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Towards a fair and efficient economy for all.

IN THIS EDITION

Competition Commission

focuses on Service Standards

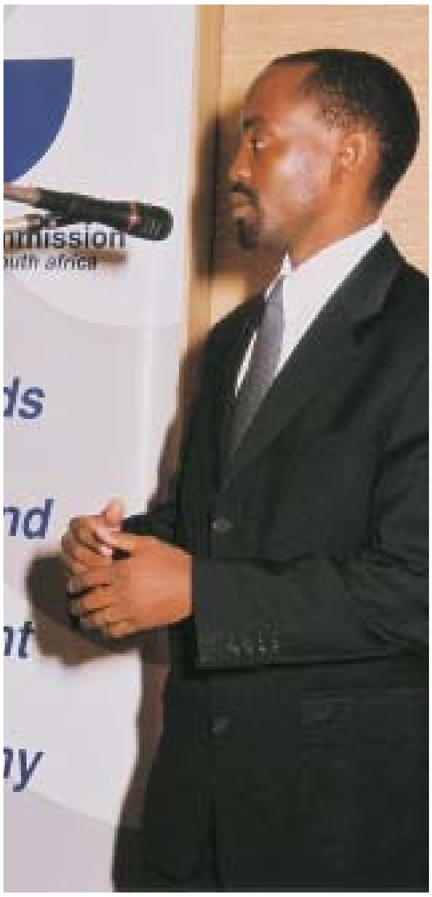
On 14 and 15 March 2002 the Competition Commission hosted a consultative conference focusing on service standards. The conference was held at the Sandton Convention Centre.

The need to review and revisit the Commission's service standards stems in part from analysis of the views articulated by various stakeholders. Whilst recognising the achievements and strides taken by the Commission in its first two short years of existence, the stakeholders seemed to be consistent in their observation that more work still needed to be done in order to propel the Commission into one of the best competition agencies in the world.

In embarking on this exercise, the Commission took a leaf from other leading competition agencies who had gone through similar exercises, such as the Canadian Competition Bureau and the Office of Fair Trading of the United Kingdom, to mention only a few. These agencies have, like the Commission, sought to identify the key factors that make for an effective competition regime. The Commission saw the need to incorporate a consultative conference into its process of setting service standards.

The Minister of Trade and Industry, Mr Alec Erwin, opened the conference. His address focused on the importance of competition policy as part of the economic policy of a country, particularly in the face of modernisation and globalisation. Mr Erwin also accentuated the importance of the Commission in the South African policy framework and announced that he had requested the Commission to launch an investigation into the increase in food prices as recently experienced in the economy.

The first plenary address was by



The Commissioner, Advocate Menzi Simelane, welcomed delegates to the conference and expressed his wish that the stakeholders participate in the conference in order to improve the service delivery of the Commission.

CONTINUED ON PAGE 2

FROM PAGE 1

Mr Nkonzo Hlatshwayo, Divisional Manager, Mergers and Acquisitions.

Ms Diane Terblanche, Divisional Manager Enforcement and Exemptions.

Mr Gaston Jorré, Senior Deputy Commissioner of Competition, Mergers Branch, Competition Bureau Canada. He spoke via a satellite link on *The Canadian Merger Review Process – Best Practice and Service Standards.*

Mr Nkonzo Hlatshwayo, Divisional Manager, Mergers and Acquisitions, Competition Commission listed stakeholders' complaints and concerns and explained how the Commission's Mergers and Acquisitions Division proposed to address these concerns and improve service delivery.

One of the strategies to improve service delivery lies with the **vigorous implementation of fast-track procedures**. The Commission proposed the following eight categories of cases that could ordinarily be regarded as fast-track cases when supported by the correct relevant information:

- Property transactions.
- Companies in liquidation (failing firms).
- Transactions where one of the parties is a new entrant into the market. Justification for this proposal lies in the fact that the transaction would normally represent the replacement of one participant by another.
- Management buy-out transactions are similar to new entrant cases and should therefore be treated in accordance with the above suggestion.
- No product overlap in respect of the product market and no vertical concerns.
- Where the parties to the merger are not in the same geographic market.
- Where the investigator has determined that the parties are in the same relevant market, both in terms of the product and geographic markets, but the combined market share post merger is less than 15%.
- Where the parties are in the same relevant market and their combined market shares are above 15%, but:
  - The post-acquisition HHI is below 1000 points.
  - Where the post-merger HHI is between 1000 to 1800, but the increase in HHI is below 100 points.
  - Where the post-merger HHI is above 1800, but the increase thereof is less than 50 points.

The Commission further stated that the categories do not reflect public interest issues and that, should any public interest issue arise, a case cannot be fast-tracked.

The Commission requires the correct and complete information in order to accept a case for fast-tracking.

The following information requirements have to be met for a case to be fast-tracked:

- All the forms and annexures must be included. This means, amongst others, that the business plans, annual reports and/or financial statements, board minutes relevant to the transaction, and complete lists of all the products and services of all the companies in the acquiring family and target firm.
- The filing must deal with a worst-case scenario in respect of the impact of the merger on employment.
- A comfort letter from the trade unions. This letter would convey that the trade unions were notified of the transaction and that they support the merger or would not oppose the merger.
- The description of the transaction should be clear and thorough.
- All the relevant information for market share calculation is included in the filing:
- Parties should not just provide their "conclusions" on the relevant market, but also the information these conclusions are based upon. The availability of the data used for the analysis would speed up the Commission's investigation.
- The relevant information on the activities of firms in the acquiring family must be supplied, not only those for the acquiring firm.
- When a market definition is proposed it is suggested that the parties put forward a narrow and a broad definition. If there are no concerns with market shares on the narrow definition, the case can be dealt with speedily.
- Vertical mergers should have information on two markets included. Two lists of customers and competitors must accompany the market definitions.
- There are no jurisdictional disputes. A matter that raises jurisdictional problems will not ordinarily be regarded as a fast-track case. However, to eliminate this problem, parties may be well advised to seek an advisory opinion

CONTINUED ON PAGE 3

FROM PAGE 3

prior to the filing when there is uncertainty on jurisdiction. Parties should then be transparent about the opinion upon filing.

As part of its commitment to service standards the Commission put the following to its stakeholders for discussion at the conference:

The Commission commits to maintain the following service standard with regards to merger review:

- Within three days of filing the parties will receive correspondence from the investigator assigned to the case.
- A CC13(2) will be supplied within five days, when applicable. No CC13(1) will be supplied.
- Parties will be informed within 15 days whether the proposed transaction raises initial competition concerns, what these initial concerns are, and what additional information will be required by the Commission to finalise the investigation and address the areas of concern. (These initial concerns do not in any way limit the focus of the subsequent investigation.)
- Merger investigations that raise no competition concerns will be completed and decisions taken within 20 days where filings are complete, correct and timeous; and accompanied by a comfort letter from the relevant trade union(s).
- Case investigators will provide regular feedback to parties.
- Case investigators will have more delegations afforded to them so that decisions can be made in shorter time periods.
- The Commission will have regular meetings to dispose of fast-track cases.
- The Commission will meet twice a week to deal with complex and problematic cases.

The second day of the conference focused on service delivery in terms of Chapter 2 investigations and advisory opinions. Ms Diane Terblanche, Divisional Manager Enforcement and Exemptions of the Competition Commission discussed, amongst others, the objectives and organisational values of the Enforcement and Exemptions Division, the stumbling blocks encountered by the Division, methods to address them, and benefits from the proposed changes.

Ms Terblanche also put forward the revised procedures and time-frames for investigations, exemption applications and co-operation with regard to advisory opinions for discussion and comment.

The Enforcement and Exemptions Division gave the following service standard commitment:

The Enforcement and Exemptions Division is committed to maintaining the following standards:

- Considering the views of all parties whilst remaining impartial.
- Treating all stakeholders with professionalism and respect.
- Adhering to the following time frames:
  - Acknowledgement and verification of complaint within two days.
  - Notification of name of investigator within seven days.
  - Constant and regular liaison with parties throughout the investigation.
  - Status report in month six after receipt of complaint by parties.
  - Prior to a recommendation of referral or non-referral, a request for input from complainant and respondent will be communicated. The time period allowed for input is two weeks.

Ms Zodwa Ntuli, Head of Corporate Compliance of the Competition Commission spoke on Service Standards for Advisory Opinions. Ms Ntuli informed stakeholders on what their expectations from the Commission should be. She stated that the Commission would always ensure that the services offered to its stakeholders met the standards acceptable to both stakeholders and the Commission.

Ms Zodwa Ntuli, Head of Corporate Compliance.

These time frames will be reviewed from time to time taking into account views of stakeholders, the cost of providing the service and best practice internationally.

The Commission is focused on service delivery to its stakeholders and to transform itself into a world-class competition agency.

SERVICE STANDARDS REGARDING ADVISORY OPINIONS

Service provided: Advisory opinion	**Maximum turnaround time**
In respect of mergers	
Non-complex	15 days
Complex	30 days
In respect of Prohibited Practices	
Non-complex	20 days
Complex	8 weeks
Other requests	
Non-complex	10 days
Complex	30 days

State Aid: The EU Review

1. Introduction

The major objective of applying competition policy in various countries or markets is to allow firms to compete on a level playing field. Competition policy seeks to encourage economic efficiency by creating a climate favourable to innovation and technical progress. It also makes it possible to ensure that any anti-competitive practices by companies or national authorities do not hinder healthy competition. It must also prevent states/governments from distorting the rules by discriminating in favour of public enterprises or by giving aid to certain private-sector companies (state aid), whilst discriminating against others.[1] This article attempts to review the EU competition policy with respect to state aid.

2. What is State Aid?

State aid concerns the intervention of government through a subsidy or provision of grants for a variety of reasons. This intervention should ensure the growth of the entire economy and not certain sectors at the expense of others. If aid gives the receiver an advantage over its competitors/rivals, it may be considered anti-competitive.

The EC Treaty considers any advantage granted by the state or through state resources as state aid where:

- it confers an economic advantage on the recipient
- it is granted selectively to certain firms or to the production of certain goods
- it could distort competition; and
- it affects trade between Member States.

3. The European Community Treaty and State Aid

The EU Treaty forms the basis and guidelines through which state aid cases are investigated. Article 87(1) (formerly Article 92) of the Treaty states that "any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market."

Thus, while the Treaty refers to aid "granted … in any form whatsoever", the community institutions (Commission and the Court of Justice) include any public aid or any aid granted by a local or regional authority. The aid may even come from a private body, such as a private company or a public company operating under private law, or from any other body over which the State, a public institution, or a local or regional authority exercises a dominant influence, directly or indirectly. Furthermore, the form and purpose of the aid and the reason for it are actually irrelevant; all that matters is its effect on competition. Therefore, not only positive contributions, such as subsidies, are considered as aid, but also any other measure which reduces the financial burden on a firm. In other words, and according to the EU competition law, the ban on state aid affects a very large number of aid measures, whether direct or indirect, of all types.

However, an absolute ban on state aid is impossible. Article 2 of the Treaty states that one of the Community's tasks is to "promote throughout the community a harmonious and balanced development of economic activities" and, given that economic development differs from one Member State to another and from one region to another, this task may require specific government intervention. Article 87(2) and (3), (formerly Article 92(2) and (3)), therefore provides for a number of exemptions:[2]

The following are compatible with the internal market (Article 87(2)):

- state aid having a social character, granted to individual consumers, provided that it is granted without discrimination related to the origin of the products concerned
- aid to make good the damage caused by natural disasters or exceptional occurrences
- aid granted to areas of Germany affected by the division of the country.

The Commission may also declare the following to be compatible with the internal market (Article 87(3)):

- aid to promote the development of certain activities or regions
- aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State
- aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest
- aid to promote culture and heritage conservation;
- other categories of aid specified by the Council.

CONTINUED ON PAGE 5

The EU Commission ensures that Member States grant only aid that is compatible with the common market. As such, Article 88 (formerly Article 93) provides that any aid or aid scheme must be notified to the Commission and approved by it before being put into effect. The Commission's incorporation with member states keeps all systems of aid existing there under constant review.

The procedural rules on state aid were consolidated and clarified in a Council regulation adopted in 1999 on the basis of Article 89 (formerly Article 94) of the treaty. Article 89 therefore allows the Council to adopt any appropriate regulations for the application of Articles 87 and 88 (formerly Articles 92 and 93). As of now, the Council adopted a regulation in 1998 enabling the Commission to exempt certain categories of horizontal state aid from the notification requirement. These are:

- aid to small and medium-sized enterprises, research and development, environmental protection, employment and training; and
- aid complying with the map approved by the Commission for each Member State for the granting of regional aid.

In other words, the EU Commission presently has the mandate to exempt aid cases that relate to public interest, aspects which are considered of importance by the South African Competition Act 89 of 1998. In 1999 the EU Commission adopted the first three draft exemption regulations concerning aid to small and medium-sized enterprises, aid to training and "de minimis" aid.

The EU commission has dealt with a number of cases that relate to state aid. It has covered a variety of industries such as transport, agriculture, fisheries and petrochemicals.

Relevance for SA

It is apparent from the EU approach discussed above, that the EC Treaty considers public interest issues of importance for State aid grants. In the case of South Africa, similar public interest issues might be expected to apply in the consideration of whether state aid is allowable or not, even if it affects competition.

1 http://europa.eu.int/scadplus/leg/en/lvb/l26055.htm

2 Treaty establishing the European Community, Section 2, P73.

State Enterprises and Competition Issues:

The Case of the South African Bureau of Standards (SABS)

1. Introduction

Standardisation is an activity that has been in existence for decades. It is sometimes referred to as an activity that is as old as mankind. It creates order, makes selections and formulates rules, the aim of which is to simplify, thereby promoting the overall economy in terms of human effort and material input. Furthermore, standards enable international trade to be conducted smoothly. The global standards development environment is facing unique challenges, and will probably change significantly over the medium to long term. Two distinct, but interrelated, drivers are of specific significance. The first driver relates to the commercial orientation of standards development organisations, and the second to the national interest role. Prior to restructuring and reformation in the SQAM[1] arena, the provision of these services has been seen to be the responsibility of government and government alone. However, of late, the importance of introducing competition, through commercialisation and letting the private sector perform some of the activities is considered the best approach. This brief summarises the findings of a research document prepared by policy and research regarding the SABS and competition issues.

2. Standardisation in South Africa

In South Africa, standardisation has been the responsibility of the South African Bureau of Standards (SABS). The SABS has been in existence since 1945. As a statutory institution, it was established in terms of the Standards Act amended several times, the last being in 1993. At present, it is known as the Standards Act 29 of 1993. Section 3 and 4 of the Act delegates and provides for the SABS to perform certain tasks deemed important for the country and the economy at large. It gives the SABS the sole mandate and powers to be the regulator, assessor and prosecutor in cases of non-compliance by companies.

Furthermore, SABS as a regulator and assessor was also a player/competitor in various markets through its own subsidiaries. This led to distortion of competition in various markets, with private companies complaining about the company favouring its own subsidiaries and not treating participants equally. Though Sections 3 and 4 of the Act[2] allow the SABS to establish its own companies and compete in the market, it does not prescribe how it should be done.

A need for an independent regulator, as compared to the SABS being both a competitor and regulator, was imperative. However, prior to the establishment of this independent regulator a number of policy documents[3] were released by both the Department of Trade and Industry (DTI) and the Department of Arts, Culture, Science and Technology (DACST). In 1996, SANAS was established and started operating fully in 1998. SANAS is now recognised as the single national authority for the accreditation of test and calibration

CONTINUED ON PAGE 6

FROM PAGE 5

laboratories, bodies for certification of quality and environmental management systems, product conformity certification bodies and bodies responsible for the certification of personnel and training. This institution took over the responsibilities of the SABS. After the establishment of SANAS, South Africa has seen the inflow of new entrants in the certification and testing market previously dominated by the SABS subsidiaries.

To further ensure that competition prevails in various markets where the SABS was operating, commercialisation of certain activities was important. This has seen the reorganisation of the SABS, which resulted in two sub-markets being the commercial and non-commercial markets. The main objective was to ensure that cross-subsidisation between these two markets was avoided. Prior to these developments there was no distinction between government-mandated activities and non-government activities. These conflicts have led to private sector complaints against the SABS. The split of the Commercial and Non-Commercial[4] activities of the SABS began in the last two years. It should be noted in advance that from 1 April 2001, the SABS has reorganised its activities, i.e. totally separating its commercial activities from the non-commercial, such that some of the major anticompetitive practices were eliminated.

3. Product/Service markets

The SABS markets are divided into the Commercial (where private companies are also competing) and non-commercial (government mandated activities). Since 1998, the SABS underwent a major restructuring process with the aim of providing a more business-like, cost-effective and customer-focused service.[5] The main object being to prevent cross-subsidisation, i.e. subsidisation of the commercial business units by state funds intended for mandatory activities. These markets are summarised below:

3.1 Non-commercial markets

3.1.1 Standard Development

The core business of the South African Bureau of Standards (SABS), as its name implies, is standardisation. Standardisation covers the activities of standards' development, publishing, sales, promotion and the provision of information.[6] The standards developed by the SABS include both voluntary and compulsory standards. Voluntary standards are customer or market driven, while the Government normally makes compulsory standards regulatory. It has the responsibility to declare any standard compulsory if it affects health, safety, the environment or consumer protection. About 2,5% of all standards are ultimately declared compulsory standards. This is usually determined by the Department of Trade and Industry, which is currently overseeing and driving changes regarding standards in the country.[7] The preparation of these standards in South Africa is still funded from the parliamentary grant and has lately been totally separated from the commercial activities of the SABS to avoid confusion and cross-subsidisation. Since standards development is considered an unprofitable market the state, in collaboration with the mandated body (SABS), determines the pricing of these products.

3.1.2 Regulatory service market

The main function of the Regulatory Division is to administer compulsory specifications (i.e. technical regulations). These standards mainly concern safety and health, and are therefore legally applicable to a wide variety of products ranging from car parts to certain foodstuffs. Compulsory specifications are administered by the SABS on behalf of the State. The products concerned are tested regularly for compliance with legal requirements. If necessary, an embargo can be placed on the sale of products that do not comply with relevant standards. The SABS currently administers all 56 of the compulsory specifications currently covered by the Standards Act. Their importance is emphasised on the WTO's Technical Barriers to Trade agreement, with which South Africa has agreed to comply. There are five areas of regulatory management in the SABS and they are: **i)** *Food and Fisheries;* **ii)** *Automotive;* **iii)** *Human, Health and the Environment;* **iv)** *Electro-technical, Electrical and Gaming;* and **v)** *Management of the Trade Metrology Act* (weights and measures). The testing and conformity assessment[8] of these areas is also open to private companies, with the SABS and other relevant government departments ensuring the accuracy of the results.

3.2 Commercial markets

The SABS commercial wing is divided into two sub-markets being Testing and Certification. The institution competes with various private companies in the provision of these services. Testing and Certification Specialists (Pty) Ltd (TCS (Pty) Ltd), is a subsidiary of SABS Holdings (Pty) Ltd. This company is one of the many companies which came into existence after the reorganisation or commercialisation of certain portions or sectors of the SABS. The company provides various services to clients and, as mentioned above, it competes with a number of private companies.

3.2.1 Laboratory testing market

Testing Services or Test House[9] falls under TCS (Pty) Ltd. Its business revolves around product conformity assessment and technical evaluation and surveys of products. Test House earns revenue by providing testing services for the manufacturing industry, importers, suppliers, consumers, Certification (SABS) and Regulatory (SABS). About 66 test laboratories covering a broad range of technologies are utilised for this purpose. The SABS Test House is considered the largest and most effective facility of its kind in Southern Africa and contains testing equipment with an estimated replacement value of more than R500 million. It provides testing services to the manufacturing industry, the food industry, government departments, the building industry, retail, SMMEs and the consumer. The client base of the Test House is notable at 4000. While this market seems competitive, other players in the market consider the nature and history of the SABS an impediment. This is discussed under the heading *competition issues*.

3.2.2 Certification market

Certification can be defined as "the process whereby an independent and accredited organisation certifies that a

CONTINUED ON PAGE 7

FROM PAGE 6

third party complies with certain requirements". There are three main certification schemes operating in South Africa. They are:

System certification schemes which involve the assessment/audit of a company's Quality (QMS) or Environmental Management System (EMS) to verify compliance with the International Organisation for Standardisation requirements. Approximately 14 QMS/EMS certification bodies are operating in both South Africa and the SADC region.

Product certification includes many of the aspects of System Certification and, in addition, includes the requirement that the product is tested to ensure compliance with a product specification, which may include additional (optional) quality and durability requirements. According to SANAS's database, there are few players in this market. The SABS seems to be dominant, with about 95% of the market. Its dominance is due to the SABS mark, which is a well-known mark in South Africa. As a result, the public would recognise products bearing the mark, and this means that most companies would prefer to certify their products with the SABS. This is to the disadvantage of other competitors providing similar services.

Consignment inspection: Consignments of goods are inspected and tested on behalf of the State and other major purchasers before shipment in order to verify compliance with the requirements agreed upon by sellers and purchasers. With its superb and expensive infrastructure, the SABS might be dominating the market and gaining from economies of scope. In addition to the markets discussed above, the SABS furthermore provides a variety of corporate services and these markets are highly competitive.

4. Potential Competition issues

It is apparent that the SABS is involved in a variety of markets. Apart from its mandatory activities – that is Standards development and Regulatory activities – the reorganisation of the SABS has resulted in the organisation taking part in different commercial markets. As mentioned above, it competes with a number of private companies, therefore business principles play a vital role. Prior to restructuring, the cross-subsidisation of commercial activities by parliamentary funds used to be prominent. This disadvantaged the SABS rivals since they are self-funding institutions. The following paragraph summarises potential anticompetitive issues as identified by the report.

4.1 History and reputation of the SABS

Sound competition policy recognises that markets without artificial borders introduced by governments or other public utilities, and those markets without distortions caused by anticompetitive business arrangements, benefit from the application of principles such as national treatment, nondiscrimination, and transparency.[10] The history of standardisation in South Africa also plays a vital role in this regard. Due to its reputation, reliability, its history and the SABS Mark, the organisation (SABS) enjoys the advantage of being the most preferred provider of services, which means that it has the opportunity of serving the bulk and major private customers in the country. In other words the reputation of the SABS, and the fact that it has been in existence for years, becomes a drawback to new players and as such is a barrier to entry.

4.2 Capital barriers

The services and activities offered by the SABS require large capital investments since highly technical and expensive machines are required to start the business, particularly laboratory testing and conformity assessment which are the major sectors of competition between the different players in the market. The SABS's infrastructure, such as laboratories, are run as commercial entities, but they have no cost of established capital outlays, i.e. equipment, buildings etc., since they were funded from government grants. This, therefore, offers the organisation an opportunity to out-compete its rivals, not because it is efficient and effective. Therefore, capital outlays are considered a barrier to entry.

4.3 SABS mark as a barrier

The SABS issues the SABS mark, which gives the manufacturer's goods a stamp of definable quality. This applies to products for which national mark specifications exist, with the SABS mark serving as testimony to the fact that the product complies with the specification and that the supplier maintains an efficient and appropriate quality system. SABS Holdings are using the SABS mark as a powerful marketing strategy. In the market for certification, the SABS mark as a brand has an advantage that will not easily be overcome on pure efficiency grounds. The mark is a sign of quality to South Africans and they have confidence in it. It will take some time for South Africans to change their attitude towards the importance of the Mark. This is at the expense of the other certified private companies operating in the various markets. As pointed out in the report, private companies have to contract with the SABS to access the mark, and a fee has to be paid.

5. Conclusions

Of the various competition issues identified above, the funding of the SABS by the State and the access to the SABS mark on a non-discriminatory basis appear to warrant further consideration. At the very least, taking note of these issues should be a useful platform as to how to respond to future complaints in this regard.

1 Standards, Quality Assurance, Accreditation and Metrology.
2 Note that the Standard Act is currently being amended to reflect changes within the SQAM arena.
3 These policy documents include The White Paper on Science and Technology, SA SQAM Report, A Review of State Owned Enterprises by the Department of Arts and Culture.
4 The new structure of the SABS is shown in an Appendix at the end of the full report.
5 South Africa Year Book, 1999, p458.
6 Department of Arts, Culture, Science and Technology, SABS Review, 1997.
7 An interview with Martin Kellerman, Director, SABS Non-Commercial.
8 Part of the commercial market.
9 Test House is an internationally recognised concept, involving the ability to test products against agreed standards and produce a test report or test certificate.
10 www.usdoj.gov:Globalisation and its implications for Antitrust Cooperation and Enforcement.

Transport Costs

and the relevant geographic market

The concept of a relevant market is very important to anti-trust economics and law, for the analysis of competition and dominance is always based on the presumption of a correctly defined product market, functional market, and geographic market. In terms of the product market, this will be determined by factors such as demand and supply side substitutability. The relevant functional market relates to the position of that product within the supply chain, from the various processes of manufacture, down to distribution and sale to the final consumer. Finally, the extent or size of the relevant geographic market will be defined by the ease with which the relevant product can be procured in different locations. In turn, this will often depend crucially on the costs of transporting that product from its supplier to consumers. This article will refer to two recent cases heard in the Tribunal, in which the definition of the relevant geographic market was argued.

• In Competition Commission v Patensie Sitrus Beherend (a former citrus co-op), a former member of Patensie complained that he was obliged to deliver all his oranges to Patensie, rather than being allowed to choose another pack-house. The Competition Tribunal found that the company's bylaws that forced members to deliver their produce exclusively to Patensie were anti-competitive in terms of section 8(d)(i), relating to restrictive vertical agreements. There was some argument over whether the relevant geographic market was confined to a localised river valley, or whether it extended globally.

The Commission and the respondent agreed (more or less) that the product market consisted of various types of oranges, but disagreed on what functional level to consider. The Commission adopted the position that it was only the market for the packing of citrus that was at issue. The bylaws of the Patensie pack-house affected farmers in respect of packing their fruit. The Commission argued that because farmers are restricted by transport costs to use pack-houses in the Gamtoos River Valley, the geographic market is confined to that River Valley.

The respondent, however, argued that the market was the global market for the final sale of citrus, of which Patensie constitutes a tiny fraction. Therefore the geographic market is the whole world.

In order to prove its case, the Commission relied on evidence of transport cost differentials for Patensie farmers between packing their fruit in Patensie (at Patensie Beherend or any other pack-house in that area) and in the closest alternative, the Sundays River Valley. It was found that the extra costs of transporting fruit to a pack-house in the Sundays River Valley amounted to about 20% of the total packing charge. The differential was computed as a percentage of the packing charges, including export agents' marketing fees, rather than as a percentage of the final price of oranges, because the relevant market was restricted to the service of packing the fruit. The inclusion of the export agents' fees was not necessary, as this is an 'appropriable' or distinct service in itself, although Patensie bundles together the services of packing and exporting its members' fruit. If transport cost differentials had been worked out as a percentage of packing costs only, then they would have exceeded 20%.

The usual anti-trust definition of a market relies on the 'hypothetical monopolist test', of whether suppliers will be able to implement a 5-10% increase in price of the product as defined, without that leading to a more than compensating decline in quantity demanded. If not, the size of the market should be expanded until the test is passed. In this case, the transport cost differential of about 20% means that pack-houses in the Gamtoos River Valley would be able to charge up to 20% more for their packing services before being constrained by competition from packers in the Sundays River Valley. That, for the Commission, was sufficient to define the

CONTINUED ON PAGE 9

FROM PAGE 8

relevant geographic market as being confined to the Gamtoos River Valley.

Once it was demonstrated that the market is confined to the Gamtoos River Valley, the dominance of Patensie Sitrus Beherend Beperk within that market was easy to show. That, in turn, allowed the Commission to proceed with its case against Patensie under section 8 of the Act, which relates to prohibited practices, but only in respect of dominant firms. The market share of Patensie in the market for packing services available within the Gamtoos River Valley is easily 70%.

- In the appeal against the Competition Commission's prohibition of the Astral/Natchix merger, transport costs of delivering animal feed in KwaZulu-Natal came under the spotlight.

Again, there was broad agreement on the product market (being various types of animal feed), but the geographic market was disputed. The Commission argued that the relevant geographic market for animal feed, for the purposes of this merger, was confined to the Natal Midlands, because of the costs of delivery from feedmills located outside that area. In contrast, the merging parties argued that the market extended at least as far as the whole of Kwa-Zulu-Natal. For its part, the Commission again relied on transport cost differentials, worked out as a percentage of the final price of the product (animal feed), and found that for farmers in the Natal Midlands area, purchasing animal feed from feedmills beyond that area would involve significant extra delivery costs. For example, these extra costs amounted to at least R208/ton from NLK in Dundee, which constitutes more than 10% of the price of the product.

The Commission also made use of the so-called LIFO/LOFI test (little in from out/little out from in), as devised by the economists Elzinga and Hogarty. This test establishes whether there is much movement of the relevant product into or out of the area being analysed. It was found that very little animal feed was being brought into the Natal Midlands area from outside, a result that satisfied the Elzinga/Hogarty test and confirmed that the Commission's narrow definition of the relevant geographic market was correct. In the end, the merger was allowed by the Tribunal, but only on condition that the parties sell off their interest in Natchix's Nutrex feedmill.

In conclusion, the definition of the relevant geographic market can be an important component of cases concerning both mergers and complaints. Two of the tests for establishing the extent of the geographic market are shipment studies (the Elzinga/Hogarty or LIFO/LOFI test) and transport cost studies. These can be important items in the economist's toolkit.

Mergers and Acquisitions

An Overview of Activity 2001/02

(Unaudited results)

The year ending 31 March 2002 saw a significant decrease in the number of merger notifications to the Commission. 407 cases were notified in 2000/01 and 220 in 2001/02. This decrease can be attributed to the change in thresholds for notification. Interesting to note is that although the number of mergers decreased, the number of large mergers increased from 16 to 47. In addition to the number of large mergers the Commission also found that the complexity of cases increased during the past financial year. More and more cases require team members from other divisions in order to do thorough analysis.

The decrease in notifications led to a significant improvement in turnaround times, from 48 days in 2000/01 to 30 days in 2001/02.

TABLE 1: OVERVIEW OF CASES NOTIFIED AND FINALISED

	2001/02	2000/01	1999/00
Number of cases notified	220	407	331
Number of cases finalised	225	414	236

TABLE 2: MERGERS BY TYPE

Type of merger	Percentage (%)	
	2001/02	2000/01
Purely horizontal	66.0	62.0
Purely vertical	9.5	9.0
Conglomerate	13.0	22.0
Management buy-out	10.5	2.0
Horizontal-vertical mix	1.0	5.0
Total	100	100

CONTINUED ON PAGE 10

FROM PAGE 9

The year 2001/02 saw a decrease in conglomerate mergers, but an increase in management buy-outs. Management buy-outs are considered to be non-problematic and pro-competitive as they usually signify a new entrant into the market. The increase in the complexity of cases thus cannot be explained by changes in the types of mergers notified.

Foreign Direct Investment

The percentage of cases with a foreign direct investment component decreased from 19% in 2000/01 to 10% in 2001/02.

Black Economic Empowerment

Of the cases evaluated by the Mergers and Acquisitions division, 4,5% of the cases had a black economic empowerment dimension to them, whilst 10% of the cases involved some form of foreign direct investment.

Failing Firm

The failing firm argument or defence was used in 6,5% of cases during the 2001/02 year. This is a slight increase from the 5% of cases in the 2000/01 year. A prominent example of the failing firm argument was the Saldanha Steel/Iscor merger.

Employment

The percentage of cases where job losses were anticipated was 6% in 2000/01 and nearly 25% in 2001/02. This is a significant increase in the number of cases with anticipated job losses.

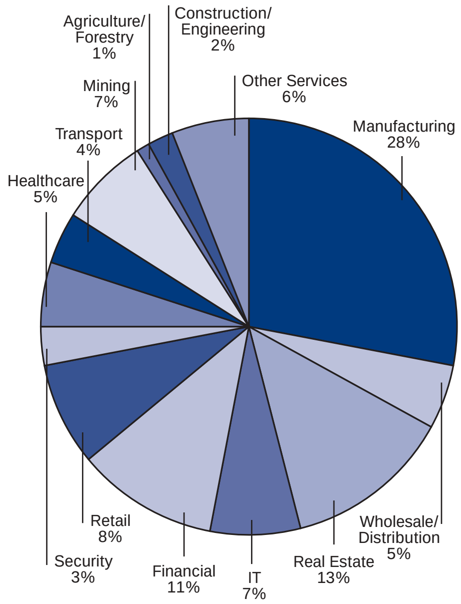
The total number of job losses anticipated was 7 735. Employment gain was estimated at 2 243 jobs. 57,75% of the job losses were due to mergers in the mining sector; 19,6% to mergers in the manufacturing sector and 14,23% to mergers in the financial sector.

Although mining sector mergers were responsible for most of the job losses, most of the employment gains due to merger activity could also be found in this sector. 1 750 Job gains (78% of the total) came from the mining sector. The sector did, however, have a net loss of 2 795 employment opportunities.

Other sectors with employment gains were manufacturing and forestry. Forestry was the only sector with a net employment gain of 146 opportunities.

The manufacturing sector remains the area of most consolidation activity, although with a decline from a third of all cases in 2000/01 to 28,5% in 2001/02. The increase in real estate transactions as a percentage of all transactions continues at a steady pace, indicative probably of not only the activity in the sector, but also the acceptance of competition legislation by parties active in this area. The other point to note is that property mergers are analysed on a smaller geographic level, thus seldom raising competition concerns. The financial services sector also afforded an increase in transactions, a trend that will probably continue as consolidation in the financial services sector takes place.

FIGURE 1: SECTORAL OVERVIEW OF MERGER ACTIVITY



In terms of quarterly trends, merger activity consistently peaked in the manufacturing sector, albeit with a decline in the third and fourth quarters. Furthermore, whilst merger activity increased consistently in the retail, mining and IT sectors during the first three quarters, all three sectors experienced a decline in the last quarter. Merger activity in the real estate sector has been erratic, with increases in the second quarter, followed by a decline in the third quarter and a further increase in the fourth quarter.

TABLE 3: SECTORAL BREAKDOWN OF MAIN MERGER ACTIVITIES

Sector	2001/02	2000/01
Manufacturing	28,5	33,0
Real estate	13,5	8,0
Financial services	12,0	6,0
Retail	8,0	6,0
Information technology	7,5	11,0
Mining	6,5	4,0

"The Competition Commission reviews public interest issues when notified of M&A activity, including impact on employment, black empowerment and international competitiveness."

Overview of Enforcement

and Exemptions activity

(Unaudited results)

As at 30 April 2002, 67 cases were under investigation in the Enforcement and Exemptions division. A sample of 38 cases were analysed and the results revealed that 47% of the cases are investigated under Sections 8 and 9 of the Act, which prohibits the abuse of a dominant position, 29% of cases are investigated under more than one Section of the Act, while 13% and 11% of the cases are investigated under Sections 4 and 5 of the Act respectively.

46% of the multi-dimensional cases are investigated under Sections 5, 8 and 9 of the Act. Section 5 deals with the vertical relationship between a firm and its customers or suppliers. This section only raises significant competition concerns when either firm, in the upstream or downstream market, is dominant. 27% of the multi-dimensional cases have an element of an abuse of dominance, horizontal restrictive practice, and vertical restrictive practice.

The Enforcement and Exemptions division is currently investigating two exemption applications. One is in the finance sector, and the other in the transport sector. There are 13 cases currently at the tribunal stage, awaiting hearings. Of the 13 cases, five deal with an abuse of a dominant position and four deal with more than one prohibition of the Act. Two cases each are being tried for violations of Sections 4 and 5 of the Act.

TABLE 1 : CASES PER SECTION OF THE ACT

Section of the Act	Number of cases	Percentage of total
Section 4	5	13%
Section 5	4	11%
Section 8 & 9	18	47%
More than one section	11	29%
Total	**38**	**100%**

TABLE 2 : MULTI-DIMENSIONAL CASES

Combinations	Number of Cases	Percentage of Total
Section 4 & 5	1	9%
Sections 4, 8, & 9	2	18%
Sections 5, 8 & 9	5	46%
Sections 4, 5, 8 & 9	3	27%
Total	**11**	**100%**

Commission Cases

Competition Commission prohibits merger between Mondi and Kohler

The Competition Commission has recommended a prohibition of the merger between Mondi Limited and Kohler Cores and Tubes to the Competition Tribunal.

Mondi Limited (Mondi), a wholly owned subsidiary of Anglo American plc, notified the Commission of its intent to acquire Kohler Cores and Tubes, a division of Kohler Packaging Limited (Kohler Packaging) as an alternative to starting its own cores and tubes manufacturing business. Cores and tubes are spirally wound paper tubes, which are used for various applications as an inner core for winding products thereon, such as paper, board, steel, textiles and plastic.

An objection from Diversified Cores and Tubes was subsequently lodged, which claimed that the merger would be financially detrimental to its business.

Following an investigation, the Competition Commission recommended a prohibition of the merger because the transaction would have given rise to the only vertically integrated entity in the core and tube manufacturing industry.

Secondly, the Commission found that the merged entity's dual position as supplier of paper and core board and competitor of cores and tubes would be likely to create a channel conflict in the market. Using its strong market position as supplier of the raw material, the merged entity might have been able to raise core and tubes manufacturers costs and marginalise their market position as suppliers of cores and tubes.

Furthermore, the Competition Commission found that the merger may have resulted in foreclosing existing and potential suppliers' paper and core board. This is used in conjunction with Mondi's Ndicore

CONTINUED ON PAGE 12

core board, for producing cores and tubes in both the high-end and lower end of the market.

In a previous case referred to it, the Competition Tribunal concluded that increased barriers to entry, market foreclosure, and the ability to raise rivals' costs were of most concern in a vertical merger. A vertical merger may foreclose new entry by eliminating potential purchasers or suppliers for a potential entrant. Raising rivals' costs can be described as a form of non-price predation, which raises rivals' supply cost. [See Case No: 23/LM/May01, Merger between Schumann Sasol (South Africa) (Pty) Ltd and Price's Daelite (Pty) Ltd, 18 July 2001, available on the Competition Tribunal website, www.comptrib.co.za.]

Both the upstream (supply of paper in this case) and downstream (cores and tubes industry) markets must be conducive to the exercise of market power. The Commission concluded that both markets are highly concentrated in this industry and, as stated, the merger might have created a structure that could give rise to both foreclosure and raising rivals' costs.

The Commission found that potential job losses would not have been sufficient to raise significant public interest concerns.

The fundamental problem with the merger would have been structural. Mondi can still enter the market on its own without prohibitive costs. Since the structure of the merged entity would have ensured that a crucial input – Ndicore core board – would have been available only to the parties and possibly not to competitors, the Commission recommended against the merger. Were Mondi to decide to enter market on its own, the Commission concluded it would have continued to supply other customers with the key input.

The Tribunal subsequently upheld the decision of the Competition Commission.

Competition authorities' ruling to benefit small farmers

Recently, the Competition Tribunal upheld a Competition Commission decision which sought to protect small farmers. The ruling voided certain articles of association of the former co-operative Patensie Sitrus and found that the company was contravening the Competition Act of 1998 by prohibiting competition.

The decision has implications for compliance by the larger farming companies and should make competition more vigorous for farmers at the smaller end of the scale.

Because of the way cooperatives now work as companies, the ruling protects farmers who are made to be, and are bound as, shareholders. To the extent that small farmers become shareholders, farmers will still have obligations if they have signed contractual agreements, but the company (formerly co-op) can no longer oblige small farmers to surrender their production to it. This is why the Commission criticised the articles of association. Farmers can still be members of these companies, but they should be free to sell their products elsewhere, unless bound to contractual obligations.

Though the Commission could have fined Patensie, for acting in an uncompetitive manner thereby contravening the Act, it elected not to do so because it would have punished the same individual farmers (as shareholders liable for the fine) it was trying to protect.

Competition Commission approves Computershare acquisition of Mercantile interest with conditions

The Competition Commission had given conditional approval for the acquisition of certain interests held by Mercantile Lisbon Bank Holdings Limited (Mercantile) by two subsidiaries of Computershare Custodial Services Limited (Compushare). The merger size was categorised as 'intermediate'.

The merging parties would dominate the share registry market in South Africa and so raise significant competition concerns, which were ameliorated by public interest concerns. And because of the introduction of STRATE (Share Transactions Totally Electronic), additional mitigating circumstances were considered. Consequently, the Commission approved the transactions, applying two conditions to the approval.

Income in the registry market will be limited following the advent of STRATE. In time, the dematerialisation of shares will contribute further to the natural consolidation in the market, which has left only Computershare, Mercantile and Ultra Registrars (Pty) Ltd as market participants. The natural decline in the market and sufficient constraints exist to suggest deterrents for the parties to abuse their market dominance.

Ultra Registers (Pty) Ltd was set up in 2000 and formed an alliance with Mercantile, whereby Ultra uses

CONTINUED ON PAGE 13

Mercantile's STRATE-compliant system and Mercantile, in return, holds a 45% shareholding in Ultra. Because the merger will create a dominant player in the market, the conditions are designed to bolster Ultra's competitiveness: Mercantile should sell shareholding in Ultra back to Ultra and should provide Ultra access to the Mercantile system for a period until the end of December 2002.

The conditional approval was endorsed by the Financial Services Board.

Anglo American Medical Scheme vs USAP

These complaints related to an alleged cartel in the supply of prescription medicines to members of the two schemes. It was averred that a large number of retail pharmacies had formed an association named United South African Pharmacies (USAP) which negotiated with medical schemes on their behalf and which recommended the terms on which the schemes should be supplied. Moreover, a form of boycott was also recommended against certain schemes who insisted on discounts that were above what USAP considered to be reasonable.

The Commission was satisfied that a referral in terms of section 4(1)(a) and 4(1)(b) could be substantiated on the evidence before it.

Competition Commission approves Nampak-Malbak merger with conditions

The Competition Tribunal upheld the decision by the Competition Commission to approve the acquisition of Malbak Limited (Malbak) by Nampak Limited (Nampak).

The companies are both listed in the packaging sector of the JSE Securities Exchange.

The parties submitted that packaging customers in the global food, beverage and retail sectors are consolidating and creating pressure on margins for packagers, obliging them to seek critical mass, economies of scale and greater facility to accommodate exporting customers. A significant portion of Malbak's turnover is offshore, making it an attractive target for Nampak in this operating environment, particularly as there is weak domestic demand for packaging.

Overlapping products and markets between the two companies include folding carton products, paper labels and flexible packaging. The Commission reviewed market shares, barriers to entry and countervailing power for each product market and concluded that there were competition concerns only in the flexible thermal roofing insulation market.

Market shares for both Nampak and Malbak in the thermal roofing insulation market are very high and the market will be highly concentrated post merger. The Commission was concerned that an effective competitor would be removed from the marketplace and that there would be no effective countervailing power, imports, or any other mechanism to prevent a substantial lessening of competition. Therefore, they recommended to the Tribunal that the merged entity must divest the Bubblepack insulation machine currently manufacturing the products Alucushion, Alububble and Bubblefoil.

While there were other products and markets overlapping, powerful customers, the procedures for international tendering and smaller players in the market continuing to operate in the domestic market were factors which convinced us the operating environment would prevent the company from abusing its dominance. In fact, this countervailing power indicates that the merged entity will have no market power to influence prices.

The Competition Commission reviews public interest issues when notified of M&A activity, including impact on employment, black empowerment and international competitiveness. In this merger, the Commission deferred to testimony from the parties that it would have minimal impact on employment and that exports could double in the next two years.

Competition Commission recommends conditional approval for Distillers and SFW merger

Following the Competition Appeal Court ruling that the transaction between Distillers Corporation (SA) Limited and Stellenbosch Farmers Winery Group Limited (SFW) constituted a merger, the Competition Commission has completed its investigation considering the anti-competitive effects of the merger and recommended that it be approved subject to several conditions.

Both companies are engaged in production (including blending and bottling), wholesale distribution and marketing of alcoholic beverages. Both parties also buy wine and raw material used in the production of beverages.

It is the Commission's view that this merger has removed an effective competitor in some of the product markets examined by the Commission and created the architecture for anti-competitive behaviour.

The Commission defined the market segmentation narrowly by spirit type, different types of wine (table wine, sparkling wine and fortified wine), and the market for flavoured alcoholic beverages (FABs). It was found that product overlap between the two parties occurred in nine markets: whisky, brandy, vodka, cane, gin, table wine, sparkling wine, fortified wine and FABs.

The Commission found that there are high barriers to entry, chiefly manufacturing, distribution, branding, and that these barriers are difficult to overcome. It also found that the 'portfolio effect' of the merged entity – where a combined range of brands and products can afford the parties greater flexibility to structure prices, promotions and discounts – also contributed to these high barriers to entry.

Strong competitors still exist in the whisky, vodka, cane and table wine markets. The Commission determined that the FAB market was subject to fashion and was highly volatile. Consequently, the Commission seeks no remedies in these markets.

However, the brandy market is highly concentrated, with the parties controlling in excess of 20 brands, equating to a cumulative market share of approximately 70% in volume and 75% in value. Further, it is legislated that 30% of brandy must be matured for three years. Only Distell and KWV control this 'raw material'.

Similarly, the parties dominate and hold all the major brands in the market for sparkling wine. The high concentration of market share, approximately 75%, is

CONTINUED ON PAGE 14

growing. The Commission had no doubt that the merger has substantially prevented or lessened competition in this market.
The gin market, in which the parties currently control 68%, includes a licensing agreement for Gordon's Gin, which is currently under litigation. Notwithstanding competition concerns, any recommendation by the Commission relevant to this market would be overwritten by the outcome of litigation.
When approaching remedies to counter the anti-competitive affects of the merger, the Commission also examined public interest issues and any efficiencies or countervailing powers the parties could demonstrate.
The Commission concluded that the positive aspects of the parties' export initiatives in the table wine industry satisfied the definition of a public interest issue under Section 12(3)(d) of the Competition Act of 1998 to compete in international markets and that it could ameliorate the anti-competitive effects of high market share.
While the Commission acknowledges that efficiencies will flow from the merger and some will address the anti-competitive concerns raised by the merger, it is extremely difficult to quantify the anti-competitive effects of the merger as it is highly unlikely that the parties would act anti-competitively in a period of regulatory intervention. Nevertheless, the Commission finds it highly unlikely that the efficiencies gained from the merger would outweigh the anti-competitive effects.
The positive effects of efficiencies must be passed on to consumers and not just shareholders.
In order to alleviate the competition concerns in the following markets, the Commission recommends the following remedies:
The Commission identified KWV as a potential competitor to Distell in the brandy market and accordingly recommend that Distell be precluded from distributing KWV brandy brands. With regard to high market concentration, the Commission has recommended the divesiture of certain brands, which constitute a portion of the market share in this market.
The Commission also recommends divestiture of a portion of Distell's market share in sparkling wine.

South African Regulators

launch new Forum to integrate policy framework

The Competition Commission, spearheading the drive to convene regular meetings between South African regulatory bodies, has announced the launch of the Regulators' Forum. The aim of the Forum is to promote transparent, consistent and coherent business regulation.

"We hope to harmonise the myriad of regulations governing business activity – both parastatal and private – through better communication and co-ordination of policy. It is important that we ensure our combined approaches to various issues, so that stakeholders enjoy the benefit of certainty and consistent regulatory processes," said Commissioner Menzi Simelane from the Competition Commission.

Advocate Menzi Simelane was elected Chairperson and Doctor Snowy Khoza from the National Electricity Regulator was named Deputy Chairperson of the Forum.

Amendments to the Competition Act of 1998 last year gave the Commission

CONTINUED ON PAGE 15

concurrent jurisdiction over competition matters across all sectors. The Commission may now negotiate agreements with other regulatory authorities, participate in their proceedings, and advise or receive advice from any regulatory authority.

The creation of this concurrent jurisdiction means that the competition authorities remain responsible for competition regulation (which includes preventing firms from concluding anticompetitive agreements, abusing dominant positions and implementing anticompetitive mergers). Sector regulators remain responsible for technical regulation peculiar to their specific sectors. Economic regulatory responsibilities may be allocated to the competition authorities or a sector regulator, depending on the needs of a particular country and sector.

"As competition policy evolves in tandem with the privatisation of state enterprises, the need for a more co-ordinated approach is necessary in order to ensure that markets are as efficiently "self-regulating" as possible. The objective of the Forum is to avoid ambiguity and contradictory regulations," explained Simelane.

He said that regulation, whether sectoral or economy-wide, required a range of expertise and skills that may not necessarily be found in a single regulator. As the economy-wide regulator, the Commission may be in a position to provide information relating to all sectors, while sector regulators may provide information and expertise on specific sectors.

The launch of the Forum is the culmination of many meetings and discussions between the various regulators involving the drafting of the Constitution in terms of which the Forum will operate.

The regulatory institutions in South Africa comprise of:

- The Independent Communications Authority of South Africa (ICASA)
- The Registrar of Banks at The South African Reserve Bank (SARB)
- The National Electricity Regulator (NER)
- The Postal Regulator (PR)
- The Financial Services Board (FSB)
- The Securities Regulatory Panel (SRP)
- South African Bureau of Standards (SABS)
- The Roads Agency (RA)
- The Civil Aviation Authority (CAA)
- The Medical Council
- The National Gambling Board
- The Wine and Spirit Board
- The National Agricultural Marketing Council
- The Liquor Board
- The Estate Agency Affairs Board
- The Competition Commission

Adv Menzi Simelane and Dr Snowy Khoza at the launch of the Regulator's Forum.

Competition Commission

and ICASA complete concurrent jurisdiction agreement

Following the merger review of the Stanbic / Nedcor transaction last year, the Competition Act of 1998 was changed to accommodate concurrent jurisdiction between South Africa's regulatory bodies and the Competition Commission. On 23 April 2002 the Commission and ICASA presented the first such Memorandum of Agreement detailing how they will co-operate in respect of the investigation, evaluation and analysis of mergers and acquisition transactions and complaints involving telecommunications and broadcasting matters.

The agreement is designed to assist the two regulators to form a working partnership and will be adopted following

ICASA

competitioncommission south africa

CONTINUED ON PAGE 16

FROM PAGE 15

a two-week period during which the public may comment, said Competition Commissioner, Advocate Menzi Simelane. ICASA and the Commission will continue making independent determinations on the basis of the criteria and mandates of their respective legislation. Similarly, none of their respective powers will be waived. The partnership between the regulators will allow for more formalised consultation regarding transactions and could minimise the negative impact on the stakeholders at the end of the day, explained Simelane, by, for instance, consolidating any penalties or fines.

The Chairman of Icasa, Mandla Langa, said at the briefing: "The publication of a draft Memorandum of Agreement between the Competition Commission and ICASA is an important milestone in the history of regulatory cooperation in South Africa. By agreeing on the management of concurrent jurisdiction over competition matters in the telecommunications and broadcasting industries, the Commission and the Authority are also sounding a warning to those who abuse their dominant positions in these sectors. This agreement should be seen as another indication of ICASA's commitment to promoting competitive markets in the broadcasting and telecommunications sectors."

Commissioner Simelane expressed similar sentiments saying, "We hope the agreement will create certainty for the parties involved in corporate activity in this sector. By harmonising operations and creating an overarching framework under which stakeholders are regulated, the process should be faster and more efficient overall."

The Competition Commission is currently negotiating similar Memoranda of Agreements with a number of other regulators, including the National Electricity Regulator, the Reserve Bank and the Financial Services Board.

International News

Dominance to the Test – The case of Napp Pharmaceuticals

The UK Competition Tribunal has fined Napp Pharmaceuticals, a pharmaceutical company based in the UK, a fine of 2.2 million pounds for infringing Chapter 2 of the Act by abusing its dominant position in the market for the supply of sustained release morphine tablets and capsules in the UK.

The case involved allegations of predatory and excessive pricing. The Office of Fair Trading (OFT) found the relevant market to be the "supply of sustained release morphine tablets and capsules in the UK". Within the market, OFT identified two distribution channels servicing two different customer groups: supply to hospitals and supply to the community. About 86 to 90 percent of sales are to the community segment. The Tribunal found that while sales to the hospital segment were small in comparison to the community segment, it played a key role in determining the point of entry into the entire market. In the hospital segment, hospitals purchase the drugs from Napp, either individually or as a collective, while in the community market, Napp sells to wholesalers who then sell on to individual pharmacies.

The Tribunal agreed that Napp was dominant by virtue of its high market share in both market segments, and that Napp's market share had remained high long after the expiry of its patent, which the Tribunal found to be unusual, as one would expect the firm's market share to decline as its patents rights are removed. Furthermore, dominance was strengthened due to the existence of barriers to entry created through Napp's first mover advantage.

Two abuses were alleged: a) excessive discounting in the hospital segment, and b)

CONTINUED ON PAGE 17

International News continued...

FROM PAGE 16

excessive pricing in the community segment. The Tribunal found that in 1996, Napp was discounting in excess of 90%. On four strengths of tablets it was found that prices were below the direct cost to Napp (calculated by taking materials and labour costs as proxy for variable costs), and in some cases 30% to 50% below direct costs. The Tribunal also rebutted Napp's defense of "follow on effects" in which it proposed that in about 15% of cases the choice of sustained release morphine tablets is determined by the choice of the hospital doctor and that it competed in the hospital segment in order to obtain the linked sales to the community segment which was rational for it to do. It further argued that this follow on effect was at a ratio of 1:1.35. and its pricing decision was based on this.

The Tribunal found that Napp's pricing was driven by a "hospital influence" which recognised the importance of the hospital segment to the community segment in determining choice and influencing sale to the market as a whole. "Hospital influence" refers to the case where a patient starts a drug in hospital and who continues to be prescribed the drug in the community, and other ways in which hospitals influence community markets such as referral letters, hospital training programs of GP's and pharmacists. The Tribunal argued that Napp's discounting in the hospital segment resulted in barriers to entry, thereby driving competitors out of the market, and giving rise to a virtual monopoly in the community segment (due to the follow on effects) that then allowed it to maintain and derive monopoly profits. The Tribunal further said that there is only one point of entry into the market, which is through the hospital. Foreclosure to this market foreclosed entry in to the community market. "Napp had the key to the only viable point of entry to the market, but chose to keep that gate locked".

On the charge of excessive pricing in the community segment, the Tribunal found that Napp had charged significantly higher prices to the community segment than in other segments where it faced competition, and that it had significantly higher margins in this sector than its nearest competitors. Prices in the community segment were found to be 500% higher than in the export segment and for some tablets, 1400% higher than the hospital segment.

EU Green Paper on Merger Regulation

On 11 December 2001, the European Commission released its Green Paper on Merger Review. The purpose of the Green Paper is to initiate a discussion on the existing merger regulation.

The Green Paper's three main ideas are:

- changing the EU test from a "dominance based test" to one of "substantial lessening of competition"
- extending the operation of the "one-stop-shop" to cover mergers that would be notifiable in three member states
- introducing a "stop the clock" provision for remedy proposals.

There are basically two legal tests for merger review: the "dominant position test" and the "substantial lessening of competition test". The EC adopts the former while many of its members use the latter, US based approach. The "dominance test" requires one to determine whether a merger would create, strengthen or enhance a dominant position. This test often encourages an excessive focus on the relative strength of competitors, and does not provide enough focus on the impact of the merger on consumers.

The substantial lessening of competition test is more economic oriented and is broader than the "dominance test", since the lessening of competition may result from the creation of a dominant position, but not solely. The "substantial lessening of competition test" asks whether a merger would substantially lessen or reduce competition in a market if it is approved. In the US based test, a merger is allowed to proceed if the benefits arising from the merger outweigh the anticompetitive effects. In the GE/Honeywell case, the US department saw efficiencies where the Commission saw none, yet both parties were looking at the same facts.

A change to an economics based approach would be more suited to addressing industrial concentration and globalisation, as well as collective dominance and oligopolistic dominance. It would also create a more uniform international standard of merger assessment allowing for greater consistency between international competition authorities. The US "substantial lessening of competition test" is considered to be more flexible than the European approach of dominance.

In the EC there are certain turnover thresholds that serve to allocate jurisdiction between the EC and its member states. The EC has jurisdiction to deal with merger cases that fall above a certain minimum threshold, while the national authorities have jurisdiction to deal with all cases that fall below the threshold. A common criticism of this method has been that while some cases

CONTINUED ON PAGE 18

International News continued...

FROM PAGE 17

reviewed by the Commission have no community interest, there are mergers that are of community interest but are not reviewed by the Commission.

In this regard the Green Paper on Merger Regulation suggests a move away from the "one stop provision" to a "three member state rule", in which the EC would review all cases qualifying to be notified in three or more Member States. No minimum turnover requirement would apply. The Green Paper has been severely criticised for not tackling these issues, but simply tinkering with the existing regime. Some questions raised by competition law practitioners are the requirements for Member States to notify the transaction if it falls within a three-member state jurisdiction, and how consensus would be reached among the member states.

The Commission in its Green Paper has also proposed the introduction of a “stop the clock" provision, allowing extension of time periods in order to assess remedies. This proposal would give parties the chance to "stop the clock" for 15 - 20 days during the remedy stage (Phase ii or just before the end of the three month period), allowing them time to improve a remedy proposal if the Commission finds the first offer unacceptable. This would introduce the concept of "negotiation" into the merger process, which the Commission has always resisted. However, many practitioners have welcomed the idea as it gives the parties more time to contemplate and discuss remedies after the competition review process. Certain business leaders have said that "allowing more time is essential" since the Commission has been poor at hinting what its concerns are and has the tendency to rather surprise people. Johan Ysewyn, of the EU and Competition Group of Linklaters and Alliance in Brussels, has said that "the risk of the Green Paper’s proposal is that The Merger Task Force would let the timing of the statement of objectives slip even further, knowing that the parties will stop the clock anyway". It is therefore important to require that the Merger Task Force issues its Statement of Objections by a specified date.

Commission and Tribunal Dispute over Merger Provisions

The Canadian Competition Bureau has filed a Notice of Appeal with the Federal Court of Appeal regarding the Competition Tribunal’s second decision on the Superior Propane/ICG Propane merger. In this case, the Tribunal concluded that the merger was anti-competitive and would create a monopoly in many markets resulting in negative consequences for consumer choice, services and price in Canada. In assessing the efficiencies, the Tribunal concluded that the efficiencies outweighed the anti-competitive effects of the merger. The Federal Court of Appeal, however, instructed the Tribunal to re-examine the case and to take into account public interest issues. It said: "The Tribunal is charged with the responsibility of protecting the public interest, which it does by striking a balance between conflicting interests and objectives”. The Tribunal, however, disagreed with this and said that it was not the Tribunal’s mandate to consider public interest issues. Competition Commissioner Konrad van Fickenstein said: "this fundamental disagreement is the key reason for our appeal". The Tribunal’s interpretation that efficiencies were the fundamental objective of the merger provisions of the Act was unacceptable. He further said that the Federal Court of Appeal had instructed the Tribunal to consider other objectives of the Act, such as the impact on consumers, and small and medium-sized businesses.

IBA hosts conference in Cape Town

On 18 March 2002 the International Bar Association (IBA) hosted a conference on *Competition Law and Policy in a Global Context* at the Mount Nelson Hotel in Cape Town. It was the first time the competition section of the IBA hosted a conference in Africa.

The conference was co-chaired by J William Rowley QC, Chairman of McMillan Binch, Toronto, Ontario and representing the IBA Global Forum for Competition and Trade Policy; and Advocate Menzi Simelane, Commissioner of the Competition Commission South Africa.

International speakers at the conference included Bill Kolasky, Deputy Assistant Attorney General, US Department of Justice; F Enrique Gonzalez Diaz, Merger Task Force, EU Commission; Jacques Buhart, Coudert Frères and IBA Section on Business Law; Michael J Reynolds, Allen and Overy and IBA Section on Business Law; Dr Fernando Sanchez Ugarte, President of the Federal Competition Commission of Mexico; Olivier Guersent, European Commission; Hassan Qaqaya, UNCTAD; and Pradeep Mehta, Secretary General Consumer Unity and Trust Society (CUTS).

Local speakers included David Lewis, Chairman of the Competition Tribunal South Africa; Anthony Norton, Webber Wentzel Bowens; Michael Katz, Edward Nathan and Friedland; and David Unterhalter.

The conference brought to the southern tip of Africa a host of expertise, experience, and opinions on lessons learnt in competition policy and law over varying time periods and from varying backgrounds.

The theme of the conference – the global nature of competition policy and law – was carried through not only the speakers and the topics, but also in that such an important event was successfully hosted in South Africa.

Code of Ethics

for employees of the Competition Commission

Competition Commission staff realise the importance of ethical behaviour and developed the following Code of Ethics:

I commit to:

- Execute my duties efficiently and without fear or favour.
- Treat all people with dignity and respect, as I want to be treated.
- Uphold the principles of equality, fairness and basic human rights.
- Not take improper advantage of my position.
- In all my actions, uphold the values and the spirit of the Competition Act.

Where to get hold of us

Visit the Competition Commission online at **www.compcom.co.za** for more information about the Commission and the Act, as well as rules and amendments to the Act. You may also forward enquiries, comments and letters to:

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Towards a free and fair economy for all