The total discount fee, yes.

ADV PETERSEN: Yes so in other words commission here is the same as what somebody else might call MSC, is that right?

MR SINTON: Yes.

10 ADV PETERSEN: Okay and here is my last one positively on page 37, to whom are the respective fees indicated in that table charged?

MR FERGUS: To the issuer.

ADV PETERSEN: Wait a minute; this is your transaction fee income.

MR FERGUS: This is the transaction fee that the acquirer receives for passing through these transactions to the issuer.

20 ADV PETERSEN: So acquirers...

MR FERGUS: Yes...

ADV PETERSEN: Transaction fee income?

MR FERGUS: Yes.

ADV PETERSEN: From the issuer?

MR FERGUS: It is when you move outside of the four party model.

ADV PETERSEN: Okay thank you very much.

10 CHAIRPERSON: Thank you.

MS NYASULU: Mr. Sinton and team my..., you do not need any fine print for my questions. I am just going to go for the broad principals. Just to check some..., what I perceived as slight inconsistencies but just to make sure that I understand quite clearly. Just on the issue of interchange, the need for interchange and the whole concept of the two sided market which is really what all the banks have used as motivation for the interchange fee. I just need to understand a few things, if you look
20 at page 24 of your April 10 document...

MR FERGUS: On issuing?

MS NYASULU: On...

MR FERGUS: Interchange...

MS NYASULU: In...1.4 and again it says a market is considered to be two sided if it has the following features and I am gonna read them, one “it needs to have a joint demand. A product or service has two distinct sets of customers who must both demand the product or service in order for a transaction to occur. The joint demand
10 and in the case of card payments systems the two sets of customers are cardholders and merchants.” And then in 4.4.4.2 one of the other features is “it should have the indirect network externalities.”

“The service exhibits indirect network externalities whereby the value of the service to one group of consumers is dependant on the number of consumers on the other side of the market and that leads us to therefore the need for the presence of an intermediary.” If I could ask a question because I really, I go through periods when I
20 think I understand this two sided markets and then something comes up which confuses me. Do all two sided markets need an intermediary? Bearing in mind the features that I have read out as per you definition of the two sided market?

*Pretoria
05 June 2007*

MR HODGE: Look I think the presence of..., you know in a three party model there is someone who produces for both sides. In the four party there is a transfer from one side to the other so how that is facilitated might be more formalised or less formalised but the specific intermediary producing both sides is probably an incorrect characterisation as it was put here.

10 MS NYASULU: Let me give you an example of what I see as a two sided market and knowing me, I probably got it completely wrong but if I use the definition that has been used of a two sided market which says, you know one side needs the other probably equally. One that strikes me as a two sided market but I am battling to see where the intermediary sits and where an interchange fee, if we use the terms we have said, is cars, automobiles and filling stations because even in that example, as far as I am concerned, you have a two sided market. You know and your chicken and egg comes into play, you need to have cars in order for there to be filling stations and we still do not know which one comes first. Now I am battling to see how that two

20 sided market works without an intermediary and why here there needs to be an intermediary simply because it is a two sided market.

*Pretoria
05 June 2007*

MR FERGUS: Well one can argue the petrol company is intermediary.

MS NYASULU: And then explain to me where the fee is then transferred from one to the other in that example. I will tell you why I am asking those questions in a few minutes.

MR FERGUS: The payment from the garage proprietor of that service station proprietor to the oil industry.

10 MR HODGE: But I do not think this is..., I mean that is a two side market. Petrol is in the input, you need it for cars. It is the derived demand that comes from selling cars. I think the point of the two sided market is that you are selling the same product to both sides. You are selling it to the merchant to get acceptance in the selling to the cardholder to use the card as well. So transactions can only take place if they both purchase the product or purchase into the system.

20 MS NYASULU: Sounds exactly the same to me. You are selling to both markets in that situation exactly, you are selling to the people who need the cars and you are selling to the filling stations, you have the merchants in this instance.

*Pretoria
05 June 2007*

MR HODGE: But you are not selling the same product, the same system, you are selling to the consumers a car and a petrol seller..., stations selling petrol.

MS NYASULU: Okay let us just leave it at that for a while. Let me ask you a different question and if you go to page 54 of the same submission I think, I hope..., just make sure first. Now this is the October submission. The blue one, the 27 October submission which is I suspect confidential. So I am going to refer you to page 54 of that 4.2 on 4.3. Are you with me on that?

10

MR FERGUS: Yes.

MS NYASULU: I think the whole document was confidential if I am not mistaken, so is 4.2.4.3 something that you would want to read out?

MR FERGUS: It is not confidential.

MS NYASULU: Is it not confidential? Okay in trying to understand the role of interchange in this two sided market, I am trying to understand whether that fee is there to balance the two markets as has been said or whether it is really just a fee to

20

compensate one, in other words to compensate the issuer for cost in the issuing business.

MR FERGUS: It is to balance the value between the participants in the scheme. It is not actually intended to do anything else. It is to say you have a scheme and you have a disproportion of allocation of the costs and the value in the scheme in its natural stage and therefore you need an adjustment that says this balances that value between the participants and you know, it is not actually trying to do anything else other than that. So it is some cost but it is also some value. Yes so in some cases it is actual cost in some cases it is cost substitution. So there is a value to the merchant, there is a value to the cardholder. You know the issuer out of the parties is paying a disproportionate amount towards facilitating the activity. You know because of the very nature of how it operates and interchanges the balancing mechanism between the participants.

MS NYASULU: In other words when you talk about the fact that the issuer markets to the general public, accesses the credit and makes the credit decisions issues and

*Pretoria
05 June 2007*

reissues the card services and maintains the cardholder base, all of those activities, interchanges is not just meant to help the issuer recoup those charges?

MR FERGUS: No it is..., in the pure economic argument for any interchange it says, if you did not have credit cards the merchant to get these sales would have to run a credit book and run all the risks of doing that. By having the credit card that cost is substituted and then therefore there should be a correction. So it is balancing the value the merchant gets from getting the sales to the cost of running the end to end process.

10

MS NYASULU: Okay, if we just go to the same, the April 10 submission, the one on the card interchange fees, page 31, item 4.6.6. Just also need to understand the point and the footnote that Advocate Petersen read out. You are arguing that bilateral setting of interchange fees would lead to a discrimination against smaller banks...

MR FERGUS: Yes.

20

MS NYASULU: By the large..., the large banks.

MR FERGUS: We are saying there could be a higher cost for small players. I mean this has not happened anywhere in the world so there is not evidence to support it.

We are saying the risk is that as in any negotiation, the bigger you are the more negotiating power you have and therefore the cost still remains. So if Standard Bank is getting a discount, a small bank can end up having to pay more. I just think that is economic power in the market place.

10 MS NYASULU: Can I just explore that because if there was real competition in the market place, is it not conceivable that Bank A, large Bank A could charge a smaller bank higher but large Bank B could therefore charge it much lower to position itself a bit more positively in the market?

MR FERGUS: Look here, I mean, you know, I cannot argue with your supposition because there is no evidence one way or the other.

MS NYASULU: I am just arguing with your supposition.

20 MR FERGUS: What we are saying is there is a risk of this happening in most economic negotiations. The bigger you are the cheaper the price and therefore if you

move away from interchange, you have a risk that the costs will go up for the smaller banks, which I think is a very real risk.

MS NYASULU: And I am saying there is enough mitigation in a market that operates competitively to actually work against that unless, and I am not suggesting there is, unless there was collusion and all the big banks decided to charge the smaller ones...

10 MR FERGUS: Yes if we...

MS NYASULU: Which I doubt would happen.

MR FERGUS: Have a choice between partnering with a partner that is three times bigger than the small one, we are going to charge the small one more than we charge the big one. That is just the reality. That is what is going to happen. Now you know Nedbank may come along and say "we will charge slightly less than Standard Bank" but they are still going to charge more for the small bank than that they would for the
20 bigger bank.

MS NYASULU: Thank you.

CHAIRPERSON: Earlier on...

MR HODGE: Sorry maybe just to add to that, I think the footnote refers to if you are acquiring and a customer comes with say a Standard Bank card then that small bank still has to interact with Standard Bank. So the relevant charge is still the charge that a large bank in that case may charge a small bank whether the acquirer is a small bank or in a large bank. So that is where the differentiation would affect their ability in competing for acquiring business.

10

MS NYASULU: Thank you.

CHAIRPERSON: Alright, earlier on I asked about the mini ATM's, I just want to know have you entered into any bilateral agreements with any of the other banks relating to mini ATM's?

MR SHUNMUGAM: Chair we do have a bilateral agreement with one of the banks on mini ATM's.

20

CHAIRPERSON: Will that have been then notwithstanding your concern about the regulatory issues you referred to?

*Pretoria
05 June 2007*

MR SHUNMUGAM: Yes I mean the regulatory issues were basically been handled in the inter bank arena and notwithstanding that we had to enter into a bilateral agreement for the fee.

MR FERGUS: It was to facilitate the trial) just to get us out and learning about what is going on. It is not the preferred route.

CHAIRPERSON: Well I am just asking whether..., with that particular bank which
10 is rolling out mini ATM's. You signed a bilateral agreement with them that was my understanding.

MR SHUNMUGAM: Yes we have. Notwithstanding the risks that exist currently in the industry.

CHAIRPERSON: Okay.

MR FERGUS: I mean it is so new, we are having to do things to get the experience
20 to work out what we should do going forward. So it is..., you know how do we get the experience if we do not make any agreements if we cannot get agreement in the industry. It's the chicken and egg again.

*Pretoria
05 June 2007*

CHAIRPERSON: Any more questions?

MS NYASULU: No.

CHAIRPERSON: Okay thank you. Thank you for coming, we will then adjourn for lunch. We will start with Ms Meijer after lunch. We start at 14:00.

(Lunch Break)

On Resumption:

10

CHAIRPERSON: Alright then, Ms Meijer we are going to resume with the legal arguments. I know we are going to move into Canada but I know Ms Nyasulu had some questions for you before we move on to Canada. The one aspect I am going to ask you to also look at..., maybe you can address it at some stage during your argument is basically why should we not regard the “off-us” transactions in ATM’s as or even in other transactions as not being an allocation of customers as anticipated in section 4(1)(b) from Roman letter two. It is a legal point, we try and look into...,

20

because I know you seemed to be only concentrating of price fixing but there is the

*Pretoria
05 June 2007*

other issue relating the allocation of customers, Section 4(1)(b) from Roman letter two.

MS MEIJER: I think the arguments in terms of approach to the section apply equally to all of the subsections of Section 4(1)(b) and I will address you with regard to whether or not there has been market division with regard to ATM but if it would be acceptable to you, could I do that at the end?

10 CHAIRPERSON: No that is fine. That is why I am just raising it now so that you can think about it and then maybe you can address it with us at some stage here because basically the way the entire transaction unfolds, those are the queries we have as to whether is this not allocation of customers. Okay let us proceed then.

MS NYASULU: Sorry I had a very quick question and it related to your slide 8 on the “risk of error.” I was just trying to understand because you used the analogy of error number or type one error versus type two error, are you then arguing for the fact
20 that it is better to rather let a guilty person go free than to ensnare an innocent person. I mean taking into consideration the fact that we are using that as an analogy, are you

*Pretoria
05 June 2007*

saying it is better to let an anticompetitive behaviour go unsanctioned if the opposite risk is actually stopping behaviour which is not necessarily....?

10 MS MEIJER: I think our approach is that it is equally important so that if your only focus is on catching the guilty person and you do that at all cost and you ensnare in the net, a whole lot of innocent people that that outcome is just as..., that as a cause a serious outcome but we say it is equally serious to..., you know we are saying that both types of error are equally important particularly in the context of the Competition Law and that this Act needs to be interpreted in a way that is consistent with its purpose which is to prevent playing the anticompetitive behaviour but at the same time which prevents what we would say is an equally serious consequence which is to prevent efficiency enhancing or pro competitive behaviour. So I do not think we are giving more weight to the one or for the other.

20 MS NYASULU: Okay you see my problem is precisely that because if you bundle and it is not just you doing that in fact the Act itself does exactly that. It bundles efficiency enhancing with pro competitive. Now is it your view that necessarily what is efficiency enhancing is by implication pro competitive and I want to take you back

*Pretoria
05 June 2007*

to the examples that you used with the sharing of warehousing facilities although I can see in that example that that would be efficiency enhancing it is not necessarily pro competitive.

MS MEIJER: I do not think that the terms are the same where I have used them. I think I have intended to say either efficiency enhancing or pro competitive and then that either outcome would be something desirable for our economy and that you would want to be careful to prohibit those *per se* without any consideration of the conduct and its purpose and its consequences.

MS NYASULU: Okay and just finally just so that I understand you, would you say even when it was quite obvious that the effect of an arrangement between two competitors was going to be anticompetitive that it would still be necessary to go through the whole process of coming to a conclusion about the purpose of that arrangement and the intent?

MS MEIJER: If there is no effect other than an anticompetitive effect, then that may well be sufficient and that would be conduct that over time, you know, I think if the only possible effect is anticompetitive then you would not necessarily need to look

Pretoria
05 June 2007

into the purpose that the parties had in entering into it. I think the reason for looking at the purpose is that the parties is..., if the parties had a pro competitive purpose and it is apparent that in fact or that they had an efficiency enhancing purpose or even just a genuine legitimate business purpose which happens to have an anticompetitive effect, then considerably more care needs to be taken in analysing it and particularly so if on the face of it, there is arguably..., there are arguably efficiencies or pro competitive gains that are achieved.

10

MS NYASULU: So just to summarise trying to understand you, you are saying even though the effect has been proved to be anticompetitive, you would not necessarily find the arrangement to be an arrangement that should be discouraged even if the..., let us assume the purpose of the arrangement was quite innocent but the effect is actually not good for the market, you would still argue that the effect alone is not sufficient.

20

MS MEIJER: I mean I think in those circumstances you would tend to analyse under 4(1)(a) but I just want to go back to saying if the arrangement is clearly a naked restraint and it has no, you know it is anticompetitive and it has nothing to commend

*Pretoria
05 June 2007*

it, you know and the parties cannot put forward any reason why the conduct would be efficiency enhancing or potentially pro competitive or any satisfactory explanation at all, then that should be *per se* prohibited.

MS NYASULU: Okay let me remind you again of your... the example of the case that you read with the warehousing. Clearly when two competitors decide to share facilities and it is quite obvious that there were efficiency enhancing reasons why they did it. So we have to assume the reasons for doing it were innocent enough. The effect though could quite possibly be that another competitor who does not have..., let us just assume for that example that there were only three people in that market, three companies. The fact that the two have already joined forces to extract these efficiencies and excluded the third one who now no longer has the opportunity to join up with another one to share those efficiencies, the effect of that has become anticompetitive because this third one does not have the ability to extract the economies of scale and the efficiencies that the other two have. Even though the intent and their purpose for doing it had nothing to do with the third person and who was purely innocent.

Pretoria
05 June 2007

MS MEIJER: I think the question is, you know in that same example they could have been no anticompetitive effect other than the fact that competitors had agreed or potential competitors even in this case, had agreed that you know the one would not sell certain products and neither would the other. In other words, that they would not compete in relation to their product lines. Potentially that has no anticompetitive effect...

10

MS NYASULU: Absolutely I agree.

20

MS MEIJER: And I think our approach to Section 4 is to say that when faced with particular conduct that may fall within the ambit of the section, the competition authority in order not to make an error in circumstances where its *onus* of proof is very low and in fact in order that it may not commonly make errors, it needs to pause and say “is this the kind of conduct that intuitively is wrong that on the face of it as a naked restraint, there is nothing there that could potentially justify the conduct.” If that is the case it can *per se* prohibit it. If the parties can demonstrate a purpose in entering into the arrangement that that is a normal business purpose that potentially makes sense in the context of, you know the market in which they operate, the fact

Pretoria
05 June 2007

that there may have been some anticompetitive effect should not be enough to say, well you know we condemn it. We are saying that in those circumstances a more detailed level of inquiry needs to be undertaken.

MS NYASULU: Thank you.

CHAIRPERSON: Alright you may then proceed with your submission on the Canadian Law.

10 MS MEIJER: Yes and if I can just qualify this by saying that I am not by any means an expert on any of this foreign law but I have taken some reasonable steps within my budget in order to verify the information that I have gathered for you. In relation to Canada which, as the Chair pointed out last time, was in large you know, in large part our Act was based on the Canadian Law but in relation to the *per se* prohibitions, there are some fairly significant distinctions in terms of how Canadian Law operates and our law operates. They have two *per se* prohibitions. The first is in Section 47 of
20 the Canadian Act and it is a *per se* prohibition on bid rigging where the agreement or arrangement was not made known to the person calling for the bid and it is my understanding that the intention behind that was to avoid joint ventures from being

Pretoria
05 June 2007

caught within the ambit of this prohibition. The second prohibition which is contained in Section 49 of the Canadian Competition Act, prohibits banks or federal financial institutions from reaching an agreement or arrangement in respect of a series of different interest rates and charges to customers.

10 You will notice that in that list inter bank fees are not included so that this is again..., it..., this is an instance where it is..., the interest rates or end user pricing that is *per se* prohibited and as with Section 47, Section 49 does not apply if the customer had knowledge of the agreement between the banks. In prosecuting under this section the authorities have to simply show that there was an intention to enter into the agreement and that..., yes essentially that there was an intention to enter into this agreement which is a bid rigging agreement or which has the effect of setting interest rates or bank charges?

20 So there needs to be no proof of anticompetitive effect so that this is truly a *per se* prohibition but in a number of respects different from ours and in particular I want to highlight how specific the *per se* prohibitions are in relation to the conduct that is prohibited. Price fixing and market division and other arrangements, which would not

Pretoria
05 June 2007

fall under either Section 47 or 49, are dealt with under Section 45(1) of the Canadian Competition Act and it prohibits anyone who conspires, combines, agrees or arranges with another person to prevent or lessen unduly, and this is an important concept, unduly, competition in the production manufacture et cetera of a product. This is generally referred to in Canada as a partial rule of reason in that in order for the state to be successful in a prosecution under this section, it has got to show that there has been a undue restriction on competition but it does not allow any kind of full blown
10 discussion of economic advantages and disadvantages as one would expect in a normal rule of reason analysis.

So price fixing would be prohibited under Section 45(1) and that would apply both to the kind of naked cartel that I have described and potentially joint ventures can also fall within this prohibition. The leading case and as I mentioned to you earlier there have not been that many cases in Canada, is R vs Nova Scotia Pharmaceutical Society and the reference is (1992) 2 S.C.R. 606.

20 ADV. PETERSEN: Sorry just before you go further, when you say that the Canadian Partial Rule of Reason Test as you describe it does not allow a full blown discussion

Pretoria
05 June 2007

on economic advantages and disadvantages, is that the way that is has been interpreted?

MS MEIJER: Yes.

ADV. PETERSEN: That is not your..., simply your construction?

MS MEIJER: No that is the way that it has been interpreted and if you read the case that I have just cited, there is I think a fairly clear explanation which I am going to run through...

10

ADV PETERSEN: Thank you...

MS MEIJER: In point form of how “undue” is approached under their law.

CHAIRPERSON: Can you give us the citation again, 1992?

MS MEIJER: (1992) 2 S.C.R 606.

CHAIRPERSON: Okay.

20

MS MEIJER: And if you have difficulty in locating this kind of material I am happy to make copies available to you.

*Pretoria
05 June 2007*

CHAIRPERSON: Okay.

MS MEIJER: What Section 45 (1)(c) requires, is proof that there is an agreement that was entered into by the accused and I think similar to the EC Treaty. In fact this agreement need not be as between competitors and there needs to be proof of an undue prevention or lessening of competition flowing from the agreement and the way that the court has interpreted “unduly,” is essentially to say it is a term that denotes “a sense of seriousness”. It is something that is not trivial.

10

The only relevant issue is whether the agreement impairs competition to the extent that it will attract liability. Factors such as the private gains of the parties to the agreement and countervailing efficiencies lie outside of the enquiry and the two key features are; number one, the structure of the market and number two, the behaviour of the parties to the agreement. And in analysing the structure of the market, the court in R vs Nova Scotia said that the aim of that analysis is to ascertain the degree of market power the parties that entered into the agreements hold and many factors other than market share are relevant in this enquiry and they are all the normal kinds

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Pretoria
05 June 2007

of factors that would be taken into account in South African Law in deciding whether or not a firm has market power.

10 Interestingly in R vs Nova Scotia it indicated that parliament and I thought it was quite a strange choice of words but that parliament intended it to apply..., that parliament had not intended Section 45(1)(c) to apply in the absence of at least a moderate amount of market power but that it was not necessary to show that the firm had overwhelming market power or the ability to control prices, that this was some lesser test than that. The behaviour of the firms focuses primarily on the object of the agreement but other factors maybe relevant for example, you know, how the agreement has been carried out whether there is any other behaviour that tends to reduce competition or limit entry.

20 So it is the combination of the market structure and the behaviour which together would lead to a conclusion or could lead to a conclusion of an undue restriction on competition. Section 45 does have a mensural element which is divided into, and the case states this explicitly, into both a subjective and objective elements. The subjective being the people..., the..., you know the individuals who entered into the

*Pretoria
05 June 2007*

agreement must have subjectively had the intention to enter into that agreement. The objective element is a broader one which is more like reasonable man on the omnibus and the question is whether a person in ordinary commerce entering into that agreement would have realised that it would be likely to lessen competition unduly.

So that is sort of a brief overview of the Canadian approach and to highlight before I move on to Australia, there is this very narrow category of *per se* probations which are clearly defined and which do not apply if the person on the receiving end of the practice was aware of it. And all other price fixing and you know arrangements like interchange would as I understand this Act, be dealt with in terms of a partial rule of reason where there would have to be this demonstration of an undue restriction and a undue prevention or lessening of competition in order to be successful.

And I think these factors that are taken into account do significantly reduce the possibility, you know because there is this enquiry and because there are only very limited categories that can be prohibited outright. There is significantly less chance under the Canadian approach of catching in the net arrangements that are efficiency enhancing or pro competitive.

Pretoria
05 June 2007

The Australian Law is set out in an enormous piece of legislation known as the Trade Practices Act and here the relevant provision is Section 45 and it is a very difficult section to read. So that I have paraphrased it in a manner which I hope you see appropriate sense but it prescribes the making of giving or giving effect to a provision in a contract arrangement or understanding that has the purpose effect or likely effect of substantially lessening competition.

10 So this is not a *per se* prohibition. Again I think this is a partial rule of reason analysis but Section 45(a)(i) deems agreements that fix, maintain or control prices to have this effect. So that in a sense that is a *per se* prohibition and all that you would have to demonstrate in order to come right under that prohibition is that the parties to the agreement are competitors or would have been but for the agreement that the conduct relates to goods or services supplied in competition with each other and that the conduct has the purpose or is likely to have the effect of fixing, controlling or maintaining prices and having shown the purpose then there is the..., it is deemed to

20 have had the effect.

Pretoria
05 June 2007

That is as I understand the provision. This *per se* prohibition on price fixing, I think in much the same way as it has in South Africa was cause for and has been over for many years, cause for considerable concern in Australia and the particular concern was that it was impacting on ordinary joint venture arrangements that ought not to have been included in this net. Initially there was a Section 45(a)(ii) which was... which provided for very limited exemptions for only particular types of conduct undertaken by joint ventures and it was in particular where they had pooled their

10 assets in order to conduct joint activity that they were entitle to these exemptions. But more boarder collaborative arrangements of the kind that one would find in innovative industries like the banking sector and like communications, could not qualify for exemption under that provision. And as a result of these concerns a committee which I suspect was not that different to this panel was asked to look into the Competition Act and whether or not it was achieving its objectives and it was a very broad enquiry not only into this aspect.

20 And that committee concluded that joint ventures may very well be pro competitive in particular when they may result in the development of new products or may produce products..., existing products more efficiently and that the public benefits

Pretoria
05 June 2007

may very well outweigh any detriment to consumer that might arise from price fixing in the context of those joint ventures.

And they believed that the exemption that existed was too narrow as it did, as I mentioned earlier, primarily relate to the pooling of resources to produce or supply products jointly and as a result a new Section 76 (d) has just been inserted into the Australian Competition Act and I understand that that was effective from January of this year and it creates a complete defence for price fixing and also for certain other practices butt I have focused on price fixing for the purposes of a joint venture.

If it does not..., if it is not likely to have the effect of substantially lessening of competition so that it essentially subjects those arrangements to a type of rule of reason analysis and if I can just go back two slides, a joint venture is defined very broadly in the Australian and Canadian Act to include an activity in trade commerce carried on jointly by two or more persons or carried on by a body corporate formed by then to carry on that activity jointly. So it is considered quite a wide definition but there has as yet been no case law to consider..., you know, just what would constitute a joint activity and as I sit here I cannot offer a view on whether interchange

*Pretoria
05 June 2007*

arrangements would be considered to be this type of joint activity or not although it is certainly not beyond the realms of possibility that they would be.

ADV. PETERSEN: Could I just interrupt you there and pickup on a question that was asked earlier by Mrs. Nyasulu and it is something that troubles me both with the Australian example you have given and the Canadian. Now if you just look at our Section 4(1)(a) and now we are not dealing with a *per se* prohibition here, we are dealing with a full rule of reason analysis to use the American expression. “The agreement would be prohibited if it has the effect of substantially preventing or lessening competition in the market unless a party to the agreement et cetera can prove that any technological efficiency or other pro competitive gain resulting from it outweighs that effect.”

Now on the face of it, the legislature is saying to us that a technological or efficiency gain is to be considered a type of pro competitive gain because of that word other or other pro competitive gain, so then what is the substantial preventing or lessening of competition that precedes the rest of the analysis and it comes up again..., it comes up in your Australian statute and the Canadian one. Are we talking about on the one side

Pretoria
05 June 2007

of the balance and it is enough if one can show that there is a significant weight on the one side of the balance, on the negative side and then we can stop, I am talking about the Canadian and Australian partial rule of reason analysis or are they talking about the net effect on competition once both side of the balance have been tested.

MS MEIJER: My understanding is that they look only at the first part.

ADV. PETERSEN: But is that rational?

10 MS MEIJER: It falls short of a full blown rule of reason analysis which I think is what our Act proposes so that it says on the face of it, agreements like price fixing would generally not be favoured by competition authority but it also says that there may well be circumstances where those agreements are potentially pro competitive and so in the context of both of these Acts, you have to show once the authority has shown the lessening of competition then is not open to the parties to say, “Well we can weigh against that” or kinds of other practices.

20 ADV. PETERSEN: But is that not classic type one error because on the full analysis, it might turn out that the positive side was far more important than the negative side

*Pretoria
05 June 2007*

and so...but the inquiry has stopped and the positive side is not allowed to be demonstrated.

MS MEIJER: I think it allows..., it does it..., I mean it is quite possible that a type one error would be made under either of these provisions and in fact I think the amendments relating to joint ventures in Australia specifically recognise that and they have chosen to deal with it by specific exemption for joint ventures rather than amending Section 45 but I do think that the fact that the authority has to at least show
10 in the one case an undue lessening of competition in the other they have to show purpose effect or likely effect of substantially lessening competition. That substantially reduces the likelihood of making a type one error.

ADV. PETERSEN: Yes but again it is perhaps an interpretation problem. It maybe a policy problem but again is one considering only one side of the balance or both sides of the balance in order to get to a conclusion of an effect or likely effect of
20 substantially lessening?

MS MEIJER: I mean it explicitly considers only one side of that balance which is if they can demonstrate the lessening of competition then they are entitled to succeed.

*Pretoria
05 June 2007*

ADV PETERSEN: To the extent that we may have the privilege of being able to suggest changes to legislation, would it not make more sense in terms of the avoidance of both type one and type two errors, in other words catching the guilty and not catching the innocent, to structure it rather in terms of *onus* so that the prosecution discharges its burden if it can show either purpose or an effect or likely effect on the one side of the balance and then the defence can succeed, if it can fill the other side of the balance sufficiently to outweigh that. So that purpose would be sufficient for a *per se* and then in an extended or what a partial rule of reason effects on the one side of the balance would be sufficient to shift the *onus* on to the defence to prove the pro competitive features of the agreement, would that not be a way of both maintaining the necessarily simplicity of prosecution in appropriate cases with the safeguards against inappropriate convictions?

MS MEIJER: Are you suggesting an amendment where there would be one prohibition as opposed to our (a) and (b) as hypothetically, where there would be one section prohibiting restrictive practices and that in that context you would have different *onus*es as you described?

Pretoria
05 June 2007

ADV. PETERSEN: Well a question more than a suggestion but not a wish to do away with the *per se* element which may be capable of being a criteria which may be capable of being satisfied by a quick look in certain cases but to relieve the competition authorities when you are prosecuting under these circumstances of having to go any further in a more complicated case than having to show effects on the negative side of the balance. Perhaps that is there already in the section, I do not know.

10

MS MEIJER: My view is that it is. I think it..., I mean my view is that is that Section 4(1)(b) can be interpreted in a way that it impacts, you know only on the naked type of restraint and that to the extent that there are arrangements that may well be efficiency enhancing or pro competitive, they can then fall under 4(1)(a) and then those *onus*es that you referred to are already there.

20

ADV. PETERSEN: But just let me pursue that a little bit further because if it is already all catered for by the section, then it is just a matter of interpretation. In 4(1)(a) as it stands, the burden on the prosecution, you know what I mean by that in precise expression, the burden on the prosecution is only to show the negative side.

Pretoria
05 June 2007

It is as it is, then the *onus* shifts to fall in the positive side. Right so the..., if there is no positive side capable of being filled in or it is inadequate then one has a partial rule of reason even in the application of section 4(1)(a).

MS MEIJER: Correct.

ADV. PETERSEN: So then do we need to bring effects into 4(1)(b) at all?

10 MS MEIJER: Would you then posit a situation where in 4(1)(b) you would only look at purpose?

ADV. PETERSEN: Yes with that little logical detour that I raised this morning that if the..., if just on looking at it, you can see that this would have anticompetitive effects and that is so obvious that it must go to the purpose that therefore that must have been the purpose in the beginning and you can use that as a way of getting to purpose but nevertheless that the inquiry under 4(1)(b), should essentially be an inquiry about purpose.

20 MS MEIJER: I think it is a clean..., it would be a clean approach in a sense where you would say that and I mean certainly if one looks at other jurisdictions purpose

plays a very important role. So that if you were to approach 4(1)(b) on the basis that the primary inquiry was purpose that effects maybe relevant to the extent that they show purpose. I think that is quite seductive but I would be concerned to leave out of it effects all together except to the extent that they show purpose.

ADV. PETERSEN: But why? Are you not creeping into 4(1)(a) then?

MS MEIJER: Because this is simply a high level..., it is a high level inquiry into
10 effect and that if something plausibly might have a positive effect, it does not need to be established that it definitely does have that effect and that would then shift it into 4(1)(a).

ADV. PETERSEN: I think you agreed this morning with reference to the European Article 80...

MS MEIJER: One...

ADV. PETERSEN: (1)(1) that if purpose is shown that is enough, does not have to
20 go further. Is that not also the case in what you have given us in relation to Australia?

Pretoria
05 June 2007

MS MEIJER: It is the case in relation to price fixing in it.

ADV. PETERSEN: So if I am the prosecutor and I can show purpose I do not have to go further?

MS MEIJER: Correct.

ADV. PETERSEN: Alright in relation to Canada?

10 MS MEIJER: In relation to Canada for the *per se* prohibitions that limited category, you only have to show purpose but for price fixing there you would have to show undue lessening of competition.

ADV. PETERSEN: As well?

MS MEIJER: Yes.

ADV. PETERSEN: Okay thank you.

20 MS MEIJER: In Australia and I know that to some extent exemption is not directly relevant to the issues that we discussing, but I do think in the broader context, exemption is relevant and Section 88 of the Australian Act gives the Commission

Pretoria
05 June 2007

power to grant authorisation for all of the arrangements but including price fixing and that authorisation is similar to our exemption provisions. The difference is that under Section 96, it can be granted on the basis of any benefit to the public. So it is an extremely broad provision that deals with exemption and very briefly I want to discuss the A Triple C which is the Australian Consumer in Competition Commission or maybe Competition and Consumer Commission and you know the tussle that they had with regard to interchange fees in the card world.

10

In 2000 the A Triple C announced that it had instituted proceedings against National Australia Bank for price fixing and it took the view that the interchange fee in the credit cards schemes in Australia did constitute price fixing in terms of that deeming provision and in the press announcement they said that they had been in discussions with the banks but the banks although willing to talk about some things were not willing to talk about, you know anything that had a bearing on the interchange fees.

20

And also in that press release the A Triple C recorded that it was not opposed to the credit card interchange system and it in fact believed that if the banks were willing to conduct a review of how it was set that it would be authorised and that or if said an

Pretoria
05 June 2007

authorised joint system they believed would be to the benefit of Australian consumers. The A Triple C then dropped its inquiry because it was taken up by the Reserve Bank of Australia who as you know designated the credit card schemes.

And ultimately the Reserve Bank after a very detailed inquiry has permitted interchange fees but has dealt with the level of those fees to ensure that they are appropriate. So what I do think is important is that even if and this bear in mind was prior to the recent amendments relating to joint ventures, even if the interchange fees had been caught by the *per se* prohibition on price fixing, there is still this possibility to seek authorisation on any public interest ground and in fact that the authorities in Australia had formed a view and they had already done some detailed inquiry with regard to the credit card system that they had formed a view that this was in all likelihood something that ought to be authorised in terms of their Competition Act and in saying that I mentioned for what it is worth that I shared the view that Mr Petersen has expressed that our arrangements in South Africa, I think it would be something of a stretch to try to fit them in any of our categories for exemption which I believe makes it all the more important to approach the section in a proper way.

Pretoria
05 June 2007

ADV. PETERSEN: Sorry which section are you talking about? I know Section 10 is the exemption section...

MS MEIJER: I am talking about Section 4.

ADV PETERSEN: So that makes it Section 4, is it your submission that we ought also irrespective of the interpretation of Section 4 or changes to Section 4 which we might favour, is it also your submission that we should recommend a broadening of
10 the grounds of potential grounds of exemption under Section 10?

MS MEIJER: I believe that strongly and have done for some time. That section has not been used extensively and the reason I think that it has not been is because, you know the grounds of exemption are so narrow and it is not difficult to think of a circumstance where, you know where an arrangement is entered into that is anticompetitive but which for example creates a 100 thousand jobs, very hypothetical example and yet that is not a ground upon which you could seek exemption under our
20 Act.

*Pretoria
05 June 2007*

CHAIRPERSON: If I may ask you whilst we are still on Australian Law, you say the Reserve Bank of Australia permitted interchange subject to the fact that the level is not too high, what model did they set up to look into that?

MS MEIJER: They have essentially set an..., they have set the interchange fees in respect of the different payment mechanisms. So there is a Gazetted figure as I understand it which the banks are permitted to charge.

10 ADV. PETERSEN: A maximum.

MS MEIJER: A maximum.

CHAIRPERSON: It is a maximum figure?

MS MEIJER: It is a maximum figure that they are permitted to charge and as I understand it there is a formula that is applied and the banks on a regular basis, submit their information and that is..., that information is used in order to determine the appropriate figure.

20

CHAIRPERSON: Okay you may proceed.

MS MEIJER: Sorry just..., it is probably not really necessarily to summarise but I do think the important thing is that the Australians were hitting their head against the same frustration that certainly practitioners experience here, which is that the *per se* prohibition very likely had an impact on ordinary joint ventures and this..., one should not underestimate the effect that that may have had in South Africa.

10 I, you know as a practitioner in this field, clients frequently consult me on joint venture arrangements and if you cannot give an unqualified green light, many clients will not proceed with activities. So that I think that there are arrangements which have not been entered into out of, you know, ordinary joint ventures that may well have been pro competitive that have not been entered into because of this provision and also I think that there are instances where firms have restructured their arrangements in order to, you know sort of try to get themselves into rule of reason as opposed to fitting within the possible *per se* prohibition and that that may in fact may not always have been efficient. So the Australians have come up against this and

20 have dealt with it in term of excluding joint ventures from their Act and of course they have this very wide authorisation provision. We have already dealt with the EU

Pretoria
05 June 2007

and I am not going to go through this slide because it is largely summarises what you put to me earlier, Mr Petersen.

One addition though is that whether an agreement has as its object or its effect prevention restriction or distortion of competition, it must appreciably restrict competition and have an appreciable effect on trade so that it is a requirement in all cases this prohibition would not relate to an arrangement which had an only trivial effect whereas in South Africa I think can apply to any arrangement that meets those requirements unless some form of characterisation is undertaken.

10

ADV. PETERSEN: And then it may nevertheless be exempted?

MS MEIJER: Yes and it may nevertheless be exempted under Article 81(3) and the grounds for exemption are set out there which I think are narrower than the grounds that one sees in Australia but of certainly substantially wider grounds than are available for exemption in South Africa.

20

With regard to interchange fees, you will be aware that there was a detailed inquiry into Visas multilateral setting of interchange fees and I think it is important there to

*Pretoria
05 June 2007*

note that the European Commission in its investigation and this was when it was still looking at the arrangement under Article 81.1, found that it did not restrict competition by its object.

10 So in other words, because it did not restrict by its object, it instead was something which was considered to have the effect of restricting competition and was for that reason subjected to the full blown rule of reason analysis. And it was ultimately exempted under Article 81.3 and I am not now going to go into the details with regard to that but the authorities were certainly satisfied there that it was in arrangement that had as its object to increase the stability and efficiency of operation of that system and they believed that it indirectly strengthened competition between payment systems and I think in the EU there is again significantly less risk of the type one error than we find in relation to our *per se* prohibition.

20 So turning to our section and I will deal with this quite quickly because we have debated some of these issues but I do think that our Section 4(1)(b) uses words that have a particular meaning which, you know these are words like restrictive, collusive, dividing, fixing. You know words which have a particular meaning and would

Pretoria
05 June 2007

suggest a type of conduct which ought to be outlawed and we believe it was the intention that it is the intuitively obvious anti..., you know arrangements that were intended to be outlawed by this provision as in a naked cartel.

10 And the approach which we suggest should be taken is that if an agreement is not a naked restraint obviously intent on achieving only anticompetitive effects, then it should in fairness be subjected to scrutiny on its facts for the purposes of characterisation. The characterisation process would permit limited evidence with regard to..., I would say nature, purpose and effect of the arrangement and it could still result in *per se* prohibition. If on the other hand that characterisation reveals that the agreement does have a legitimate business purpose that it promises for example greater productivity or output, then it should be subjected to a full rule of reason analysis.

20 ADV. PETERSEN: Before you go on, in relation to output it seems to me to be a troublesome criterion because we imagine an actual cartel consisting of say three out of five players in a market. They may well increase the output of the cartel but at the expense of the other players. So whose output are we talking about and is it enough

Pretoria
05 June 2007

that the participants in the venture, because we are now having to characterise to see whether it is a cartel or a legitimate joint venture, to what extent can the participants in the venture simply claim the benefits for their own output as a sufficient justification for the agreement?

10 MS MEIJER: I think it is..., it would generally be accepted and I may turn to James Hodge for assistance on this but I think it would generally be accepted that increased output would be pro competitive so that even if..., I mean you would normally expect that additional output could very well have the effect to be exerting downward pressure on prices, I would think it would be unlikely to have the opposite effect.

MR HODGE: Well I suppose almost by implication that there is a demand out there that to increase sales you need to drop price and if that is where you are looking for the effect on the market because you normally characterise anticompetitive effect as raising prices or restricting output but I think your point is more subtle that it is not their output, it is the output of the market that matters.

20

MS MEIJER: And we believe that this interpretation does preserve the ability to prohibit naked cartels but it also prevents prohibition of arrangements that are

*Pretoria
05 June 2007*

potentially pro competitive. And our analysis suggests to us that in South Africa with regard to Section 4(1)(b), we have far less in the way of checks and balances to guard against a type one error than is evident in the other jurisdictions that we have reviewed. Applying this to interchange fees, it is our submission that the multilateral setting of interchange fees is certainly not something that would fall within the category of a naked restraint.

10 We believe that evidence to characterise it will show that it has a legitimate business purpose and that it is something that should be analysed under a rule of reason and we believe that once analysed under the rule of reason it is an arrangements that ought to be permitted and I think you have heard all of the arguments about, you know what the..., you know the various submissions about the arrangement and you know the arguments that acquirers and issuers are free to compete vigorously with regard to end user pricing.

20 That it certainly results in a larger scheme with greater economies of scale and in fact this balancing of the market is likely to..., is also likely to raise scale and maximise output, the balancing that occurs through the interchange fee. We believe that in the

Pretoria
05 June 2007

system barriers to entry for small banks and for new banks are significantly lower and that establishing a three party system is much more difficult and that if that was the only model that was present in our market which is something that has been debated that there would in fact be substantially less competition.

10 The levels of interoperability which have been achieved, we do not believe could ever have been achieved without the current system which includes as an integral and an essential part, the setting of default terms including the interchange fee and we considered that the process that the banks went through to set this fee was one which has insured that the fees in the different payment streams have not been set at a level that is too high.

20 And the banks in fact demonstrated that it was not their intension to do so by setting a lower interchange in respect of debit cards than had been recommended in the Edgar Dunn process and to take this view would be consistent with the US which has said that the interchange fee and that the arrangement between Visa and its members, you know showed the characteristics of a joint venture. It would be consistent with Australia where the authorities have expressly said that they believe.... that an

*Pretoria
05 June 2007*

authorised joint system would be to the benefit of Australian consumers and with the EU which acknowledged that this was not something that restricted competition by object and the EU then went on to allow and exempt the arrangement under Article 81(3).

MR BODIBE: Sorry before you move from that slide. In both the US and EU case, not having looked at those cases, just clarity to on what did the matter turn on? Was it on a necessity of interchange or was it a comparison of inter scheme competition?

10

MS MEIJER: In the US, I think the necessity of interchange did play a role in the characterisation argument but certainly I think the considerations were broader in terms of ultimately analysing it under the rule of reason and I think a key factor was the universality that was achieved through the system. In the EU they looked at a whole series of factors. The issue of necessity only came in, I believe in the context of the exemption where you got to prove that what you do is indispensable to the achievement of..., let me just go back to..., so they was satisfied that it did contribute to improving the production, you know to the first criteria and they believed that because the interchange fee could be competed away and because Visa had put in

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*Pretoria
05 June 2007*

place a whole lot of steps to ensure that interchange was not set too..., sorry..., a too high level..., That was the meeting I was meant to be at now

MR BODIBE: Sorry

MS MEIJER: That because interchange had..... you know the various steps Visa initially when this was first investigated put in place a whole lot of different mechanisms to bring interchange down and in the process in which this exemption
10 was granted, interchanges fees in the EU came down very significantly.

So for that reason I think they believed that there were resultant benefits for consumers and then they had to prove that the restrictions that they had and that was in particular the setting of the interchange fee, was indispensable to obtaining those objectives and the authority there was satisfied that that was the case.

MR BODIBE: So it did not turn on competition between the schemes?

MS MEIJER: No, I think they did believe that it enhanced competition between you
20 know that the ability for aggressive competition between the schemes remained but that was not really the focal point as I saw it of the decision.

*Pretoria
05 June 2007*

MR BODIBE: Okay, so would I be right then to conclude that there is enough case law on that test inter scheme competition but also looking at level of interchange?

MS MEIJER: Sorry, could you repeat that?

MR BODIBE: Okay is there any case law that looks at inter scheme basically looks at competition between Visa and MasterCard and the three party scheme and the level of interchange between these schemes?

10 MS MEIJER: Not..., there is not a case that explicitly deals or that focuses on that issue but in the Visa exemption application there is some discussion with regard to three party systems and how..., you know the kinds of efficiencies that are achieved in a four party scheme versus a three party scheme, there is discussion of that there and I think it is also mentioned in the NaBanco case in the US but I can not recall off hand, you know all of the details of what was said.

20 MR BODIBE: Now considering that the requirements of both Visa and MasterCard are almost identical, is it therefore probable that the schemes could compete and one

*Pretoria
05 June 2007*

scheme actually pricing below the economically efficient level of interchange to try to out compete the other, is that potentially feasible?

MS MEIJER: I think it is, I mean it is at least theoretically feasible but that would not logically be what the scheme would do, I mean James I don't know if you want to answer it.

MR HODGE: Well I suppose, I mean given that this is a two sided market, they
10 would need..., when they decide on how to compete if interchange is the means which they are going to try and use. They will have to consider both sides. So let us say you dropped interchange, that might make you slightly more attractive on the acceptance side but maybe less attractive on the issuing side. So they are going to have to consider both aspects in doing so. It is not definite that it would go one way or the other.

MR BODIBE: Sure I do accept that but I was just trying to test whether at the
20 moment we would be considering cases where we are looking at one particular scheme and its arrangement and what I was interested in is in that situation where there is two schemes and potentially the ability to create other schemes. Okay in

*Pretoria
05 June 2007*

what way can competition be enhanced which can also bring down, ... which means is interchange itself subject to competition among the scheme, between the schemes and of course that the other factors that you have just explained have a bearing on the outcome ultimately but I was just wondering whether in the inter scheme competition sphere it is possible for the schemes themselves to compete on interchange as well.

10 MR HODGE: Look, it must come in as one of the factors for competition between them. I mean possibly the fact that many jurisdictions have chosen to regulate and they feel that that is not a sufficient dynamic between that. As I said, in terms of the competitive dynamics it could go either way and it could be a factor but I mean maybe in relation to one of the theories of harm that you put up interchange rates and try and keep the profits in the system. So you are not passing any benefits on to consumers at all. There competition between schemes would surely make such behaviour, such a unilateral behaviour unlikely to succeed because other schemes are going to be passing on benefits and offering both sides of the market a better deal so

20 they are going to grow at their expense.

*Pretoria
05 June 2007*

MR BODIBE: Okay, now you may choose to answer this question or you may choose not.... may elect not to, but in your judgement do you think that there is sufficient competition between Visa and MasterCard at least in the South African market?

MS MEIJER: I do not think that is something that we have really applied our minds to. I mean obviously we have noted that interchange is the same for both of the schemes, we have noted that but we have not really applied our mind to the issue of
10 the extent of competition between the two schemes.

MR BODIBE: Thank you.

MS MEIJER: So that was really what I wanted to say. If I have not emphasised sufficiently..... just to sum up. It is our view that Section 4(1)(b) with the approach taken to it, has been too broad and that if an approach if taken now which *per se* prohibited interchange fees or in fact any of the other inter bank fees that are levied,
20 would be too..., it would reflect that that approach was too broad. We do believe that there is room within the current legislative framework to interpret Section 4(1)(b) in a manner that would not prohibit these kinds of inter bank fees.

*Pretoria
05 June 2007*

They have not been prohibited *per se* in any of the jurisdictions where they have been considered generally as a very complex matter and there has been careful scrutiny of these arrangements and we believe that rule of reason analysis, it will be permitted in South Africa as it was permitted in the US and as we have emphasised repeatedly, we are willing to subject ourselves to appropriate measures to ensure that the level is not set too high.

10 So that really concludes what we wanted to say. I just wanted to come back to the question that the Chair raised regarding the three party system and whether or not there is not some form of division of markets there. We believe that the relevant markets and I may ask Mr Hodge to assist me with this in due course but we believe that the relevant market is the market for the transaction account and that what has happened in that context is that banks initially gave their own customers access to their transaction accounts by going into the bank and you know drawing money over the counter and another means of access which they developed over time and

20 Standard Bank was one of the first banks to do this, was where you could access your cash through the ATM.

Pretoria
05 June 2007

It was a customer convenience issue, it was an innovative issue and I think it was also a competitive issue because having ATM access, I have no doubt at that time was something that gave a firm a competitive edge. And the logical next step from that and it was not something that the banks had to do but something that they chose to do was to give their customers access to that account through any ATM of any other bank and part of what they did in that context was to agree carriage fees. And I see the primary purpose of what was done there as being a purpose of giving customers access to their accounts with a particular bank in a context where the market is a market for that transaction account. So I do not really see how a division of markets could have occurred and I do not know if that answers your question.

10

CHAIRPERSON: Then coming into the allocation of the customer.

MS MEIJER: Well it is..., the customers belongs to the transaction account although transaction account belongs to the customer so that the customer already belongs to one of the banks and that bank is just facilitating its customer having access to its account through a whole series of other means and as you know, you know those means of access have developed over time and so they can now be done with your

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*Pretoria
05 June 2007*

mobile phone and it can be done over the Internet but at the end of the day the..., what the bank is really after is the transaction account and I think that Standard Bank did say that it is not..., it would like customers to hold transaction accounts with it, not customers who hold transaction accounts with other banks to be using its infrastructure. That is...it does not mind if they do that, but that is not what motivates how it competes in the market. It is really seeking to get the transaction accounts.

10

CHAIRPERSON: Yes, anyone to add anything? From the Standard Bank team on the particular aspect?

MR HODGE: Well as far as..., I mean maybe just to add very little to this but obviously what is relevant is what is the market and that is I think the point that Jean is trying to essentially make that if there is a theory of allocation then it has to happen within the market and identifying what that market is, is important. At the moment you know, access to others ATM services is really wholesale services provided and the customer is another bank so the bank certainly sees this as the transaction account

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*Pretoria
05 June 2007*

is the market for the customer the final customer and this is a mere wholesale arrangement.

CHAIRPERSON: Okay, any questions?

MR BODIBE: Thank you Chair, I am trying to understand what you are saying on the two bullets. It can be interpreted in different ways on so..., for the record it is slide 43. And you know in this particular case, you understand the frustration of some
10 former US president who was demanding an economist with one hand . Anyway are you saying as matters stand, which means as the law stands at the moment, the multilateral setting of interchange fees is *per se* prohibited, is that what you are saying with the...

MS MEIJER: No I am saying that on the approach that the competition authorities have taken which is that you have to show an agreement between competitors that fixes a price arguably the multilateral setting of interchange fees would have been *per*
20 *se* prohibited if that was the approach. I think ANSAC has suggested although it has not said but it has suggested that that would be the wrong approach and we believe that without legislative amendment there is more than sufficient scope to interpret

Pretoria
05 June 2007

and one should interpret Section 4(1)(b) in a manner that would not impact on an arrangement like this that has a legitimate business purpose and arguably does and we say in fact does, increase efficiencies and is pro competitive.

MR BODIBE: Okay thank you, on a slightly different topic that relates to horizontal relationships. Can you explain that term for me?

MS MEIJER: Horizontal relationships are arrangements between firms that are
10 competitors and it has also been more broadly interpreted to include potential competitors and those are parties that operate in the same level of the market.

MR BODIBE: So when banks come together in a forum to discuss say interchange fee, are they still in horizontal relationship?

MS MEIJER: I heard the argument made that they were in a vertical relationship for that purpose and I suppose that in relation to any two banks, they would be in both horizontal and a vertical relationship so that I submit that it would be difficult to
20 argue that, bearing in mind that all of the parties at both levels of the market are

Pretoria
05 June 2007

together negotiating that it would be perhaps stretching it to argue that they are not competitors although I suspect others may do that.

MR BODIBE: So you are saying it is open to debate whether they are in a vertical or horizontal relationship in that instance.

MS MEIJER: I think that there are arguments that could be made but we do not make them strongly, I think it is our view that you know the banks are competitors
10 and although this is a wholesale price that they have agreed, they all agreed it together.

MR BODIBE: And in relation to Bankserv, is that a vertical or a horizontal relationship?

MS MEIJER: Explain...

MR BODIBE: Given the part ownership of Bankserv by the banks or some of the
20 banks...

MS MEIJER: I do not believe that that is..., well I believe that the arrangement where banks procure services from Bankserv is a vertical arrangement. I believe

*Pretoria
05 June 2007*

Bankserv is a joint venture and should be treated as such and that it is not, you know I do not think it should be viewed as an agreement between competitors and properly characterised, it is a fully integrated joint venture which certainly has efficiency gains.

MR BODIBE: And what about the ownership component?

MS MEIJER: I do not think that that matters. Yes you know, the banks do own
10 Bankserv, they were the most likely firms to have set up that kind of a joint venture. They..., but I mean the fact that they are in a joint venture does not remove the fact they are competitors but for purposes of that joint venture, it should be viewed in my opinion, not as an arrangement between competitors but as a fully integrated joint venture.

MR BODIBE: So when you say it does not matter, it does not matter for who?

MS MEIJER: I do not think it matters for purposes of competition analysis.

20 MR BODIBE: Okay, now if I am to make a different example and say this is a firm that produces the good and also owned the pipeline to transport whatever is the good,

is that not the analogy could it not be extended to the relationship between banks and Bankserv.

MS MEIJER: Well is that not..., it is more a question of

(Error on transcript tape)

I mean if it were the act it is more a question of an entity that is vertically integrated but it is not. Yes...

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(Caucus)

MS MEIJER: I think it is more analogous to having a public utility and in fact historically it is operated as a kind of a utility that everyone has access to and I think that is really the context in which it should be viewed, not in the context of it being an agreement between competitors that potentially restricts competition.

MR BODIBE: I was not trying to draw the latter conclusion. I am just trying to understand how you characterise that relationship. Now if they come together in the PCH, how do you characterise that relationship? Is it still the horizontal or vertical relationship?

*Pretoria
05 June 2007*

MS MEIJER: That is a horizontal relationship.

MR BODIBE: And the purpose of the PCH is really to set some rules. Okay now which brings me to the point that I want to understand between why is it necessary to have branded cards as opposed to white labelled cards which is an agreement that..., how did that come to be? Just inform us before I make the assumption that it is an agreement to exclude white labelled cards.

10 MS MEIJER: My understanding and if the business people have a different view, I am sure that they will express it but it..., the..., that..., it is all about having appropriate standards and there is in a schedule to the ATM, sorry it would be to the card PCH agreement. There is in a schedule, there are details of the standards that need to be met in order for white labelled cards to be issued and they certainly appeared to me to be reasonable standards that would enable interoperability of a card. So the restriction is simply that they have not yet met or there are not any white or that white labelled cards need to meet those criteria before they can be issued by
20 any of the banks...

(Error on transcript tape – Tapes change)MR BODIBE:between banks.

*Pretoria
05 June 2007*

MR SHUNMUGAM: Sorry if I may just answer, I think...

CHAIRPERSON: I think that he is changing the tape. Are you done? Done. Okay, sure.

MR SHUNMUGAM: If I may just give some feedback there. I think originally when the PCH agreement was signed in 2004, the banks made a decision to basically all the white labelled cards that were in existence at that point in time were accepted
10 into the payment clearing house. The only..., and going forward what the banks collectively decided including that banks that had white labelled cards, is that we do not want to recreate rules and standards when we do have rules and standards set by Visa/MasterCard and they are quite comprehensive. So why reinvent the wheel for South African situation.

And what the banks then did is adopted Visa/MasterCard standards and the agreement that says the banks that did have white labelled cards is that we will accept
20 those white labelled cards but no new white labelled cards will be introduced going forward unless banks that do want to introduce white labelled cards, get together and create a local association with local rules that can then be inter-operable with the

*Pretoria
05 June 2007*

international rules and I think that was the agreement at that point in time. So it was not a restrictive clause in terms of going forward and I think at that time if you take a typical example like SAPO and the Post Bank, they came in with white labelled cards but they are actually at this point in time doing the conversion to Visa brand cards because of the international inter-operability and the rules and standards that go with it.

10 MR BODIBE: Okay, now suppose my business model as a bank is purely based on this white labelled cards, I do not want international inter-operability but I want local inter-operability, what is the process that I will have to follow to gain acceptance and to practice considering that I have now satisfied the SARB requirements. I have satisfied the technical standards that you are talking about. So how would I go about participating in this arena?

20 MR SHUNMUGAM: I think firstly those banks that want to introduce white labelled cards will have to get together and define those standards for the white labelled cards to be inter-operable with the international standards because you need to maintain the same level of inter-operability and there is nothing stopping them

*Pretoria
05 June 2007*

from forming a local association with local rules and taking it forward on that basis. So there is nothing stopping two banks if they wanted to introduce white labelled cards to actually go in and form a local association apart from Visa/MasterCard, a separate association, nothing stopping them from doing that.

MR BODIBE: Do I not need an agreement of existing banks if I want to inter-operability with also the existing banks?

10 MR SHUNMUGAM: Yes I think even you, you can get an agreement where the two banks enter into the agreement for that white labelled cards or if those standards are defined appropriately and the existing payment clearing house deems them to be appropriate in terms of risk reduction measures and mitigation of appropriate risk in the system, there is nothing stopping the loca..., the current PCH from adopting going forward. I..., but that will obviously need to be explored.

MR BODIBE: Are the standards substantially different?

20 MR SHUNMUGAM: Sorry?

MR BODIBE: Are the standards substantially different between white labelled cards and international cards?

MR SHUNMUGAM: I think basically on the white labelled there are no predefined standards so essentially you can just introduce a card, you know there are specific standards from a Visa/MasterCard perspective in terms of the labelling and so forth and so forth. So there is no prescribed standard for white labelled cards. If I take
10 current white labelled cards as they exist, you necessarily would not find two of the same white labelled cards having the same standard across them. So there is no prescribed standard that would have to be defined.

MR BODIBE: And what about the take-up rate? What influenced the take-up rate of branded cards compared to white labels?

MR SHUNMUGAM: I think it has more uses and acceptance of the card and the fact that if you look at MasterCard and Visa and the logos associated with it, it gives a
20 customer the perception or it gives the customer the confidences of international inter-operability and obviously local inter-operability as well.

MR BODIBE: So there is assuming customer knowledge.

MR SHUNMUGAM: Yes.

MR BODIBE: So in the instance where it is..., there is no customer knowledge it is your marketing decision that influences take-up.

MR SHUNMUGAM: You know I would assume so, from the issuing perspective.

10 MR HODGE: Yes, from the issuing perspective.

MR BODIBE: Okay thank you. I am done Chair.

CHAIRPERSON: You are done.

ADV PETERSEN: To take you back to the law of it, the..., Ms Meijer the criterion of object or purpose of the agreement which you would seem to agree is either the essential or one of the essential criteria in the application of Section 4(1)(b).

20 MS MEIJER: Correct.

ADV PETERSEN: That can itself be a slippery thing to prove, do you agree.

MS MEIJER: Correct.

ADV PETERSEN: And it is in that regard that there has been developed a doctrine of ancillarity, am I right so far?

MS MEIJER: Yes.

10 ADV PETERSEN: Of course every restrictive clause, you yourself pointed out I think that every contract is restrictive, every restrictive clause in the contract must have been intended to restrict. So to that extent its purpose is anticompetitive but that would not be enough to bring it under 4(1)(b)

MS MEIJER: Correct.

ADV PETERSEN: If that restrictive purpose is purely ancillary to another purpose, is that how you also understand the doctrine?

20 MS MEIJER: Yes.

ADV PETERSEN: Of ancillarity. And as part of testing that ancillary character of the restrictive purpose, one looks at whether it is reasonably necessary to the attainment of the main purpose, would that be sound?

MS MEIJER: I think that that is part of what one looks at but I am not..., we would say that showing that it is necessary is not an absolute requirement for one to escape Section 4(1)(b).

10 ADV PETERSEN: Just help me there because I am....thinking an answer to what you have said...that in response to what you have said that, well if it is not necessary or reasonably necessary to the legitimate purpose of the agreement and its purpose is restrictive as it stands...that clause, why should it escape?

MS MEIJER: It maybe a difference in terms of what is understood by necessary because I think if it is..., if what you postulate is something.... is an objective test of necessity then I am not sure that that is required but if the parties at the time
20 considered that it was necessary that they enter into the arrangement that would be adequate and if I can go for a moment back to the beads worker example, you know. Was it necessary for them to enter into and let us assume for a moment that that is not

*Pretoria
05 June 2007*

an agreement which would be *per se* prohibited and as I have indicated earlier, it is not that different to the ANSAC arrangement where that indication was given. Is it objectively necessary that one of their number should travel to Johannesburg to sell? You know and one of the competitors should do it. Could it not you know they each have done it individually, could they not have appointed an independent agent and had individual terms with that agent? So I think it depends on what you mean by necessary and it may be that necessary takes it a step further than I would submit is required in order to take something out of the ambit of Section 4(1)(b).

10 ADV PETERSEN: In your client's submission of the 10th of April 2007 on card interchange fees, where a considerable part of the argument that you have addressed us today is set out, it said for example on page 22, paragraph 3.10.5:

“It is submitted that an inquiry into the necessity or otherwise of a particular practice is not relevant to the determination of whether an agreement contravenes in section 4(1)(b) of the Act.” Is that essentially what you have been arguing to us now?

20 MS MEIJER: I believe necessity maybe a component of what causes the adjudicator to look at the arrangement and say that it is not a naked restraint and it is not

Pretoria
05 June 2007

something that clearly only has as its end, the setting of a price but I do not believe that it has to be shown and as I say again, I think it comes back to what you mean by “necessary.” If you mean by necessary that this is the only way that something could have been done, then I do not believe that necessary is a requirement in terms of the characterisation process. It is that those parties in entering into the arrangement had a legitimate purpose and what they did formed a part of that and it was reasonably a part of that but not necessarily something that was absolutely in objective terms
10 necessary to what they did.

ADV PETERSEN: Would you agree that in the approach taken to the doctrine of ancillarity in the United States, there is a test of whether the restrictive provision is reasonably necessary and on that basis...

MS MEIJER: That...

ADV PETERSEN: Ancillary to the legitimacy to the legitimate purpose of the
20 venture.

*Pretoria
05 June 2007*

MS MEIJER: That test certainly has been applied in some of the cases but I do not know that it has been applied in all of the cases. I think it is more..., it maybe more a perceived necessity and one of the cases that was considered was the..., one of the US cases that deals with this is the National Collegiate Athletic Association case and there the court.... are you familiar with the facts of that of that case?

ADV PETERSEN: Please help me...

10 MS MEIJER: Okay...

ADV PETERSEN: My memory is fading.

MS MEIJER: Essentially the...

ADV PETERSEN: It has something to do with the setting up of fixtures in that..., in the Sports Association.

20 MS MEIJER: Yes the NCAA had implemented a plan that limited the total amount of televised college games that would be permitted and the number of games that each college could televise and it also negotiated a minimum aggregate compensation

*Pretoria
05 June 2007*

which ended up being the compensation that was paid so that it was argued, one: that they had restricted output and, two: that they had fixed a price.

And the court held it while the plan constituted horizontal price fixing and output restrictions, restraints that ordinarily would be held illegal *per se*, it would be inappropriate by the *per se* rule in this case wherein it involves an industry in which horizontal restraints on competition are essential if the product is to be made available at all and it went on to say that some activities can be carried out jointly, perhaps the leading example is League Sports, it would be completely ineffective if there were no rules on which the competitors agreed to create and define the competition to be marketed. You know, there would need to be rules regarding the size of the field, the number of players on the team and the like.

And my assessment of that, is that the focus was on this thing and industry where horizontal restraints were necessary but in order for that not to be considered under the *per se* prohibition, it was not required to show that the particular restraint was necessary. So that, I do not think it would be true to say that the necessary tests is being applied across the board but it has certainly been applied in some of the cases

Pretoria
05 June 2007

and that arrangement ultimately after a rule of reason analysis was in fact prohibited but it was not prohibited *per se*.

ADV PETERSEN: Would you agree that at the very least an unnecessary restriction could have an evidential bearing upon the purpose of the restriction.

MS MEIJER: Yes.

10 ADV PETERSEN: Now let me try to move along that same track towards this issue of ATM's and customer allocation. Now you have explained that in the development of the automatic cash dispensing service this was an extension initially by banks to their own customers of over the counter withdrawals from the transaction account, quite understandable to me and also that in its further extension to make available the facilities of other banks by inter bank agreement, it clearly developed with the object of extending the transactional facility and convenience to the banks own customers. That is what you have explained if I have understood you correctly.

20 MS MEIJER: Correct.

Pretoria
05 June 2007

ADV PETERSEN: Fine. So from that then comes the argument, well that is the relevant market is the transaction account and facilities connected with the transaction account. Now what I want to raise with you to comment on is whether that is not too static an approach. Once the potential has developed significantly for cash dispensing from automatic machines, has become a real practical possibility and at least a potential market. Must we not ask ourselves the question that if the previous ownership of the customer in relation to cash dispensing to the debit of the transaction account, is no longer necessary and banks persist in maintaining the restriction so that this possibility of this somewhat different market developing namely the market for cash dispensing services with payment being effected by way of the payment system. Does it not, once that has become apparent and the realisation has dawned, does it not from that point on take on the character of having an anticompetitive purpose if the restriction continues to be maintained.

MS MEIJER: There is case law certainly in the US that suggests that the purpose that should be considered is the purpose at the time that the arrangement was entered into. I think we would have a series of different points of departure from you with

*Pretoria
05 June 2007*

regard to what you have said because we certainly would not view that... we would not view the market for dispensing cash as a separate antitrust or competition market.

So I think that is the first point and secondly even if it is correct that there has been some change in the market or that there..., so even if you are correct in your assumption that that is a separate relevant market and that...

ADV PETERSEN: Or potentially so?

10 MS MEIJER: Yes and that there has been a change in the market that makes a particular practice no longer necessary, my submission would be that that would not on its..., that would not alone be sufficient in order for you to say that the character of something that was originally had a legitimate business purpose has changed.

ADV PETERSEN: Thank you, I have raised the point with you and you have addressed it and I do not think it is appropriate for me to comment further on that argument. Turning to the..., you want to pursue it?

20

*Pretoria
05 June 2007*

CHAIRPERSON: Yes there is just one point I want to..., I just want for clarification, you say it is an extension of a transaction account to offer the cash to the customers, what would you define as a transaction account?

MR SHUNMUGAM: Chair it would be the account that the cash withdrawal in the case of ATM's or where the cash withdrawal will be made that would be the transaction account. It would either be a current cheque account, savings account or credit card account.

10

CHAIRPERSON: Including a credit card account?

MR SHUNMUGAM: Yes, as a product.

CHAIRPERSON: As a product that will be a transaction account?

MR SHUNMUGAM: Yes, well those three are permissible products right now from which customers can withdraw...

20 CHAIRPERSON: No, no, no I know that the permissible from which to withdraw cash, I am just trying to find out whether you classify a credit card account as a transaction account.

*Pretoria
05 June 2007*

MR SHUNMUGAM: No it is not a transaction account, it is a product by virtue of... from an issuing kind of view, it is a product and obviously there is various mechanisms that one can access their account.

CHAIRPERSON: Right.

MR SHUNMUGAM: Cash withdrawal being one of them.

10 CHAIRPERSON: So a credit card account, it is a product it is not a transaction account.

MR SHUNMUGAM: No it is not a transaction account. It would be current and savings.

CHAIRPERSON: So it is current and savings.

MR SHUNMUGAM: Yes.

20 CHAIRPERSON: So basically then your point is the withdrawal of cash as an extension of the current account and the savings? Okay thank you.

ADV PETERSEN: But you can withdraw cash on a credit card.

MR SHUNMUGAM: Yes you can.

CHAIRPERSON: Okay, yes?

ADV PETERSEN: Just finally in regard to vertical/horizontal analysis. It is in fact put, as you will be aware in..., on page 23 of the card interchange fees submission that the non horizontal nature of this process is a fundamental issue. Look at paragraph 4.3 for example.

10 MS MEIJER: Yes but I think that makes a slightly different point which is that it..., if all of the firms involved in issuing and all of the firms involved in acquiring agree between them voluntarily in a willing process to a fee that that is not the type of arrangement that would have been contemplated by Section 4(1)(b). That that falls short of a collusive kind of outcome which is what was intended.

If all of the acquiring firms had agreed or all of the issuing firms had agreed that that might have been different, so I think the point that we are making there is that the
20 fact that they all reached this agreement together takes it out of 4(1)(b) but does not necessarily mean that it could not have anticompetitive effects simply that that is not

*Pretoria
05 June 2007*

price fixing. And in a sense it perhaps goes back to the Canadian example where if the arrangement is made known and I do not suggest that that should be adequate, just that the arrangement is known but the fact that all of the acquiring and issuing firms have actually agreed to it voluntarily, is what I think makes that something which would not constitute price fixing.

10 ADV PETERSEN: Forgive me but you lost me a bit there and I have to go back. As I understood it, the argument proceeds from the idea, which may with respect be sound, that interchange is a fee agreed for a service or supply. Now a supply is a vertical process and so therefore if we are limited to a bilateral relationship for the moment, it is purely vertical. That is the argument if I understood it so far and you are nodding?

MS MEIJER: Say that it is reciprocally vertical.

20 ADV PETERSEN: Yes but two people are agreeing to make a comparable supply to each other under different circumstances at the same price.

MS MEIJER: Correct.

ADV PETERSEN: But in each case it would be a vertical relationship.

MS MEIJER: Correct.

ADV PETERSEN: Now it seems to me that the..., and you know all the PCH agreements are structured on the basis that multilateral fixing is to be avoided like the plague and everybody must get involved in bilateral agreements and presumably that is based on an analysis that was made that that would be okay because it was vertical
10 as long as it was bilateral.

MS MEIJER: That is as how I understand the advice that was given.

ADV PETERSEN: Yes but as soon as two suppliers get together to agree at what price they will supply to others, then the argument would be that those suppliers are in a horizontal relationship with each other and are perhaps illegitimately fixing. I am not saying they are illegitimately fixing but are perhaps, that again is correct so
20 far?

MS MEIJER: Correct.

ADV PETERSEN: Fine. Now it may well be that on a proper characterisation of that arrangement it is not prohibited, okay. But I am at an earlier stage, you will appreciate it, of the building blocks of the analysis because if there is no horizontal relationship, it does not come into Section 4 at all and we never have to get to characterisation, you are nodding again?

MS MEIJER: Correct.

10 ADV PETERSEN: I just want to invite your comment on this point which it seems to me is the serious analytical point that has been raised and not to make it as difficult as possible or as clean as possible, let me confine it to a two party, a bilateral interchange agreement. Now I hear and you have agreed with me so far, the parties are in a vertical relationship in relation to each supply.

MS MEIJER: Correct.

20 ADV PETERSEN: So when it comes to each of those suppliers, they are not actually in a horizontal relationship at all. They maybe in a horizontal relationship considered generally because they both in the same market for comparable suppliers generally

*Pretoria
05 June 2007*

but in their agreement between each other they are never horizontal in relation to that agreement that seems to be what we have established.

MS MEIJER: In respect of each individual agreement

ADV PETERSEN: Yes. And we are talking only about a bilateral setting now.

Okay what has troubled me with that point which seems so strong analytically in its own framework is that perhaps the framework is too narrow even in the bilateral
10 case. Let me put this to you. It seems to me that the problem with analysing interchange in that case as involving only a vertical relationship is that it ignores the fact that interchange is intended, we have been told in previous hearings indeed is designed to be something that is passed through to the merchant as a component of the merchant service charge which is levied by each participant in the agreement in its capacity as an acquirer.

Now I know the extent to which it is passed through can be varied but to the extent
20 that interchange is designed to address imbalances of demand between merchants and cardholders if it was not conceived of its being passed through, it would be completely ineffective as a balancing mechanism. So in this regard and I pose the

*Pretoria
05 June 2007*

question to you, it seems to me the relationship of the participants in the agreement over interchange is also a horizontal relationship i.e. that of competitors whether there are many participants involved or only two because interchange is feeding through into a market in which they are in fact in a horizontal relationship.

I do not know if I have succeeded in articulating the suggestion that you are invited to comment on and if you do not wish to comment on it now, it is also fine.

10 MS MEIJER: Is your point that it fixes an input price?

ADV PETERSEN: Or trading condition.

(Caucus)

20 MS MEIJER: I think I..., I mean I think perhaps we should come back to you with regard to your specific question but the point that we were trying to make in paragraph 4.1 about submission on interchange fees was that a price fixing arrangement assumes that the firms that pay the price are excluded from the agreement and that their inclusion here in the agreement removes it from the ambit of price fixing and although it may have the effect of fixing an input price in respect of

*Pretoria
05 June 2007*

the merchant service fee that that is only an input price not a price fixing in the sense that would be contemplated in the section.

And that although that might conceivably, and I do not say that it would but might conceivably have an anticompetitive effect that is one that should be analysed under the rule of reason that that was the point that we were making.

ADV PETERSEN: I hear you. But you would have..., I mean you must
10 acknowledge that Section 4(1)(b) deals not only with direct fixing but indirect fixing.

MS MEIJER: Yes, but it would be our submission that this certainly does not fix the merchant service charge.

ADV PETERSEN: No, but does it not fix a trading condition? I mean you said you may come back later that is fine. I am just making sure that you come back on what I am trying to ask.

MS MEIJER: Yes I understand that.
20

ADV PETERSEN: Thank you very much.

Pretoria
05 June 2007

CHAIRPERSON: Anyway we have got no further questions for you. Thank you very much Ms Meijer for the submissions and doing all the research, we really appreciate that and to the rest of the Standard Bank team, thank you for coming. We will adjourn, to a date to be announced by the Competition..., the Enquiry Manager.

(End)

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Pretoria
05 June 2007