COMPETITION LAW COMMITTEE OF THE LAW SOCIETY OF THE NORTHERN PROVINCES

SUBMISSIONS ON THE COMPETITION COMMISSION OF SOUTH AFRICA'S DRAFT GUIDELINES FOR THE DETERMINATION OF ADMINISTRATIVE PENALTIES FOR PROHIBITED PRACTICES DATED NOVEMBER 2014

Introduction

The Competition Commission's (the "Commission") publication and call for comments on the draft Guidelines for the Determination of Administrative Penalties for Prohibited Practices ('the Guidelines") is a welcome development and the Competition Law Committee of the Law Society of the Northern Provinces ("LSNP") of South Africa thanks the Commission for the opportunity to comment thereon. We believe that the adoption of guidelines will promote settlement of prohibited practices cases as they bring much needed certainty on how the Commission intends to exercise its discretion in determining suitable penalties for offences under the Competition Act, 89 of 1998.

Since the Competition Law Committee of the LSNP consists of lawyers from Gauteng, Mpumulanga, the NorthWest and Limpopo provinces of South Africa who frequently practise before the Competition Authorities in South Africa and engage in settlement negotiations with the Commission, we believe we are uniquely qualified to comment on the Guidelines. We therefore trust that you will find our submissions useful and shall be happy to engage in discussions with the Commissions about them.

At the outset we wish to emphasise what we think is a common point of departure in respect of the Guidelines, namely that it does not constitute a legally binding document and does not fetter the discretion of the Commission, the Competition Tribunal or any court of law. That much is suggested in paragraphs 4 and 10 of the Guideline. What must also be clear, however, is that the Guidelines (and the Commission's concomitant exercise of discretion in terms thereof) could never be permitted to go beyond the parameters and provisions of the Competition Act ("the Act") and the case law developed by South Africa's courts.

What must also be recognised is that the Guidelines cannot cater for every eventuality or possible circumstance in a particular prohibited practice. For instance, there may be cases where despite a contravention having been committed a zero or nominal penalty is justified.

References to paragraph numbers below refer to paragraph numbers in the Guidelines. We first repeat the content of the paragraph (in *italic* typeface), whereafter we state our submission in respect thereof.

1. Paragraph 1.1.3

   Affected turnover means the annual turnover of the firm in the Republic and exports from the Republic in the line of business in which the contravention has taken place

1.1 The word *firm* should be capitalised, as it is a defined term under paragraph 1.1.10 of the Guidelines (assuming the term remains defined).

1.2 Reference to the words *line of business* is overly broad and is likely to result in a far-reaching application as the meaning can be extended beyond the scope of the alleged conduct. For example, it could extend into the geographic or adjacent markets that are not affected by the conduct.

1.3 In the context of bid rigging cases referred to in paragraph 5.3 of the Guidelines, a narrower meaning is ascribed (in that the firm's affected turnover is derived from the products or services that are the subject of the contravention to the one provided under this paragraph), providing clarity and reason. It is proposed that the words *line of business* be replaced with words commensurate with the case law.

2. Paragraph 1.1.5

Base year means the most recent financial year in which there is evidence that the firm participated in the contravention

2.1 The word *firm* should be capitalised, as it is a defined term under paragraph 1.1.10 of the Guidelines (assuming the term remains defined).

2.2 The term *base year* is vague and lacks particularity. There is a lacuna as to how the *base year* will be determined in the event that the alleged conduct ceases halfway through any financial year. Additional wording should be inserted to qualify the time at which the *firm* participated in the alleged contravention, such as the most recent (*completed or full or annualised)* financial year.

3. Paragraph 1.1.10

Firm means a person (juristic or natural), partnership or trust. This may include a combination of firms that form part of a single economic entity, a division and/or a business unit of a firm.

3.1 We note, in general, that the meaning in this definition goes beyond the scope of the definition of "firm" as provided for in the Act. Under the Guidelines, a wider meaning is given which includes a combination of firms that form part of a single economic entity, or a firm and its division and/or business unit. It seems the Commission intended to widen the scope for parental liability where a firm is structured into subsidiaries rather than divisions. As indicated above, we do not believe that it is legitimate to change the Act through the Guidelines. On the contrary, if the legislature intended to have the proposed expanded meaning of the term 'firm' it would presumably have to state that expressly in the definition.

4. Paragraph 2.2

The Act provides for administrative penalties to be imposed on firms for engaging in conduct that it prohibited in terms of sections 4(1)(b), 5(2) or 8(a), (b) or (d) of the Act and for engaging in conduct that is substantially a repeat by the same firm of conduct previously found by the Tribunal to be a prohibited practice in terms of section 4(1)(a), 5(1), 8(c) or 9 of the Act.

It is proposed that paragraph 2.2 of the Guidelines be deleted as it is a mere repetition of paragraph 4.3 of the Guidelines.

5. Paragraph 4.3

As a general remark, it is proposed that reference to section 59(2) of the Act be included under the legislative framework of the Guidelines, confirming that a cap of 10 percent of the firm's annual turnover in the Republic and its exports from the Republic is taken into consideration.

6. Paragraph 5.3

The affected turnover is the firm's turnover or the turnover of an association of firms, derived from the products or services that are the subject of the contravention.

The definition of *affected turnover* is not consistent with the one provided for in paragraph 1.1.3 of the Guidelines, yet it appears to offer more guidance. The Commission should apply its mind to the meaning assigned to these terms to avoid confusion, going forward.

7. Paragraph 5.6

Where the contravention took place within the auspices of an association of firms and the association is responsible for aiding, organising, and/or executing the contravention, the association will be liable for payment of the administrative penalty, separately from the members of the association. The affected turnover that will generally be considered shall be based on the total revenue of the association.

7.1 In general, the Act does not make provision for an association to be held accountable for decisions taken by its members. The association cannot be said to be in a horizontal relationship with its members, which is a necessary condition for a finding of anti-competitive behaviour under section 4. This is further evidenced by the fact that even though collusion may occur within an association, the association in itself does not derive turnover from the sale of products and services; rather it is the members that derive turnover affected by the conduct.

7.2 Furthermore, an association of firms, for example an industry association, will not have an affected turnover. It will also almost never earn a profit. Accordingly, it usually will not be able to pay from turnover-derived profits, as contemplated in paragraph 7 of the Guidelines.

7.3 Accordingly, in our view, it seems to make better conceptual and practical sense to pursue each liable member of an association individually. Penalising both the association and its members amounts to impermissible 'double jeopardy'.

7.4 Furthermore, a different definition of affected turnover or revenue has been introduced, being the total revenue of the association, adding to the mounting ambiguity.

7.5 In the premises, it is proposed that this paragraph be deleted.

8. Paragraph 5.7

In circumstances where the affected turnover of a firm is zero for a particular market (for example in the case of market allocation agreements precluding entry into certain product or geographical areas), the Commission may consider the firm's annual turnover in the market that was protected as a result of the conduct, that is the market that was allocated to the firm as a result of the conduct.

This paragraph appears to be tautologous, if not confusing. It seems clear that the "protected" turnover would qualify as "affected" by conduct disguised to protect the market.

9. Paragraph 5.8.2

For the firm that did not win the tender, where it was party to the collusive agreement and submits one or more of the complementary bids, or where it agrees to not submit a bid or submits a higher bid to ensure that a bid is won by another firm, the Commission will consider the affected turnover to the greater of (1) the turnover generated by the firm in the goods or services that were affected by the contravention, or (2) the turnover reflected in the contract or bid on which the firm submitted a rigged bid or a cover bid in connection with the contravention, or (3) the value of the tender or contract.

9.1 As a general remark, paragraph 5.8.2 of the Guidelines introduces yet another definition of "affected turnover". Part 1 needs more clarity, part 2 is arbitrary and under part 3 the meaning of the *value of the tender* is unclear (is it the amount that the parties bid for or the amount of the contract). On the face of options 1 and 2, it is conceivable that a party that did not win the rigged bid could be made subject to a higher affected turnover than the firm that won the tender.

9.2 Moreover, more clarity and guidance should be given to the term "once off bid rigging". In this regard, the Guidelines do not adequately explain –

(a) the circumstances in which bid rigging will *not* be regarded as once-off, but will instead be regarded as continuous; and

(b) how the Commission intends to treat an “overarching” bid-rigging agreement that affects numerous tenders.

10. Step 2: Calculation of the Base Amount

As a general remark, step 2 appears to redistribute the various sub-sections within section 59 of the Act on an apparently arbitrary basis. This approach does not appear to lend much clarity to but merely itemises the statutory criteria in a manner which seems arbitrary.

11. Paragraph 5.10

The base amount will be calculated as a proportion of the affected turnover on a scale from zero percent (0%) to thirty percent (30%).

Reference is made to sections 59 (a), (b) and (d) of the Act – it seems arbitrary not to include the other subsections of section 59 of the Act at this juncture.

12. Paragraph 5.11

In determining whether the proportion of the base amount will be at the higher end or the lower end of the scale (0% to 30%), in light of the factors listed above, the Commission will consider the following: the nature of the affected product(s), the structure of the market, the market shares of the firms involved, barriers to entry in the market and the effect of the contravention on competitors and third parties including the likely impact on small and medium sized enterprises and the likely impact on low income consumers.

It is not clear why the market share of the firms is included as a consideration and, if so, how. In addition, some of the factors are already taken into account in paragraph 5.10 of the Guidelines. This would appear to amount to "double accounting".

13. Paragraph 5.12

…. For cartel conduct, harm is presumed and will not be proved

The import of the last sentence in this paragraph is unclear. Surely the extent of harm remains relevant.

14. Paragraph 5.13

The higher end of the scale will be reserved for the most serious contraventions such as hard-core cartel conduct (price fixing, market allocation and collusive tendering) and some forms of abuse of dominance or unilateral conduct (excessive pricing, predation, refusal to provide access to essential facilities, inducement-related practices and buying up a scarce supply of intermediate goods or resources)

14.1 Under this paragraph, resale price maintenance has been excluded from the list of conduct. Moreover, the Commission should take caution in equating unilateral conduct/abuse of dominance with hard-core cartel conduct. In cartel conduct, a contravention is clear *ab initio,*

but economic effects based conduct might not be. There ought to be a greater scope to settle at the lower end of the scale for such conduct.

14.2 The following qualification should be considered: so-called *per se* contraventions can still take the form of technical or bona fide contraventions, in which case, the conduct should not attract maximum penalties, despite technically falling within section 4(1)(b) of the Act. On the other hand, we fully accept that long running "hard core" cartels require harsher penalties to the upper end of the scale.

15. Paragraph 5.17

For contraventions relating to section 4(1)(b)(iii) of the Act, ie collusive tendering, the Commission will use the number of years for which the contract lasts, as the multiplier. In cases relating to compensation payments, the Commission may consider the duration as extending to the period up to at least the date when the final compensation payment was made.

15.1 This paragraph is vague as it is difficult to interpret the duration of the alleged conduct in certain contexts. There may be cases involving collusive tendering where the contract in issue does not have a fixed duration and is a service contract, for example in building maintenance. Furthermore, the use of the duration of the contract seems arbitrary. All other things being equal, there is no reason why collusive tendering in respect of, for example, the construction of a road that takes 10 years to build ought to attract a larger penalty than that in respect of a road that takes 5 years to build. This illustrates the irrelevance of the duration of the contract as a consideration in the determination of penalties for collusive tendering.

15.2 It is not clear why the date for a compensation fee is relevant. This paragraph appears to be an attempt to circumvent the statute of limitations in the Act by artificially extending the period of the collusive conduct, where such conduct in fact took place at a particular point in time.

16. Paragraph 5.19

As a general remark, if the respondent firm has a compliance policy in place, it should be construed as a mitigating factor to be taken into account under 5.19 of the Guidelines. This requirement should be included into the Guidelines.

17. Paragraph 5.9.1.5 and 5.9.1.7

Whether the firm continued with the conduct or ceased the conduct, following its knowledge of the Commission's investigation.

Evidence that demonstrates the termination of the conduct as soon as the Commission intervened.

It is difficult to understand why lenient treatment attaches to stopping only once discovered. It would seem that ceasing prior to investigation is more deserving, but is not mentioned.

18. Paragraph 5.19.2

Section 59(3)(e) of the Act which relates to the profit derived from contravention. This may include but is not limited to a consideration of an assessment of the level of profit achieved by the firm as a result of the contravention. The Commission notes that this may not always be possible to assess in all cases. This is because the benefits of participation in some anticompetitive conduct not only translate to quantifiable monetary benefit but also extend to the protection of participants from the demands of competition such as efficiency, investment and service. For 4(1)(b) cases, there will be a presumption that the conduct was profitable.

It is not self-evident that collusive conduct is always profitable. Moreover, the extent of profit should always be a relevant factor.

19. Paragraph 5.19.3

Section 59(3)(f) of the Act which relates to the degree of co-operation with the Commission and Tribunal. This may include but is not limited to a consideration of:

The extent to which the firm, inter alia, delayed, obstructed, and/or assisted in expediting the investigation and litigation process.

Whether the firm co-operated through tangible actions to facilitate the speedy resolution of the case.

As a general premise, it should be recognised that defending a case cannot be construed as a failure to cooperate.

20. Paragraph 6

20.1 Given the discretionary nature of the imposition of administrative penalties, limiting discounts to between 10% and 50% is arbitrary. Some thought could be given to a clear sliding scale similar to the one adopted in the US and/or UK to be used as a basis for the assessment of discounts.

20.2 Subject to the above proposal, it is proposed in the interest of transparency and certainty that the processes, discounts and calculation relating to settlements with the Commission be adopted in a similar fashion as the Corporate Leniency Policy of 2008 ("CLP").

20.3 On the basis of the principles enunciated in *Agri Wire (Pty) Ltd and Another v Commissioner of the Competition Commission and Others* [2012] ZASCA 134, and notwithstanding section 58 of the Competition Act, the Competition Commission may adopt policies or put in place measures that will enable it to pursue cartels and bring them to an end. In *Agri Wire,* the

Supreme Court of Appeal ("SCA") ruled that "there is no merit in…submissions" which state that the Competition Tribunal may still impose a penalty on a party which was granted immunity based on the Corporate Leniency Policy. In this regard, the SCA specifically stated:

"We venture to suggest that the CLP would be far less effective, if not entirely useless, if it contained a disclaimer to the effect that the Commission would not seek an order against the party seeking leniency, but that the Tribunal would be free to impose such administrative penalty as the Act permitted against them. Hard-headed businessmen, contemplating baring their souls to the competition authorities, will generally want a more secure undertaking of a tangible benefit, before furnishing the co-operation that the Commission seeks from them." (our emphasis)

20.4 On this basis it is suggested that the principles adopted would be more effective in the detection and prosecution of cartels if they were adopted in similar fashion to the CLP.

21. Paragraph 7.2

To be considered for this, the firm must provide the Commission with objective evidence that the imposition of the administrative penalty as provided for in these guidelines would irretrievably jeopardise the economic viability of the firm concerned and cause its assets to lose all their value. This evidence may include, but will not be limited to, audited financial statements attesting the veracity of the firm's financial position. The Commission will consider the financial viability of a firm as a whole and not of any specific division(s).

The test is too strict and is likely to cause difficulty in its application. For instance, under what circumstances will assets lose all their value? It is not clear why a significant reduction in competition is relevant to an ability to pay. This may prejudice small firms whose exit might not materially affect the market.

22. Paragraph 7.4

If a firm is able to demonstrate its inability to pay the administrative penalty in accordance with 7.1 and 7.2 above, the Commission may consider the use of favourable payment terms. The Commission will only consider a discount on this basis if a firm can objectively demonstrate that, even in the long term, it will still not be in a position to pay the administrative penalty.

The use of favourable payment terms should not be limited to an inability to pay in the strict sense.

23. Paragraph 8

23.1 As a general remark, parental liability under the context of paragraph 8 of the Guidelines is complicated and the Commission is urged to take extreme caution in this regard.

23.2 The following should particularly be noted -

(a) Paragraph 8.1 sets out the requirements for liability to be imputed to a holding company. Paragraphs 8.3 and 8.5 provide that, where liability is imputed based on the requirements set out in paragraph 8.1, the applicable statutory cap is based on the consolidated annual turnover of the parent company and not that of the subsidiary. However it is unclear where such an approach is sourced in the Act. In fact, to the contrary, the firms are separate entities with distinct legal personality. Section 1 of the Act defines a “firm” as including a person, partnership or trust. Section 59(2) provides, in turn, that an administrative penalty may not exceed 10% of “the firm’s” annual turnover in its preceding year. Yet nowhere in the Act, or in our case law, is it suggested that a “firm” includes a parent company and subsidiaries; and

(b) The word “or” at 8.1.3 suggests that these requirements are disjunctive (i.e. that each requirement is, on its own, sufficient) and not conjunctive (which would be indicated by the word “and”, and in which case each requirement would be necessary but not, on its own, sufficient). The implication is that, in a situation where a parent firm which does not:

(i) wholly owns its subsidiary (as required by 8.1.1);

(ii) have decisive or material influence over it (as required by 8.1.2);

(iii) have knowledge of its participation in the contravention (as required by 8.1.3),

but nevertheless (perhaps unwittingly) derives substantial financial benefit from the activities of its subsidiary (as required by 8.1.4), then the parent may nevertheless be liable, In practice, a holding company may control a subsidiary for competition law purposes, but have very little knowledge of its business decisions. Such a scenario does not appear to align even with the Commission’s own rationale for the inclusion of paragraph 8, which seems to be that parent firms which control or are aware of their subsidiaries’ unlawful behaviour must ultimately bear responsibility for it..

23.3 It is also not clear whether the Commission intends to impute liability to holding companies for the conduct or only for the payment of the fine (presumably on a "joint and several" basis). Moreover, it is not clear whether this will apply in respect of all firms that are controlled by another firm (as there are often more than one company 'controlling' another). This lack of clarity is problematic. As indicated above, there is no provision in the Act which allows for the offending conduct to simply be imputed to the holding company or companies (unless of course it can be shown that the holding company itself participated in the conduct). If it is considered from a policy perspective that parent companies should be held liable for the antitrust offences of their subsidiaries, a legislative amendment would be required. But, in such an instance, it is hoped that the legislature would also consider possible unintended consequences, namely that if the conduct is being imputed to the holding company, there are also implications in respect of damages claims, potential personal and criminal liability etc. If

liability for the conduct is confined to the subsidiary, it is clear that only the subsidiary should face liability for the penalty. That does not imply that the corporate group which includes such a subsidiary can merely escape the financial consequences of a penalty by liquidating the subsidiary. The common law adequately provides that the corporate veil can be pierced in these circumstances.

23.4 If the Commission intends the parent's turnover to be used for the purpose of determining the statutory cap in step 4 and step 6, it must again be pointed out that this is not justified by the Act. The term "firm" in section 59 simply does not have the expansive meaning that the Guidelines wish to impute to it. Should policy considerations dictate that the meaning should be expanded, it is a matter to be considered by the legislature. Careful thought could also be given to successor liability and whether there is room for this type of liability under paragraph 8.

24. General remarks

24.1 The Guidelines cannot have retroactive application and specifically cannot apply to any settlement agreements reached with the Commission prior to their publication, but which have not yet been confirmed by the Tribunal.

24.2 The Guidelines do not make provision for when, and under what circumstances, they will be subject to review processes.

16 February 2015