Towards a free and fair economy for all

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GSK and BI issue anti-retroviral licences

In a first, for South Africa and the world, GlaxoSmithKline (GSK) and Boehringer Ingelheim (BI) concluded separate agreements with the South African Competition Commission whereby the pharmaceutical firms agreed to issue four and three patented licences of anti-retroviral drugs to generic manufacturers respectively.

The Commission initiated complaints against GSK and BI in 2002 after identical complaints were lodged by a number of complainants, amongst them Ms Hazel Tau and the Treatment Action Campaign (TAC).

After conducting the investigation, the Commission concluded that GSK and BI had both abused their dominance and contravened sections 8(a) (excessive pricing), 8(b) (refusing a competitor access to an essential facility) and 8(c) (an exclusionary act) of the Act. This was denied by both GSK and BI. The reasons for the Commission's findings were as follows:

(a) Despite the fact that the competitive provision of the drugs was feasible, GSK's and BI's patented products were being sold in South Africa at prices which were unaffordable to almost all South

GSK and BI issue anti-retroviral licences continued...

Africans living with HIV and which were between five and fifteen times higher than that of generic equivalents. (s8(a) - excessive pricing)

(b) Despite it being economically feasible, GSK and BI had refused competitors access to their patents that were non-duplicable resources, which were necessary to enable the competitors to provide the drugs. (s8(b) - refusing a competitor access to an essential facility)

(c) GSK and BI had impeded generic suppliers from entering the South African markets for anti-retroviral drugs by refusing to grant licences to generic manufacturers at reasonable royalty rates, when there were no legitimate business reasons for such refusals and where the anti-competitive effects of the refusals significantly outweighed any technological, efficiency or other pro-competitive gains from the refusals. (s8(c) - an exclusionary act)

Subsequent to the Commission's finalisation of its investigations, the said companies, which still denied the alleged contraventions, requested that negotiations be entered into in order to resolve the matters without their referral to the Tribunal.

The negotiations culminated in separate agreements being entered into between the Commission on the one hand and GSK and BI on the other, in terms of which the Commission agreed not to refer the matters to the Tribunal on condition that GSK(four) and BI(three) issued a total of at least seven licences for their patented anti-retroviral drugs to generic manufacturers which would permit the manufacture in and importation into South Africa of the anti-retrovirals. The agreements further allowed for the export of any anti-retrovirals manufactured in South Africa to all sub-Saharan African countries. The Commission is of the opinion that in the long run the agreements will result in a drastic reduction in the prices of the anti-retroviral drugs concerned both in South Africa and in other sub-Saharan African countries.

Do these settlements threaten patent laws?

Concerns were raised in the media that these settlement agreements would threaten the existence of patents. As such, companies might no longer wish to invest in research and development of products that would benefit South Africa. It is important to note that although patent holders are granted a legal monopoly, they may not abuse their patent rights. This requirement is not peculiar to the Competition Act 89 of 1998, as amended. It is also present in the Patents Act No. 57 of 1978, as amended.

Abuse of patent rights can take various forms. One form of abuse, found in both the Patents Act and the Competition Act, is that of charging an excessive price for the patented products. In several international jurisdictions, another form of abuse is recognised, namely, that of refusing to grant competitors access to an essential facility. Patent holders are not exempt from these provisions and these are the two provisions the Commission pursued in its investigation. No law gives patent holders the right to abuse their patents. The Commission's finding, therefore, does not threaten the existence of patents any more than existing law always has.

Pharmaceutical firms face similar laws throughout the world, yet the number of times in which the abovementioned provision have been applied in the context of patent holders have been few and far between. This indicates an understanding of the purpose of conferring patent rights. However, when it appears those rights are being abused, it would be detrimental to consumers if authorities allowed such abuse to continue merely because a firm held a patent.

A second concern is that the way in which the Commission defined the relevant product market, in the HIV/AIDS cases, poses a threat to patent holders because it now appears that the mere holding of a patent confers monopoly status (100% market share) on the patent holder, in respect of the product which is the subject of the patent. This concern is unsubstantiated. A product market definition depends not on whether a product is the subject of a patent but on the substitutability of the relevant product with other, comparable products. The market definition in this case was no exception. The Commission formed the view that each active ingredient formed a market on its own based on the degree of substitutability between the various anti-retroviral active ingredients, not on the fact that each active ingredient was the subject of a patent.

One suggestion in the media has been that since the Commission's market definition is likely to cause confusion amongst patent holders, the Commission should clarify its position and adopt a consistent approach to future market definitions involving patents. Given the divergent nature of complaints, markets and market participants, the Commission cannot commit to a consistent approach in defining markets that involve patents. The Commission can only commit to consistently applying competition law principles in all its cases and giving effect to the results. Competition law principles dictate that product substitutability determines what a relevant product market might be. These were the principles applied by the Commission.

Lastly, the concern raised in the media that the Commission's finding in the above cases was largely based on sentiment and not on sound legal and economic principles, is incorrect. Hopefully the discussion above highlights the fact that the Commission's finding was rooted in competition law. What the finding also showed, however, is that competition law exists not only for the benefit of large enterprises, as is commonly thought, but is ultimately there for the benefit of the ordinary citizen as well.

Corporate Leniency Policy

Whistle blowing an option

The Commission has, in line with other international jurisdictions, developed a Corporate Leniency Policy (CLP) to help detect and prevent cartel activities in South Africa, which are detrimental to the economy and to consumers.

The policy will provide incentive for firms participating in a cartel to come forward and disclose information on cartel conduct in return for immunity from prosecution. The CLP will assist the Commission's investigative arm to uncover and break up cartels operating in or affecting the Republic of South Africa.

The Commission defines a cartel as an association by agreement among a group of companies designed to prevent competition.

Cartels are a particularly damaging form of anti-competitive agreement. Their purpose is to increase prices and as a result they cause harm to the consumers of goods or services concerned. They also have a damaging effect on the wider economy as they remove the incentive for efficiency. Practices like price fixing, collusive tendering (bid-rigging) and market division or sharing are generally regarded as the worst forms of cartel activity. Most jurisdictions make these practices per se prohibitions. In other words no justification is allowed for them.

Because cartel activity is highly suspect, it is difficult to detect or prosecute without the assistance of a member who is part of it. In order to induce the member(s) to "blow the whistle" on its associate(s), leniency or immunity programmes are used by most competition authorities internationally.

The CLP outlines a process through which the Commission will have full discretion to grant a self-confessing cartel member, who is first to approach the Commission and subject to specific conditions, immunity or indemnity for its participation in cartel activity. Only a firm that is 'first to the door' to confess and provide information to the Commission in respect of cartel activity would qualify for immunity under the CLP. If other members of the cartel wish to come clean on their involvement in a cartel to which the applicant has already confessed, the Commission may explore other processes outside the CLP, which may result in the reduction of a fine, a settlement agreement or a consent order.

In the event that the matter is referred for adjudication in the Tribunal, the Commission may consider asking the Tribunal for favourable treatment of the applicants who were not first to come forward.

Granting of immunity under the CLP does not imply that the applicant is less of a cartelist than the other cartel members. Without the applicant's information, the Commission could not uproot the harmful conduct that it would otherwise have been unable to detect.

The Commission had adopted the policy in part because not all firms engaging in anti-competitive conduct are aware that such conduct is illegal. In some sectors some conduct may be so prevalent that market players assume it is legal. Even those firms that become aware of the illegal nature of their conduct may fear disclosing the conduct for fear of severe consequences flowing from the Act.

In the South African context, the requirements of public interest and the interests of justice support the need for leniency programmes.

This Policy became effective on 6 Feb 2004, Government Gazette no. 25963/195 and may be amended by the Commission as the need arises. The full text of the Corporate Leniency Policy is available on the Commission's website, www.compcom.co.za and in booklet form.

Firms seeking to make an application may forward them for the attention of the **Corporate Leniency Officer:** Exemptions and Enforcement Division at:

Facsimile number: +27 12 482 9003
Dedicated Line: +27 12 482 9118
E-mail: dianet@compcom.co.za
or
Hand deliver the application to:
cnr Glenwood Road and Oberon Street
Block B
Glenfield Office Park
Faerie Glen
Pretoria.

Import parity pricing and currency volatility:

Implications for competition policy

The Commission recently completed a report for the Department of Trade and Industry (the dti) on the practice of pricing at import parity. Import parity pricing (IPP) is when a firm sells goods locally at the price that customers would pay if they were to import the same goods from another country. Therefore IPP involves setting one's price at the world price, multiplied by the relevant exchange rate, and adding tariffs and transport costs that would be faced by the customer if the product were imported.

The Commission found that IPP might contravene several sections of the Competition Act. These sections relate to colluding to fix a price; the charging of an excessive price; and engaging in prohibited price discrimination. These three possibilities are briefly explained below.

First, if two domestic firms collude to set their prices at import parity, then they are guilty of contravening section 4(1)(b)(i) of the Competition Act, which prohibits the fixing of prices between competitors. However, competitors are prohibited from fixing their prices at any level, so it is not really important that a price is set at import parity. Therefore, there is not necessarily a relation between price fixing and IPP, although setting prices at that level might be a convenient way of shutting out imports and avoiding price competition domestically. In any event, if there were evidence that competitors have fixed their prices at import parity, then they would be prosecuted, as they would have contravened the Act.

Secondly, it is prohibited for a dominant firm within a particular relevant market to charge an excessive price. It might be that for a dominant firm, the charging of a price at import parity amounts to excessive pricing. For example, if transport costs add 100% to the price of importing a certain product, then a domestic firm might charge the world price converted into rands and inflated by 100% to arrive at an import parity price. The Commission would observe that the domestic price is 100% more than the global price and thus might find that the domestic firm is charging an excessive price. But the domestic price must be evaluated for excessiveness according to criteria such as international price comparisons, price/cost measures, and profitability measures. The fact that the domestic price has been set at import parity does not affect the analysis.

Finally, if a firm prices its product at import parity to its domestic customers, but receives only export parity proceeds from its sales to foreign customers, is that firm guilty of prohibited price discrimination (section 9 of the Act)? (Note that the export parity price is the world price multiplied by the exchange rate, minus the transport cost to the foreign customer, and minus the tariff in that market). Like excessive pricing, prohibited price discrimination only applies to a dominant firm. The price discrimination considered here is between SA customers and foreign customers. Therefore the relevant market within which that discrimination takes place must embrace both SA and the foreign market. If we define the geographic market as global, then a firm accused of prohibited price discrimination must be dominant globally. Seeing that SA is a relatively small economy, it is unlikely (but not impossible) that a domestic firm will be globally dominant in the market for its product. Therefore, in most cases, a domestic firm would be entitled to price discriminate as between domestic and foreign customers, without causing any harm to competition. If, however, there are transport cost and tariff barriers that seal off the domestic market from international competition, then the relevant geographic market may be regarded as being confined to SA. In this case, price discrimination as between competing domestic customers might be prohibited in terms of section 9 of the Act. Again, however, the intervening factor of setting one of these prices at import parity does not affect the analysis of whether there has been prohibited price discrimination or not.

Therefore the report found that although IPP might be the basis for setting prices that are found to be anti-competitive, nevertheless there is no predictable connection between

IPP and any of the contraventions mentioned above: collusion to fix a price, excessive pricing, or prohibited price discrimination.

One reason why there can be no predictable relation between IPP and anti-competitive pricing practices, is the variable influence of the exchange rate, particularly as it relates to allegations of excessive pricing and prohibited price discrimination. As explained above, IPP (and its counterpart, export parity pricing) are derived by means of converting into rands, a global price for a product expressed in foreign currency units. This is achieved by multiplying the foreign price by the relevant exchange rate (expressed as rand per foreign currency unit).

An import parity price is a moving target, and as such cannot be outlawed by any sensible policy measure. This is particularly so in the environment of extremely volatile exchange rate fluctuation that has been a feature of the rand over the last few years. Prices should be evaluated for their anti-competitive effects according to established, predictable criteria. But the view of the Commission is that import parity pricing is as volatile as the underlying exchange rate movements, which means that it is not sensible to formulate a rigid rule about the practice of setting prices according to import parity.

Government legislation and competition policy:

Is Black Economic Empowerment becoming the primary driver of Merger & Acquisition transactions in South Africa?

Introduction

Black Economic Empowerment (BEE) is considered one of the main pillars of the South African government's economic policy. In SA Competition policy, BEE is considered one of the most important public interest issues in deciding whether a merger should or should not be approved.

There are a variety of reasons why companies merge:

1) A failing firm may be motivated to sell to avert liquidation.
2) The buyer or acquiring firm is motivated by the perception that by merging, economic efficiencies will be realised. Because of their increased size and greater market share post-merger, the new entity could invest in newer technology and more specialised equipment, skilled operators, high-speed automation, and high-tech equipment. These aspects create greater efficiency among the firms so the merger appears desirable to both the firm and to society (greater production efficiency).
3) The merged entity may gain economies of scale and scope (ability to reduce average costs).
4) In the case of conglomerate mergers, risk spreading through diversification may be a motivating factor.
5) Some firms merge with others in the same industry and in so doing are able to create or enhance monopoly power. Mergers to increase market power typically cause the most concern to society and are most closely scrutinised by competition authorities worldwide. The motive behind such mergers results in, or has the ability to create, higher market concentration, the foreclosure of competitors, a strengthening of the barriers to entry, raised prices, and in general, reduced economic welfare.

Black economic empowerment as a reason for merger

Other mergers and acquisitions (M&A) are motivated by a desire to promote black economic empowerment. In terms of new legislation[1], government requires firms having dealings with it to have a black economic empowerment component. In merger activity or in the determination of whether a transaction should be approved or not, the Commission also considers the public benefits that might be brought about by the merger. These public interest issues include amongst others, BEE. This brief attempts to detect if there is a link between government policy (BEE charters) and M&A activity.

The equity market and BEE in 2003

The equity market seems to have reacted positively, recording an increase in black equity deals. South Africa's black economic empowerment drive is said to have hit a high in 2003, with more than R30 billion worth of black equity deals having been concluded, compared to the peak of R21 billion in 1998.[2] This peak coincided with the introduction of empowerment legislation[3] and sector specific charters, which were introduced during the year. At present, there are two sector specific empowerment charters in mining and financial services. A charter in the information technology sector is in the offing. From the 2003 equity figures it can be seen that companies took a proactive stance to forge ahead with empowerment, especially in the mining and financial service sectors, where business with government is thought to be crucial.[4] BEE has been recognised by business leaders and is considered an integral part of doing business in South Africa.

Some corporate finance executives envisage that BEE could be responsible for generating deals valued at anything between R50 billion and R80 billion over the short term. As such, it is considered an area of activity that is bound to draw considerable attention and focus.[5] The question is: is government policy through the introduction of BEE charters having a positive effect on mergers?

Black economic empowerment in merger activity: The period 2000 - 2003.

From the diagram on the following page it is noticeable that the manufacturing sector

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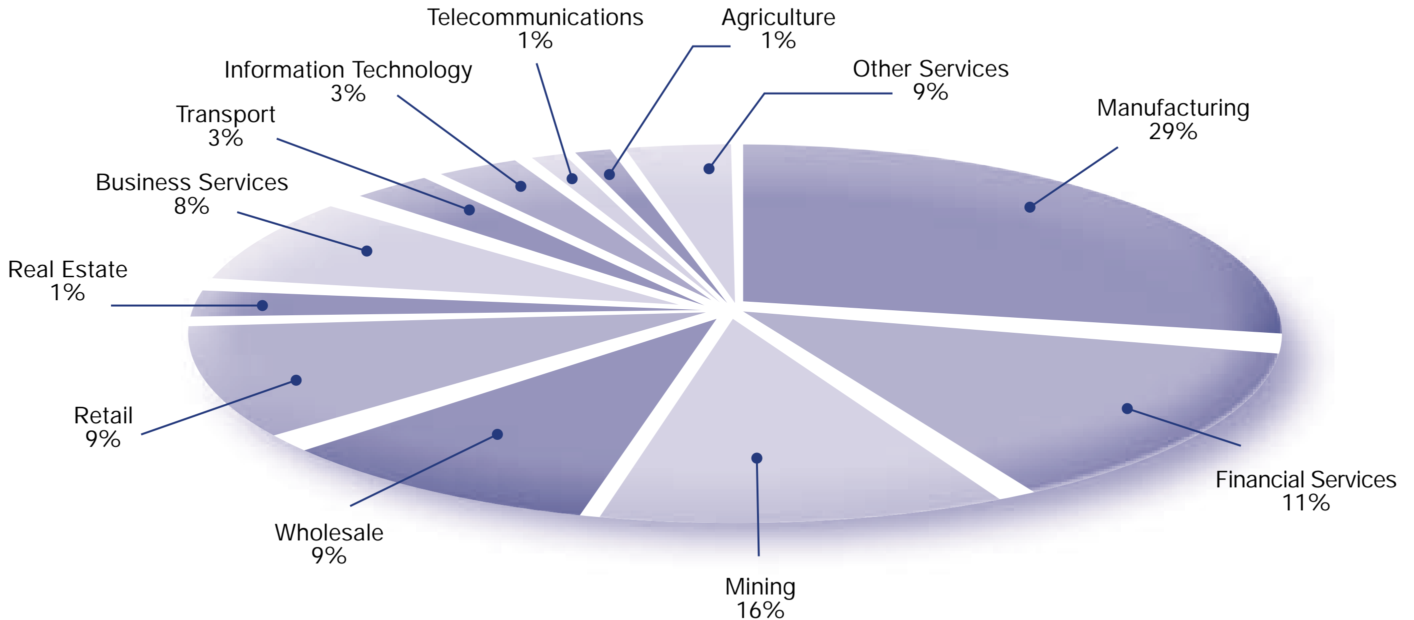
1 The Broad-Based Black Economic Empowerment Act
2 Companies take proactive stance ahead of new empowerment legislation, by Patrick Wadula, Senior Business Correspondent, Business Day, December 20, 2003
3 The DTI's Broad-Based Black Economic Empowerment strategy document
4 Ibid.
5 Deal Makers, Vol 4: No 3.

Government legislation and competition policy continued…

led in terms of mergers, with a black economic empowerment component, followed by the financial services and mining sectors. The fact that financial services and mining are amongst the top three sectors might be an indication that companies are gearing themselves up for BEE charters introduced by government. During the year 2003, the Commission saw a total of 24 deals in which Historically Disadvantaged Individuals (HDIs) were participating. Of the 24 transactions, the financial services and mining sectors accounted for 26% and 13% respectively. In 2002, 21 mergers with a BEE component were received. The financial service and mining sectors accounted for 5% and 29% respectively. Comparing these two periods, it can be seen that the mining sector peaked in 2002, considering that the Mining charter was introduced in 2002 and slowed down in 2003 (with 13%). The opposite can be said of the financial service sector, which seems to have peaked last year[6] (29%) as compared to 2002. The diagram below shows the overall performance of sectors for the period 2000-2003. The top three sectors are manufacturing with 29%, mining 16% and financial service sector with 11%.

Based on statistics analysed, it can be concluded that government legislation does have an effect on competition policy via M&A activities. Mergers with BEE components seem to have increased when government legislation was introduced, signalling some positive response from the South African business sector.

Black Economic Empowerment in Mergers & Auquisitions: 2000 - 2003



6 The Financial service BEE charter was introduced in 2003.

Case Reviews

The settlement agreements reached with IHD

The Commission initiated complaints against International Healthcare Distributors (Pty) Ltd (IHD) and a number of other companies which manufacture pharmaceutical drugs, after identical complaints were lodged by a number of complainants.

Having conducted its investigation, the Commission concluded that IHD and the other respondents had contravened one or more of sections 4(1)(a), 4(1)(b)(i), 5(1), 8 and 9(1) of the Act in that the respondents had entered into exclusive distribution agreements with IHD, a joint venture company in which they and certain pharmaceutical manufacturers were equal shareholders, to distribute their pharmaceutical products and medicines. The Commission thereafter referred the complaint to the Competition Tribunal.

Subsequent to the referral of the matter, the Commission and the respondents entered into negotiations in an effort to resolve the matter without the matter being heard by the Tribunal.

These negotiations culminated in an agreement being entered into between the Commission on the one hand and the respondents on the other, in terms of which the Commission agreed to withdraw the matter on condition that each of the respondents disposed of their interests in and terminated their distribution agreements with IHD and further each made a settlement payment of R2 000 000 (two million rand). The Commission was satisfied that the agreement addressed the competition concerns which it had identified, inter alia, by disbanding the joint venture which could be used to facilitate collusion among the pharmaceutical manufacturers.

However, after the agreement was implemented, the complainants launched an application in the Competition Appeal Court, to set aside the agreement on the basis that the Commission had acted ultra vires in concluding the agreement with the respondents and in agreeing to withdraw the matter before the Tribunal. The basis for the complainants' application is that the Act only provides for the conclusion between the Commission and a respondent of a consent order, which requires an admission of liability and confirmation by the Tribunal; and not a settlement agreement of the type entered into in this case, where there is no admission of liability and which is also not subject to confirmation by the Tribunal. This application is still pending.

Tiso-NAIL transaction gets the go-ahead

The Commission has referred the large merger in which the Tiso Consortium proposes to acquire all of the issued share capital currently held by the minority shareholders in New Africa Investments Limited (NAIL) to the Competition Tribunal for adjudication.

The Tiso Consortium comprises Multidirect Investments 180 (Pty) Ltd (a wholly-owned subsidiary of Tiso Capital Partners), Capricorn Capital Partners Holding Company (Pty) Ltd, Investec Bank Limited, Safika Holdings (Pty)

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Ltd, and Mineworkers Investment Company (Pty) Ltd. NAIL is an investment holding company with interests in printing, publishing, radio broadcasting, television production as well as "other assets".

The Tiso Consortium proposes to acquire the assets in NAIL and sell them on to interested buyers. The Commission has recommended that the merger be approved with several conditions in the event that the proposed on-selling of certain assets might be delayed or cancelled.

In reviewing the proposed merger, the Commission evaluated all the markets where the Consortium and NAIL are active in and we identified the following markets where there could be a potential product overlap, i.e. magazine publishing, radio broadcasting services in Cape Town and Johannesburg, and outdoor advertising.

The Commission found that the transaction will not substantially prevent or lessen competition in the markets for magazine publishing in South Africa or radio broadcasting in Cape Town. However, the Commission is concerned that the proposed transaction could lead to more highly-concentrated markets for both radio broadcasting in Johannesburg and outdoor advertising in South Africa.

The Commission accepts that the primary acquiring firm intends to on-sell the majority of NAIL's assets, particularly radio stations in Gauteng and outdoor advertising, which will address competition concerns, but is mindful of the fact that the sale of these assets might be delayed or cancelled for whatever reason and therefore finds it necessary to approve the proposed transaction with conditions. The recommended conditions include:

1. The primary acquiring firm will dispose of NAIL's interest in Jacaranda within a period from the date of conditional approval of this transaction by the Competition Tribunal.

2. The primary acquiring firm will dispose of NAIL's interest in Kaya FM within a period from the date of conditional approval of this transaction by the Competition Tribunal.

3. The primary acquiring firm will dispose of NAIL's interest in NAIL Outdoor within a period from the date of conditional approval of this transaction by the Competition Tribunal.

4. The primary acquiring firm shall be obliged to notify the Commission of the sale of any asset as described in numbers 1 to 3 above, irrespective of whether such transaction(s) falls below the threshold for merger notification.

5. The primary acquiring firm is precluded from appointing Primedia or any other firm that is not a member of the Tiso Consortium to dispose of any of NAIL's assets on behalf of the primary acquiring firm.

6. No veto right pertaining to the sale of any of NAIL's assets will be granted to Primedia or any other firm that is not a member of the Tiso Consortium.

7. No firm, other than the primary acquiring firm, shall be authorised to exercise any form of control, including managerial control, over any NAIL asset, whether on a temporary or permanent basis, before the Commission or the Competition Tribunal, as the case may be, has approved the particular transaction that transfers control over such affected asset(s). For purposes of this, only transactions which are notifiable transactions are relevant.

Another issue this merger transaction raised was whether change of economic control without voting control constituted a notifiable transaction. This question encouraged the competing bidders to lodge an urgent interdict before the Competition Tribunal.

The Tiso Consortium notified the Commission of the proposed transaction under protest and with full reservation of their rights. The parties submitted that, although the primary acquiring firm has obtained more than 50% of the issued share capital in NAIL, control of NAIL still vests with Phaphama, since Phaphama still holds the majority of high voting ordinary shares in NAIL. The primary acquiring firm, however, has a call option on the ordinary shares held by Phaphama in NAIL, and therefore requested the Commission to evaluate and approve the granting of the call option.

The Commission earlier ruled that the transaction is a notifiable merger in terms of section 12(1), 12(2)(a) and/or (g) of the Competition Act of 1998, read together with the judgment delivered by the Competition Tribunal in Ethos Private Equity Fund IV and Tsebo Outsourcing Group, which examined whether change of ownership of more than 50% of share capital constituted notification.

This merger was approved with conditions by the Tribunal. One of the conditions is that the Commission's concerns regarding the overlap of radio and outdoor advertising markets are addressed.

Merger in the vacuum cleaner industry

In October 2003 the Commission approved the acquisition of Conti South Africa (Pty) Ltd (Conti SA) by Nu-World Holdings Ltd (Nu-World).

Both companies are involved in the manufacture of vacuum cleaners. However, based on a narrow market definition of "dry only" and "wet & dry" vacuum cleaners there was no product overlap between the merging parties. Conti was primarily in the "wet & dry" market and Nu-World in the "dry only" market. Based on a broad market definition of "vacuum cleaners", (which is a concentrated market) there was a product overlap. Nu-World, being the acquiring company, was, however, a very small player and thus the merged entity's market share would be slightly higher than Conti's pre-merger market share. The new entity would continue to face competition from two major players, being Electrolux and Hoover. There are also many smaller players in the market such as AEG and LG who are importing as well as Singer, a Hi-FI Corporation house brand, etc.

The investigation concluded that the transaction was unlikely to give rise to a substantial lessening or prevention of competition.

The possibility of implementation prior to approval was a concern. However, upon further investigation, the Commission decided that the merger had not been implemented prior to the Commission's approval. There were no significant public interest concerns. The transaction was unconditionally approved.

Commission investigates steel giant's prices

During December 2003 the Commission finalised three investigations involving Iscor, the largest producer of steel in Sub-Saharan Africa.

The investigations, which received much media attention, in essence centred around Iscor's pricing policies and more specifically its pricing of flat steel products sold locally.

The complainants, two gold miners being Harmony Gold Mining Company and Durban Roodepoort Deep, The Conveyor Manufacturers Association of South Africa and Volkswagen of South Africa alleged that Iscor was contravening Section 8(a) of the Competition Act No. 89 of 1998, as amended, (the Act).

It was alleged that Iscor abused its dominance in the market for the manufacture of flat steel products in South Africa, by charging excessive prices for those products and by increasing its prices unrealistically.

The complaints stemmed from Iscor's practice of applying a policy of Reference Pricing or International Parity Pricing (IPP) in calculating its prices for flat steel products sold locally. This policy in practice means that the price for the basic product of hot rolled coil (HRC)[1] is benchmarked against international prices for the same product, and/or against substitute products such as plastic and cement. The lowest available FOB price per ton[2] is then used as a basis price. Onto the basis price is then added shipping costs, commission, stevedoring and harbour costs and import tariffs.

An example of IPP calculation for the basis price of HRC will therefore be as follows:[3]

HRC - FOB Black Sea	- $300 /t
Shipping cost	- $ 35 /t
Commission	- $ 5 /t
Stevedoring & harbour costs	- $ 5 /t
Import tariff	- $ 15 /t
	$360 /t

The basis price Iscor then charges for a ton of basis product HRC will be $360, which in theory will be the same price a steel consumer would pay to import the product from the Black Sea.

During the investigation information was requested from more than 25 companies involved in the South African steel industry, representing the different levels in the supply chain, being steel producers, steel merchants and customers. Numerous interviews were also conducted to clarify issues the investigation team identified in some of the information that was submitted.

In assessing the excessive pricing complaints Iscor's prices were assessed in relation to products sold by its competitors such as Highveld Steel and Vanadium Corporation Limited, imported products and substitute products. Iscor's prices were also compared with prices charged to final consumers in other national markets around the world. The investigation found that Iscor's prices were comparable to prices of competing products available locally, as well as to prices charged in other national domestic markets.

Accordingly the Commission found no evidence of an abuse of dominance on the part of Iscor in that it was charging excessive prices.

Although the Commission's decision received criticism from some of the complainants, it followed an extensive investigation, took into account economic and competition law principles and was based upon the facts and evidence at hand.

A positive result for the Commission is that Iscor, as a result of the investigations, expressed a willingness to discuss issues surrounding its prices and in media releases extended an invitation to all interested parties to engage in discussion.

1 2mm X 1225mm commercial quality material in 1000 ton lots
2 FOB, or Free on Board means the price as at the port before being loaded for shipment
3 Example used at meeting with delegates from Iscor on 27 November 2003.

Case reviews continued…

Sasol Exel merger approved

The Commission referred the large merger between Sasol Oil (Pty) Ltd, a wholly owned subsidiary of Sasol Limited and Exel Petroleum (Pty) Ltd a wholly owned subsidiary of Naledi Petroleum Holdings (Pty) Ltd to the Tribunal and recommended that the transaction be unconditionally approved.

In its investigation, the Commission found that the parties overlap in the market for petrol, diesel and fuel oils and that they operated in different functional levels. There were overlaps in the commercial petrol, diesel and fuel oil markets and the retail petrol and diesel markets. In its analysis, the Commission looked at market shares at a narrow geographic market (provincial data) and at a wider (national) market level. The Commission found that the parties' combined market shares were insignificant at the national market level to raise any serious competition concerns. While in the narrower geographic market, Exel had a greater market presence in certain areas, it was found that the merger was unlikely to result in any significant changes in the concentration levels in those areas. Sasol Oil's presence in the retail market at the time of the merger was limited to its blue pumps and the few service stations as specified by the Main Supply Agreements (MSA) that were terminated at the end of December 2003.

Hence, the Commission concluded that the accretion in market shares was minimal and that the merged entity would not have a significant presence in any of the markets. Sasol's presence in the retail market would only increase when the MSA fell away at the end of December 2003, thereby allowing Sasol to enter the retail market from January 1, 2004.

In its vertical assessment, the Commission considered the effect on competition of Sasol Oil raising its rivals' costs. The Commission found that in the short run the effect in the petrol market was limited. This was due to the fact that Sasol in the short run is highly dependent on other oil companies for the uptake of its products. It could not reasonably hold back its supply and sell this through its own limited retail outlets.

In the long run, however, Sasol Oil would be more entrenched in the retail market (given that it would enter the retail market and grow its presence in this market) and may possibly be in a position to cut back supply completely. If this were the case it would be in a position to squeeze the profit margins of its competitors forcing them to either cut back on their retail outlets or to exit the market.

The Commission proposed that while these effects seemed possible and likely, they were independent and not specific to the merger in question. Hence, the identified competition concerns could occur whether the merger was approved or not.

The Commission also found that the merger would have many public interest benefits. In particular, the transaction would enable Exel, consisting of BEE shareholders to expand their participation in the liquid fuels industry. The provision of 25% of Sasol Oil to Black economic empowerment shareholders will increase the ability of historically disadvantaged South Africans (HDSAs) to participate in this market thereby fulfilling the requirements of the Charter for the SA Petroleum and Liquid Fuels Industry on Empowering HDSAs (The Charter) which attempts to achieve the equity objectives set out in the 1998 White Paper on Energy Policy for SA (White Paper) and which stipulates that 25 percent of ownership and control of all facets of the liquid fuels industry must, over a ten year period, be in the hands of HDSAs.

Should international competition policy regimes converge?

During the last decade, a vast number of countries have enacted some kind of competition law; it is widely thought of as one of the necessities of a working capitalist economy. Subsequently, there has been a great deal of energy directed towards the question of competition law convergence. The reason is that international business increasingly engage in international transactions, while competition law is enacted at national level. The incongruity between the scope of regulated and regulatory activity has created unnecessary friction and confusion in the past.

While there is little disagreement that convergence should minimize counter-productive conflict, there is broad disagreement on what kind of transformation is necessary. Some argue that competition law must operate on the same dimensions as the regulated markets, i.e., that a supra-national body (like the WTO) should be policing such activity. Others are content with national enforcers, but believe that some degree of harmonization of the substantive laws of different jurisdictions is necessary. Others focus on the transaction and political costs associated with multiple assessments, and a fourth view expresses some "correct" competition law, not to be deviated from.

Substantive uniformity

There exists many arguments for harmonizing substantive competition law. Some believe that nothing less than a single international code will suffice. Others would permit some variation between national systems, but argue for a set of minimum standards that every system must satisfy, e.g. a law against cartels. A third group proposes the creation of a supra-national body to harmonize the results.

However, is harmonization really necessary? There has been little evidence presented that having different national competition laws creates an opportunity for arbitrage, thus permitting anti-competitive behaviour that would otherwise be prevented.

Indeed, there is good reason to believe that enforcement is most effectively dealt with at the domestic level. For example, the criminal enforcement of anti-cartel legislation. Many European regimes impose criminal sanctions against both individuals and corporations for price-fixing. They would not likely forsake enforcement of their own criminal laws in favour of a foreign antitrust regime. Moreover, local antitrust authorities, with the evidence and the experience necessary to prosecute such claims, would have to play an integral role in anti-cartel enforcement. Violations of competition laws inherently require contact between the violator and the home jurisdiction, causing the latter to be a prominent geographic market.

There is good reason to believe that substantive harmonization is very unlikely to occur; the repeated failures of past harmonization attempts lending its weight. Independent sovereigns are naturally disinclined to cede authority to another. Different countries are also at different stages of political, economic and/or institutional development, preferring competition laws that would best fit their circumstances.

None of this is to say that convergence is impossible. Over time, competition law regimes may resemble one another as countries strive to achieve best practices. But it is unlikely that convergence will be complete; some aspects would still be determined by the needs of individual nations.

Conclusion

Competition law does not have a one-size-fits-all solution. Rather than viewing temporal and geographic variations as complications for competition law, we must view them as opportunities for productive experimentation. Regulators should co-operate and communicate about what they are doing and how it is working. Not only would this be more feasible, it would also more likely produce better results than imposed uniformity.

Source:
Meiklejohn, D.S. (2003)
"You Can't Legislate Perfection",
30th Fordham Conference, New York.

The South African Competition Economics Forum

Calling upon all economists

The South African Competition Economics Forum (Sacef), launched on the 4th of December 2002 at the Competition Commission (CC) offices, is a grouping of economists and policy makers from diverse backgrounds, ranging from academia, to government, to regulatory authorities, to labour and to the private sector. It provides a platform or discussing, debating and deliberating on competition and regulatory policy issues, in particular and economic matters in general as they affect our economy. The Forum is premised along the lines of the Competition Law Committee (CLC), which meets on competition law issues but is external to the Commission. SACEF has a direct link with the Commission. This article gives an overview of the activities of the Forum and provides a summary of the debates/discussions so far.

Activities

The following are some of the activities of the forum:

1 **Information exchange**
- Economic opinions on finalised cases can be shared with interested members
- Attendees are updated on activities of the Commission
- Discussions are held on the economic approach used in specific cases/policies
- The Forum provides an interface between regulators and competition authorities
- The Forum gives an opportunity to address inadequacies in the Competition Act, investigate and recommend amendments to the Act from an economic viewpoint.

2 **Presentation of research papers by members / guests**
Members are encouraged to present research papers and/or solicit opinion on work-in-progress from the forum.

3 **Discussion on decided cases and policy papers**
Members discuss decided cases. Various economic policy positions taken by the Commission, government departments and regulatory bodies are also discussed.

The following topics/cases were presented /discussed at the forum during the course of the previous year:

Import parity pricing

The problem of import parity pricing (IPP) in the context of excessive pricing, especially in the steel industry was discussed. This was in light of the study being undertaken at that time by the

Commission at the behest of the dti into the competition impact of the practice. Among the issues discussed was the problem of geographic market definition. The way the geographic market is defined has implications on player dominance and therefore on abuse of such dominance including excessive pricing. It was also pointed out that international benchmarking is made difficult by issues such as the choice of comparator countries, price comparisons and the use of an appropriate exchange rate converter. As such, the question of whether IPP constitutes excessive pricing remains debatable; although the Commission's view is that its elusive nature does not warrant outlawing the practice.

Mondi/Kohler merger

The vertical merger between Mondi Ltd and Kohler Cores and Tubes was prohibited by the Tribunal[1] on what appears to be Post-Chicago School arguments of collective dominance or co-ordinated effects. The Commission had recommended a prohibition based on the unilateral effects argument. The Tribunal had argued that Mondi and Sappi's behaviour post-merger could lead to market foreclosure and a substantial lessening of competition in the relevant markets. Sappi is the other producer of paper products in this duopolistic market. The Tribunal identified two ways through which this vertical transaction could pose a threat to competition. Firstly, there was the possibility that the merged entity may raise the competitors' cost of doing business in either or both the upstream and downstream markets, through input or customer foreclosure. Secondly, there was also the likelihood that the merger may facilitate collusion between the post-merger participants in either or both of the relevant markets through easing the flow of information between competing firms. The discussion centred on the many theories of vertical integration and its consequences for competition and whether any of these were overlooked in this case.

Restructuring of the electricity supply industry

This presentation gave an overview of government's thinking on restructuring the electricity industry and the challenges thereof. Electricity in South Africa fetches one of the lowest prices in the world. Eskom seems to be performing well. The question then, is why is the industry being tempered with? This was debated at length with the pros and cons of restructuring the industry coming to the fore. Various models of restructuring were presented. The proposed model of divesting only 30% of the generation assets to the private sector was critiqued as being insufficient to foster effective competition, if that is the aim of the whole exercise. Experience from countries that have restructured their electricity industries provided invaluable policy lessons.

Market definition

An advisor to the CC from the US Federal Trade Commission shared her experience in approaching market definition issues both from a theoretical and practical point of view, as well as from a merger analysis and enforcement perspective. Issues discussed include the SSNIP test (also referred to as the hypothetical monopolist test), critical loss theory, the cellophane fallacy and the practicalities and tips of investigating or gathering information on the relevant product and geographic markets.

Administered prices

This presentation on the assessment of administered prices in South Africa was based on a study undertaken collectively by various consultants on behalf of National Treasury. The objective of the study was to assess the processes involved in setting prices in regulated industries. The research focused on whether administered prices in South Africa are high or low and whether they can be efficient. This was against the backdrop of government concerns about increases in administered prices that were above the rate of inflation, hence threatening the Reserve Bank's monetary policy of inflation targeting. The sectors covered in the study include electricity, telecommunications, transport, water, health and education. The study concluded that there are serious flaws in terms of processes and procedures affecting both the level and structure of prices set in these sectors, casting doubt as to whether they are efficient. The overall weakness in administered pricing in South Africa is a result of a number of factors, including institutional weaknesses, unclear objectives, insufficient monitoring and evaluation and the myth of privatisation/ liberalisation as a cure-all.

Competition policy and economic ideology

This work-in-progress is an attempt at trying to locate the Commission's thinking and ideological inclination, if any, influencing its decisions. The presenter gave an overview of the various schools of thought and the policy implications of adopting one school of thought as opposed to the other when, say, evaluating a vertical merger or analyzing the effects of various restrictive practices. The discussion revolved around certain Commission decisions involving cases and advocacy and whether these were based on certain ideological persuasions or on the practicalities of the case at hand.

The Forum promises more stimulating debates and discussions on various topics again this year. For more information on upcoming SACEF meetings please contact Charmaine Neves at:
Tel: (012) 482 9052
Email: charmainev@compcom.co.za

1 Later on appeal, the Competition Appeal Court upheld the Tribunal's decision.

Trade union participation

Its importance

Trade union participation is important in Commission procedures.

The purpose of this article is to give an overview of the merger analysis process and to provide detailed guidance as to how unions can participate effectively and efficiently in this process.

Methods of notification

The notice may take either one or a combination of the following methods:

- By handing the notice to a responsible employee who is apparently in charge of the main office of the union, or
- If there is a union office within the magisterial district of the firm, by delivering the notice at that office
- If no person, from the above, is willing to accept service, by affixing a certified copy of the notice or document to the main door of that office
- By any other method allowed for, including but not limited to:

- faxing the notice or a certified copy of the document to the union, if the union office has a fax facility,
- sending the notice or a copy of the document by electronic mail, if the union has an address for receiving electronic mail,
- sending the notice or a certified copy of the document by registered post to the union's last known address, or
- sending the notice to a union's head office address contained in the union head office address list.

If, following receipt of the merger notice, a union discovers that certain information (not claimed confidential) has been omitted from the notice, it must immediately communicate this to the Commission. The latter will then ascertain the union's claim and if the claim is proved to be valid, the Commission will then deliver to the filing firms a notice of incomplete filing in Form CC13 (2) within...

- 10 business days of having received the merger notice filed in respect of an intermediate merger,
- 5 business days following a large merger notice,

The Commission will contact the affected union(s) either telephonically or by facsimile to ascertain whether such union(s) did in fact receive the merger notice. The union(s) will further be advised of the importance of participating in the Commission's merger proceedings, for this purpose a copy of the CC5 (1) form[1] will be forwarded to that union.

Filing Form CC5 (1)

Within 5 business days following receipt of the merger notice a union may notify the Commission of its desire to participate in merger proceedings by filing form CC5 (1), which will grant to union(s) the right to make inputs on the transaction as well as to participate in merger hearings before the Competition Tribunal (the Tribunal).

The merger analysis process

The Commission has 20 business days to make a decision on an intermediate merger, with the first 5 business days allocated to the filing of the intention to participate by the union or employee representatives.

In respect of a large merger the Commission has 40 business days to make recommendations to the Tribunal on whether to approve, approve subject to conditions or prohibit such a merger. As in the case of an intermediate merger, the first 5 business days will be allocated to the filing of the union's intention to participate.

During this merger analysis process a union(s)...

- must forward its inputs on the transaction for consideration when making a ruling and for report compilation purpose as well.
- may contact the Commission when requiring further clarity on the transaction and
- may, when experiencing difficulty in arranging meetings with the parties, request the Commission to organise and facilitate such meetings.

As a participant in a merger case, a union(s) will be kept informed of the status of the case and of the decision taken by the Commission.

Post merger considerations

If, following a decision of the Commission, a union is not pleased with the verdict; the latter may request the Tribunal to consider the decision of the Commission. However, the Tribunal will only consider the union's request provided that the union had been a participant in the proceedings of the Commission.

Other methods of participation

A union can participate in merger proceedings by...

- Lodging a complaint with the Commission if parties to the merger did not notify it,
- Notifying the Commission when a condition attached to the decision is not adhered to,
- Notifying the Commission of mergers it thinks were implemented without notifying Competition Authorities.

Labour[2] inputs in merger assessment processes are highly valued. Such inputs give the views of labour on the impact the merger will have on employment conditions in the merging firms, their subsidiaries and the area within which they operate. It is therefore important for unions to familiarize themselves with processes of the Commission.

The Commission on request and at no cost also provides awareness campaigns in the form of presentations, workshops and consultative meetings. Unions can therefore take advantage of these free services. More information on these can be obtained from the Commission's Compliance Division, at the following contact details:

Tel: (012) 482 9066
Fax: (012) 482 9120
E-mail: CCSA@compcom. co.za
Website: www.compcom.co.za

1 Notice of intention to participate form
2 Representatives of the workforce (trade unions and employee representatives)

Profile

Investigating the anti-retroviral complaints

The Commission takes a look behind the scenes and talks to two of its investigators, Nandi Mokoena and Thulani Kunene who worked on the GlaxoSmithKline and Boehringer Ingelheim case.

When the complaint was first received, what did you anticipate the outcome would be?

Nandi: "We had a case dealing with a similar issue prior to the Treatment Action Campaign case. That case ended in a non-referral, therefore at the outset, we felt that it could possibly also end up being non-referred ."
Thulani: "However, as the investigation progressed, and we received more opinions and more information, the case started to look like it would be referred to the Tribunal - which is eventually the decision we made."

Was the investigation challenging, and in which way?

Nandi: "It was challenging in the sense that it dealt with a very emotional issue, which we had to approach in a rational, objective and legalistic way. As one can imagine, there were constantly varying views about the case - even amongst the team members themselves."
Thulani: " It was also challenging in that the case ventured into a virtually untouched field of competition law. Formulating theories and applying existing theories to the facts of this case was therefore difficult to do."

How did you feel while conducting the investigations?

Nandi: "We think we all went through a whole range of emotions, sometimes intimidated by the public attention, at times frustrated by the many contradictory directions the case was moving in."
Thulani: "However, we were ultimately proud that we all worked together (the Commission, the Complainants and the Respondents) and ended up with, what we think the best solution there would have been."

What is the significance of the settlement agreements?

Nandi: "The settlement agreements are very important for the public and private sector. It means the government and private hospitals will have a whole range of generic anti-retrovirals to choose from, which means they will be able to choose those drugs with the lowest prices for the public."
Thulani: " It ultimately means HIV/Aids sufferers will have greater access to the life saving drugs than ever before."

Thulani Kunene and Nandi Mokoena

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 the rules and amendments to the Act. You may also forward enquiries, comments and letters to:

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