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The treasury report
on competition in South African Banking

Competition in South African Banking is a report that was commissioned by the National Treasury and partly funded by the Commission. It was released in 2004 and has been widely referred to in the media. The report was written mostly by consultants, under the direction of the appointed task group members, including one representative of the Commission. The subject matter is wide-ranging and identifies several competition issues. Data has been compiled from a great range of secondary sources for the report, and there are comparisons with data and conclusions from other studies, notably those conducted in the United Kingdom.

The report was released in April 2004 and some data in it relates to 2003 and before. The report starts off by describing the SA banking industry as being dominated by the 'big four' (ABSA, FNB, Nedbank, and Standard Bank) or the 'big five' if Investec is included. The big four accounted for 83% of deposits in June 2003.

It is pointed out that although no single bank is dominant in terms of the Competition Act, in the retail-banking sector taken as a whole nevertheless, there may be dominance within certain sub-sectors of the industry. For example, ABSA is known to have the strongest presence in the home loans market.

The report is based partly on three British reports on banking: the Cruickshank report, and two UK Competition Commission reports, one concerning SMEs and the other relating to a proposed merger between Lloyds TSB and Abbey National.

In these reports, the focus was on sub-markets within the retail-banking sector, as well as on the complexity and transparency of service offerings and charges of banks. Switching costs (for consumers wishing to move their accounts between banks) were also explored. So were the normal measures of competition and concentration within an industry, such as concentration, pricing strategies, entry barriers and profitability.

The focus of the UK Competition Commission enquiries was on whether there was 'effective competition' in the relevant markets and on whether the conduct of the 'High Street banks' warranted a declaration that the industry operated as a so-called 'complex monopoly'. In other words, the Commission found that the big banks behaved as if they were one monopoly firm, rather than several independent banks.

In the UK, the Competition Commission characterised the banks as acting as a complex monopoly in the particular area of SME banking. Accordingly, recommendations were made, inter alia, to make error-free switching between accounts simpler and easier, to limit the bundling of services, to improve the flow of information and transparency, to improve the transparency of bank statements and to clarify the reasons for refusing a loan.

Some data is provided on the costs, revenues and profitability of SA banks in the report. Broadly speaking, the report concluded that SA banks appear to be making large and stable levels of profits, although they appear to be in line with banks in other countries regarding efficiency and interest rate spreads which are alternative indicators of pricing power and mark-ups.

An interest rate spread is the difference between a bank's lending and borrowing rates. A bank will try to borrow money at a low rate of interest and lend those funds at a higher rate, but will naturally only make money if its clients do in fact repay their loans. Therefore a bank must be selective about choosing its clients and it does not always follow that the interest rate spread indicates the degree of a bank's profitability.

Banks may make some of their money by levying bank charges rather than by means of the interest rate spread. Indeed in the report it is stated that SA banks made only half their income from interest in 2002, down from 60% in the mid 1990's. Interest spreads/margins also declined from 4% to 3%.

For specific products, concentration levels in the SA banking sector are high. The total market share of the biggest four players in each sub-market is a traditional measure of economic concentration and is denoted by the term CR4. The report states that CR4 for specific products are: credit cards 95,4% (it is noted that about 30% of credit card credit extension to households is in the form of store cards); mortgages 92,3%, and installment finance 89,5%. Interestingly, the report also shows that each of the big four banks in 2002/03 had a market share in excess of 25% in one different segment (25% was the benchmark used in the UK to reflect market power or a 'scale monopoly'). In 2002/03 Standard Bank had 26% of the credit card market (ABSA 25%); ABSA had 32% of mortgages (Nedocr 24%); Firstrand had 29% of installment finance (ABSA 25%), and Nedcor was the biggest in overdraft and other loan finance with 24%.

A later chapter in the report attempts to simulate SA bank costs and revenues, in the absence of detailed primary data, which proved hard to come by. It is noted that high fixed costs require huge volumes of transactions to recoup these costs, and if those volumes are not achieved, then bank charges must rise. Cash is the predominant form of payment in SA and there is a high cost-to-revenue ratio for cash processing. Therefore one might expect SA bank costs to be high compared to certain other markets. This conclusion is, however, slightly at odds with earlier conclusions in the report that SA banks are highly profitable.

The next chapter is also a simulated analysis of how costs and revenues would compare if the Postbank (or second or third tier banks) had to offer expanded banking services. The analysis is more speculative than conclusive, but it suggests that the low volume of transactions per person and the high costs per account holder would tend to make the Postbank a costly way of providing banking services, but more importantly that if the number of account holders increased dramatically, then costs would flood revenues. Therefore it appears that the Postbank might not be an ideal option for rollout of financial services to low-income consumers. But among the conclusions of the report are recommendations for an expanded role for the Postbank and for second and third tier banks.

Second and third tier banks are described in the report. Second tier banks may not re-lend deposits. There are two types of second tier banks: narrow banks may only invest deposits in liquid money market assets, while core banks may only lend against their second tier capital (their subordinated debt). Third tier banks may lend out their deposits but only to people within the community: they are stokvels and village banks and community banks.

The chapter also hypothesises on the viability of cell phone operators, mass retailers, Internet providers and micro-lenders becoming more involved in banking services. Here, the analysis is speculative in nature, but does indicate some of the exciting possibilities facing the industry, if obstacles such as access to the national payments system can be overcome.

The payment system is described in the report, but there is little detail about how this complex system works. There is little mention of the competition issues involved, particularly the access issues, although it is mentioned that the big banks control the payment system. A recommendation of the report is that the payments system be more thoroughly investigated in future. A possible concern is whether a potential competitor to the big banks would be able to get access on reasonable terms to the payments system, given that the same big banks control it.

The next chapter deals with how to provide services to the unbanked and considers, what was at the time, just a proposal by the banks namely, the Mzansi Account. The report expresses concern that electronic payments would not be permitted according to the basic bank account offering, although electronic credits are catered for. The chapter also mentions the plans and prospects of the Postbank, Teba and African Bank, concerning provision of banking services to the poor.

To some extent the report has been overtaken by developments in this area. The banks had originally proposed that it would be necessary for them to set uniform interest rates in respect of the basic bank account product. However, following objections raised by the Commission and by Minister Manuel, the banks decided that they would each set their own interest rates after all. The Mzansi national basic bank account was subsequently launched and seems to have been very successful.

Next, the report looks at the competitive environment in the various market segments, for both high-income and low-income consumers. For low-income consumers there is little choice compared with high-income consumers, who are relatively spoilt for choice between banks. Bank charges are also reported on, for the various SA banks as well as for various banks in comparator countries. The Commission provided some of the data for this section of the report. The data indicates that SA has very high bank charges as well as a high interest margin and is the only country apart from Canada where banks charge at all for taking deposits.

The report also addresses the costs, difficulties and availability of financing for SMEs, and finds that it is only slightly more expensive for SMEs to run a business account rather than an individual account (whereas in the UK it is far more expensive to use a business account). The problems of switching costs and the need for education of small business owners are duly noted.

Concerning transparency, governance and disclosure, the report finds that in general, information provided to consumers on bank services and charges is difficult to understand, is not comparable between banks, and cannot be untangled because charges and services are bundled together. Ways of disclosing fees and transactions are not standardised between the banks. Bundling disguises cross-subsidisation and differential pricing of services. It is noted that since the UK Cruickshank report was released, it is now possible to obtain standardised comparative banking fees for all banks in a market segment from the UK Banking Association website.

On the regulatory and legislative environment, the report notes that in SA, the sector regulators do not deal with competition or consider the effect of regulatory actions upon the competitive environment, as happens in the United States, United Kingdom and Australia. Barriers to entry (of being a bank) are explained as capital requirements (R250m), compliance and registration costs, the lack of deposit insurance (which limits the size of loans that small banks can make), and others.

Finally, several recommendations emerge from the report. These include that the Government should introduce improved disclosure requirements on banking services; banks should be compelled to offer unbundled services and pricing options; penalty fees, charges for essential services and charges for services not open to competition should be levied on a cost-plus basis; sharing of client information should be practiced, to lower information barriers of entry into banking, as well as to facilitate switching between banks.

The Government should pass enabling legislation for second and third tier banks. (This process has now commenced, with two Bills having been released for comments by the National Treasury.)

The Government should consider transforming the Postbank to provide deposit taking and electronic transmission services to the poor. It should ease entry of foreign banks by addressing capitalisation requirements therefore allowing them to count offshore capital rather than requiring SA capital. The Government should also prohibit the practice of preferential processing of payments and a deposit insurance scheme for all banks should be established.

Recommendations that apply to the Commission in particular are the following:

- The concept of ‘complex monopoly’ – how to deal with firms that are not individually dominant but that nevertheless operate in a collectively dominant fashion – should become part of the remit of the Competition Commission.

- The Commission should investigate whether the National Payments System effectively operates as a ‘complex monopoly’.

- All bank and payment regulators should be required to consider the competitive impact of their regulation.

The Commission has targeted the banking sector for extensive research and possible investigations in 2005. The payments system will be examined and the applicability of the complex monopoly concept within existing competition legislation will be explored.

Contributed by Geoff Parr

The hidden costs of BEE deals that cannot be ignored

A lot of companies are driven into buying minority stakes in bigger corporations which they tend to see as good business, growth or investment opportunities. Most of these deals are, however, driven by industry charters, which have started a race among industry players to obtain certain percentages of representation by previously disadvantaged individuals either in respect of ownership or management in order to deal with government. Strategic partnerships with BEE firms have become an important aspect in board meetings of many industry players. The country has seen this race in mining, financial services and most recently, in the ICT sectors.

The Commission reported a 61% increase of BEE transactions in its Annual Report for the financial year 2003/2004, with the manufacturing sector accounting for 22% and mining and financial services at 19% each. Wholesale, information technology and other sectors accounted for less than 9% each. These figures are likely to increase as various sectors adopt industry charters and as companies restructure and unbundle assets in preparation for the charters.

Large corporations are often willing to offer a 10% to 25% stake depending on their empowerment targets, strategies and plans. BEE companies that are acquiring these shares often negotiate certain rights to get some level of influence in the company so that they are not seen merely as ‘fronts’. The problem is that such influence does not come cheaply, especially if it is not what a minority shareholder is ordinarily entitled to in terms of the company laws of the country. There is a high chance that the acquisition of those rights may trigger regulatory intervention that may have some financial implications for the acquiring of BEE shareholders.

A 25% stake, in itself, should ordinarily give comfort to BEE shareholders in that they would have sufficient rights to protect their financial interests. However, there is a tendency to negotiate for more rights in the shareholders agreement. Though there is nothing wrong with the ability to negotiate for more, especially if one ultimately gets these rights, it is important to consider what the consequences of such negotiations may be. Because of those rights, an ordinary sale or investment venture may trigger a merger under the Competition Act, whether intended or not. This then gives rise to costs of preparing notification of that merger to the competition authorities for approval. Affected in the process may be share prices in time sensitive markets, which may drop in response to the unexpected but necessary delay.

In addition to that, filing fees are payable when notification is submitted to the Commission, which are R75 000 for intermediate mergers and R250 000 for large mergers, excluding VAT. Often, parties to the merger would negotiate and agree as to how and who will pay the filing fee in cases where the parties know about it in advance. In a case such as this, who is likely to bear the unexpected costs? If one negotiated those extra rights, would it not be courteous to offer to pay these fees? Whether one obtains a loan from a bank or from the seller - who is often a large corporation capable of providing such loan - the acquiring BEE firm may be the one paying for those costs. This is a common principle in negotiations. But would it not be sad if one did not even think about this or plan for these costs?

What if the parties did not realise in time that they need prior approval from the competition authorities to implement the deal? This is highly likely to occur because most of these deals are time sensitive. Assuming the Commission finds that they implemented the deal prematurely, they may be liable to a fine of up to 10% of their annual turnover.

The critical question is: are BEE firms receiving proper advice on these deals, do they know about these 'hidden' costs, or do they come as a surprise to them when the deal is completed? These are the questions to ask as a BEE company when negotiating these kinds of deals. We know that more often than not, the priority is to get the deal done, but the question is, at what cost?

A pure 25% minority stake may not raise the ears of competition authorities, however, it would be of concern if a minority shareholder gets given more rights than what that shareholder ordinarily would be entitled to. These include veto rights in respect of budgets, business plans, appointment of senior management, etc, which veto rights would confer de facto control. If consent of a BEE minority shareholder would be required on strategic matters such as these, a merger would be triggered. It is not necessary to buy 50% plus to acquire control for the purposes of competition laws. Material influence over a company may suffice in some circumstances.

Thus, if you do not intend acquiring control, be careful not to ask for more rights than you deserve under the normal company laws as a minority shareholder. Many companies in BEE deals that get notified to the Commission often argue that it was never their intention to acquire control. The sad part is, most minority shareholders seldom exercise many of those rights, but the mere ability to exercise them puts them in a position of control from the competition law perspective. Generally the intention is merely to negotiate for more security. Be warned because, the line between security and control is very thin.

Some sellers may be willing to give a minority shareholder those rights 'on paper' to avoid delays in the deal. Besides, the immediate benefits of getting the deal through may be more than worrying about a BEE company that wants a veto on the budget. Especially when there is a possibility that such veto is unlikely to be exercised in practice. Granting such rights may trigger a merger and may increase the costs of that deal unnecessarily for a BEE company, even if the seller thinks it is not a 'big deal'. By the way, we have seen in recent media reports that minority shareholders are now invoking those veto rights to the surprise of the majority shareholders when push comes to shove. So it may be a big deal after all.

The advancement of SME and BEE firms is key to the development of the economy. It has been found in many studies, both local and international, that the SME sector in particular accounts for a significant percentage of employment in many economies. The last thing we need is to have a situation where transactions costs become an obstacle or barrier for these companies to enter certain markets or acquire meaningful stakes in large corporations. Some markets are difficult to enter due to technology or infrastructure required and the only option available may be to acquire stakes in existing companies. Besides, there is also a need to facilitate a greater spread of ownership of the markets and the economy. Though some costs of transactions cannot be avoided, most are dealt with more easily if they are known and proper plans to cover them are negotiated in time.

It is therefore advisable for SME or BEE companies to seek legal advice in time before negotiating deals, no matter how small they think the deal is. The costs to them may not be that small. The Commission is also available to advise on deal structures that may trigger its intervention. Do not expect the Commission to advise you on how to best structure a deal to avoid notification, as it is not one of the roles of the Commission.

Contributed by Zodwa Ntuli

Compulsory notification once a merger is triggered

Before the Competition Act 89 of 1998 (the Act) was introduced, there were no pre-notification requirements for mergers. With the introduction of the Act, the situation has now changed.

It is now compulsory that the Commission is notified before the implementation of certain types of mergers in terms of section 13A of the Act. This requirement applies to intermediate and large mergers and implementation of these by the merging parties without obtaining the necessary approval from the competition authorities will amount to the contravention of the Act. Furthermore, those parties will subject themselves to prosecution and eventually to the imposition of an administrative fine by the Competition Tribunal.

However, there is an exception to the requirement of compulsory pre-notification of mergers. It is not compulsory to notify the competition authorities of small category mergers before they

are implemented. In terms of section 13 of the Act, parties to a small merger may implement the merger, but the Commission may require notification should the merger raise public interest or competition concerns. The Commission may only require such notification within six months of the implementation of such small merger.

The rationale behind notification is to enable the competition authorities to assess the impact of a merger on competition, as well as the relevant market structure. A further consideration is that of public interests set out in section 12A(3) of the Act.

The purpose of a merger is not a relevant consideration at all when it comes to the requirement to notify. "The trigger for notification is a change of control, irrespective of the consequences for competition." [1]

The common perception noted through interaction with merging parties and practitioners is that parties tend to view certain transactions merely as restructuring or re-arranging of the original one with no intention to change, establish or acquire control. They further argue that ultimate control remains the same, or that if there is any acquisition or the argument that it is often advanced in so-called rescue transactions which are aimed at restructuring financial arrangements.

A typical scenario that has been observed in most cases is as follows:

A holding company, A, has shareholders, namely A1, A2 and A3 who hold 50%, 25% and 25%, respectively of A's issued share capital. All shareholders exercise joint control over A. A1 is required to obtain funding within a stipulated time period in which to meet the financial obligations it has to its co-shareholders.

A1 fails to secure the required funding. A2 provides the required funding that A1 was unable to provide. As a result, a new structure is put in place for purposes of this funding. A1's share holding is consequently diluted in A. A1 transfers 40% of its shares in A to A2, thus remaining with 10%. A2 immediately transfers that 40% to the new structure, Newco. At the same time A1 sells its 10% to Newco. Newco then acquires 50% of the issued share capital of A which was previously held by A1.

After this, A1 subscribes for shares in Newco that would result in A1 having 51% voting shares in Newco and A2 holding the remaining 49% voting shares. Accordingly, A1 would continue to control A in the same way, but through Newco. A2 and A3 would, after the introduction of Newco, continue to hold 25% each in A directly. Joint control in A would still prevail.

It is argued that the above will not result in the acquisition of sole control by A's shareholders. Furthermore, the parties do not relinquish their existing joint control. Thus no merger occurs.

Even though the above scenario would be regarded as financial restructuring only aimed at redeeming the original transaction, during this process a number of mergers occur that would require notification if they do fall in the category of large or intermediate mergers.

Notable instances that could trigger a merger in the above scenario are the following:

A1's transfer of 40% shares in A to A2 would result in A2 beneficially owning more than 50% of A's issued share capital. This constitutes a merger where notification would be compulsory if the stipulated threshold is met. The contention often raised in this regard is that this is a temporary acquisition of control as A2 acquires those shares and passes them on immediately to Newco. A2 has no intention of owning those shares. A2 is just a conduit for those shares. Although it is appreciated that transactions similar to the one put in this scenario are entered into temporarily, the merger provisions of the Act do not distinguish between long-term and short-term acquisition and establishment of control. The mere acquisition or establishment of control triggers a merger that should be notified if the required thresholds are met.

Another instance where a merger would be triggered in the above scenario is if Newco is introduced. Newco would eventually acquire 50% previously held by A1 in A. Consequently, Newco would assume joint control over A, the type of control that it did not have before.

The contention raised with regards to this scenario is that Newco is not a commercial enterprise that generates turnover and can therefore not be considered as a business. Though this argument makes sense, the fact that it has not generated any income does not make it any less of a firm or business that is capable of acquiring control. The argument can only find relevance when one determines the threshold for notification and not as to whether a merger has occurred. Newco is, in most cases, a shelf company. It is further argued that it is just an intermediate step that makes the rescue possible.

Another transaction that could result in a merger scenario is where A1 acquires control over Newco following the subscription for shares. Again, A1 did not have such control before, and one must bear in mind that Newco is an independent and separate entity from A1.

As can be seen from the above scenario, a single transaction aimed at rescuing a deal may give rise to unintended mergers. There are also various reasons why companies choose to structure transactions like this and unfortunately these are not relevant in determining whether a merger has occurred or not.

Where multiple mergers such as these arise, all such mergers require notification separately unless the Commission directs otherwise. Where it is of the view that such mergers are interdependent and indivisible, in which case a single filing may be allowed.

In similar situations to the one illustrated by the above scenario, parties involved are urged to seek advisory opinions from the Commission so as to get proper guidance for compliance with the Act.

Contributed by Thanduxolo Lubanga

1 Brassey et al Competition Law, 1st edition 2002

The evaluation of efficiencies:

Consumer welfare standard vs. total welfare standard

The treatment of efficiencies in competition law is highly complex. Mergers and restrictive practices can actually deliver the benefits of efficiency to customers, shareholders, employees and suppliers, in certain circumstances. These benefits include products produced at lower costs, higher quality and the creation of new products. Less obviously, mergers and restrictive practices can contribute to stability of employment, the retention and better application of scarce worker skills and to the better management of supply chains. However, just as they promise benefits, mergers and restrictive practices can pose certain risks to consumers and/or competitors.

Efficiencies include anything that is likely to lower price or cost, to expand output, improve quality, enhance service, or encourage innovation. We can distinguish between two main types of efficiency: allocative efficiency and productive (or technical) efficiency.

In a free market, allocative efficiency arises when the price of a good reflects its scarcity and this ensures that the right amounts of resources are allocated to producing that good. But if a merger raises the price of a good, then the effect of that price rise is a decrease in output, and so too few resources are allocated to producing that good (compared with the competitive situation). That is what is meant by the allocative effect of a merger that lessens competition and raises price, and it is the allocative effect that leads to an inefficiency known as the deadweight loss.

Productive, or technical efficiency, is attained if the least-cost combination of resources is used in producing a particular good. Productive efficiency can be achieved for a good that is

produced under conditions of perfect competition, imperfect competition or even monopoly. But under sustained conditions of imperfect competition or monopoly, there are sometimes so-called ‘X-inefficiencies’ that erode productive efficiency because of the absence of competitive pressure on the firm.

Efficiencies may also be classified as either static (attainable with today’s resources and technology) or dynamic (expected to be reaped in future).

There is no need to emphasise productive efficiencies over allocative efficiencies or vice versa. By the same token, static efficiencies may or may not be more important than dynamic efficiencies in any given case. But it is important to distinguish between real efficiencies and redistributive (or pecuniary) efficiencies. Strictly speaking, only real savings of resources should be recognised as true efficiencies. If firms save on costs because the merger increases their bargaining power and enables the merged entity to extract wage concessions or discounts from suppliers (not corresponding to cost savings), that is only a wealth transfer (from workers or suppliers to the firm) and it should not be counted as a social efficiency. Further, both variable and fixed-cost savings are relevant to the efficiency analysis because both generate producer surplus, even though only variable cost savings generate a short-run incentive for the firm to cut prices. However, if competition authorities use a pure consumers’ surplus standard, only savings in variable costs are normally considered. This means that some types of efficiencies, for example eliminating duplication of administrative routines, might not be considered, as they do not affect variable costs.

Dynamic efficiencies are thought to be more important to the competitive process, but they may be more difficult to verify. In *Trident Steel (Pty) Ltd. and Baldwin’s Steel*[2] the Tribunal elaborated on ‘real’ efficiencies as being dynamic efficiencies and production efficiencies ranging from plant economies of scope and scale, to research and development efficiencies that might not be achieved short of a merger or restrictive practice. The Tribunal also stated that *“pecuniary efficiencies would not constitute real economies nor would those that result in a mere redistribution of income from the customers, suppliers or employees to the merged entity.”*[3] Scepticism regarding acceptance of administrative efficiencies was also expressed.

Total surplus is the sum of consumer and producer surplus. *Consumer surplus* is the difference between what consumers (in total) would be prepared to pay and what they actually pay for a good. Producer surplus is the difference between what suppliers or producers (in total) would be prepared to accept as payment for a good and what they are in fact paid.

Note that if a merger or restrictive practice affects price, then the areas of consumer surplus and producer surplus will be affected in opposite directions. If price rises (due to a merger, for example), then consumer surplus will fall and producer surplus will rise (although not by the same amount, depending on the elasticity of demand, and the shape and positions of the cost curves, etc.).

Now it is clear that the change in total surplus is the net effect of the changes in consumer surplus and producer surplus.

Under the total surplus approach to evaluating claimed merger efficiencies, a merger would be permitted if it could be shown that the total of producers’ and consumers’ surplus would increase following a merger. The total surplus approach is the most permissive of welfare standards. The implication of this approach is that certain cost-saving mergers that transfer wealth from consumers to shareholders are allowed. Under the consumer surplus approach, no mergers that would likely increase consumer prices (and therefore reduce consumers’ surplus) would be permitted as part of an efficiency gains trade-off. Efficiency arguments would be permitted only within the analysis of whether the merger would likely prevent or substantially lessen competition.

After establishing that a merger is likely to substantially lessen competition, the Act requires that we must next determine whether it is likely to result in any technological, efficiency or other pro-competitive gain, according to section 12A(a)(i) of the Competition Act (no 89, 1998):

“(i) …which will be greater than, and offset, the effects of any prevention or lessening of competition, that may result or is likely to result from the merger, and would not likely be obtained if the merger is prevented.”

Or, in the event of certain restrictive practices, according to sections 4(1)(a), 5(1), 8(c) and 8(d), whether the effect of that practice is outweighed by:

"…any technological, efficiency or other pro-competitive gains."

Although the South African Competition Act's policy purposes start with economic efficiency, they extend further. The key purpose to 'promote and maintain competition', is extended by other sets of goals. Firstly, efficiency, adaptability and development of the economy are mentioned. The second goal is competitive prices and choices for consumers. This takes cognisance of concerns about consumer welfare. The other sets of policy goals are employment and social and economic welfare, opportunities to participate in world markets, and increasing the ownership stakes of historically disadvantaged persons.[4]

It is possible, but not necessary, to interpret the term 'efficiency' in the sense of static welfare analysis. Instead, combining it with 'adaptability' implies a greater concern for dynamic considerations about entry and mobility. The extent of the economic perspective is shown in the concept of promoting 'development of the economy'. Further, the provision of consumer interests entails both prices and choices. This implies that preserving outlets or brands might be considered important, even if that meant a somewhat higher price level.[5]

The efficiency provision in Section 96 of Canada's competition statute was the basis of the provision for efficiencies in Section 12 of South Africa's Competition Act. In the context of a merger to near monopoly in the steel domain, *Trident Steel (Pty) Ltd. and Baldwin's Steel* provided the Tribunal with the opportunity to examine closely how to deal with claims of efficiency. The Tribunal panel decided on an inverse sliding scale, following a review of how efficiencies have been treated in Canada and the United States.[6] Under a normal sliding scale the more competition is restricted, the higher the efficiency claims must be. An inverse sliding scale means that the stronger the showing of real efficiencies, the less need there would be to show how consumers would benefit directly. Whether efficiencies must be passed on to, or clearly benefit consumers depend upon the nature of the claimed efficiencies.

Considering claims of efficiencies only after finding that a merger could harm competition results in the merging parties having greater difficulty justifying it. An alternative would be to make efficiencies a factor to be considered in the context of determining whether a merger leads to a substantial lessening of competition, along with any other factor that is relevant to competition in a market that is or would be affected by the merger. This approach would be consistent with policy goals based principally on economic efficiencies. It would however require changing the statute, which currently treats efficiencies as a defence.[7]

The Canadian Competition Bureau recently distributed a paper, which launched a formal consultation process[8] on the treatment of efficiencies in relation to merger review and in relation to other areas of competition policy, such as specialisation agreements, joint ventures and strategic alliances. The Competition Bureau invited interested parties to submit their comments. Generally, the two most important approaches under consideration to the treatment of efficiencies in merger review included two options, in other words, the status quo and factor approaches. The status quo approach would mean retaining the merger efficiencies defence, as opposed to the factor approach, where efficiencies would be considered in the first stage of the merger, that is, in determining the transaction's net effect on competition.

It is true of all regimes that efficiencies are generally appreciated.[9] That is, there is a place for efficiency arguments to be made that could persuade any of these agencies to permit a merger/restrictive practice that might have some potential for anti-competitive harm. The scope for these efficiency arguments varies considerably. However, it is probably fair to say that the agencies and courts do not use efficiencies to balance against anti-competitive effects in any sort of total surplus calculation. In each case it would seem the focus is very much on whether the merger, agreement or restriction ultimately provides benefits to consumers, and that a sliding scale approach is used. That said, the treatment of efficiencies continues to evolve in all jurisdictions.

Contributed by Louise du Plessis and Geoff Parr

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2 CT 89/LM/Oct00

3 Ibid

4 OECD Global forum on Competition Peer Review: Paris, 11 February 2003. Competition Law and Policy in South Africa

5 Ibid

6 OECD Global forum on Competition Peer Review: Paris, 11 February 2003. Competition Law and Policy in South Africa, Box 1: EFFICIENCIES AND CONSUMER BENEFITS

7 Ibid

8 The Canadian Competition Bureau's consultation paper, Treatment of Efficiencies in the Competition Act, September 2004

9 European Commission's Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, 2004/C 31/03, O.J. C31/5 (5.2.2004); U.S. Department of Justice and Federal Trade Commission, Antitrust Guidelines for Collaborations Among Competitors (April 2000)

Competition policy and the SA-EU Trade, Development and Co-operation Agreement (TDCA)

Background[10]

South Africa relates to the European Union (EU) at various levels and forums. These relationships are at bilateral, regional and continental levels. The SA-EU Trade, Development and Co-operation Agreement (TDCA) governs the most important of these relations, which is at the bilateral level.

At the regional and continental levels, South Africa relates to the EU through the Berlin Process (SADC), the Cairo Process (Africa) and the Cotonou Partnership Agreement (CPA), which is the basis for co-operation between the African, Caribbean and Pacific Group of States (ACP).

After the first democratic elections in 1994, the South African economy was reintegrated into the world economy as a trading nation. To spur its economic growth, South Africa needed to attract investment, whilst also gaining access to other markets for its goods and products. Pursuant to these objectives, in June 1995 the EU Council of Ministers adopted negotiating directives proposing progressive and reciprocal liberalization of trade with South Africa in order to establish a Free Trade Agreement (FTA). After consultations with all relevant stakeholders in South Africa and the SADC region negotiations began, lasting nearly four years, until March 1999 when an agreement was reached. The FTA eventually culminated into a comprehensive all-encompassing Trade, Development and Co-operation Agreement, which was signed on 11 October 1999 and provisionally entered into force on 1 January 2000 (pending full ratification by all EU Member States).

The TDCA focuses mainly on the following areas of co-operation, namely; Political co-operation, Trade and Economic co-operation and other trade related issues and Development co-operation.

The full ratification of the TDCA by all 15 EU member states (after its provisional implementation on 1 January 2000) progressed at a snail's pace and was only concluded at the beginning of 2004. The implication of full ratification has meant that, starting from 1 May 2004 the TDCA is now being fully implemented. This means that co-operation on the articles of the TDCA that were put on hold pending full ratification, are now being activated. One of these areas of co-operation, pertinent to the Commission, is competition policy.

The first review of the TDCA will take place during 2005.

Competition Policy in the TDCA

The TDCA deals with competition policy issues in Articles 35 to 41. The basic goal of these articles is to monitor and prevent any anti-competitive conduct that may take place within the EU or South Africa, in so far as that conduct affects trade between the two territories. Article 35 states:

"The following are incompatible with the proper functioning of this Agreement, in so far as they may affect trade between the Community and South Africa:

(a) Agreements and concerted practices between firms in horizontal relationships, decisions by associations of firms, and agreements between firms in vertical relationships, which have the effect of preventing or substantially lessening competition in the territory of the Community or of South Africa, unless the firms can demonstrate that the anti-competitive effects are outweighed by pro-competitive ones;

(b) Abuse by one or more firms of market power in the territory of the Community or of South Africa as a whole or in a substantial part thereof."

Article 36 of the TDCA requires the establishment of competition authorities by either party (EU or South Africa) within a period of three years after the coming into effect of the agreement. In Article 37, the TDCA addresses the situation where a conduct that is incompatible with the provisions of Article 35, and is not adequately dealt with by Article 36. In such a situation it is envisaged that the party concerned, in accordance with its own laws, will deal with such conduct.

The issue of comity is addressed in Article 38. The TDCA states, in subsection [1]:

"The Parties agree that, whenever the Commission[11] or the South African Competition Authority has reason to believe that anti-competitive practices, defined under Article 35, are taking place within the territory of the other authority and are substantially affecting important interests of the Parties, it may request the other Party's competition authority to take appropriate remedial action in terms of that authority's rules governing competition."

Article 38 goes on to address the issues of independence and consultation between the two territories in subsections [2], [3] and [4]. Technical assistance is dealt with in Article 39. In this Article, it is envisaged that the EU will provide assistance to South Africa by way of exchange of experts, organisation of seminars and other training activities. The exchange of information (taking into account confidentiality requirements) between the Commission and the South African Competition Authority is addressed in Article 40, and Article 41 covers state aid.

The Commission's position paper

In September of 2004, the Commission submitted a position paper at a TDCA meeting hosted by the Department of Foreign Affairs in respect of the areas that need review as far as competition policy is concerned. The following are some of the main points contained in that submission.

Comparing the contents of Article 35 with the contents of similar bilateral agreements on competition, other agreements start by setting out the purposes, and also define both competition legislation as well as competition authorities. Perhaps these should also be inserted into the TDCA.

The scope of Article 35 appears to cover only agreements that might be anti-competitive when evaluated according to a 'rule-of-reason' analysis. Anti-competitive practices that are prohibited outright in both the EU and SA, such as price-fixing, are presumably also to be subjected to a rule-of-reason analysis, whereby firms accused of such practices can argue that the anti-competitive effects are outweighed by the pro-competitive effects. This appears to be inconsistent with both the SA and EU competition law.

Article 35 does not appear to extend to merger consideration. Co-operation on merger consideration with the EU Commission would be extremely helpful in many transactions that must be notified to both the EU Commission and to the SA Competition Commission. The Competition Commission recommended that such co-operation on mergers be provided for explicitly in Article 35.

There might be a problem of how to deal with leniency. Both the EU and SA have leniency policies in operation. Perhaps there is a need to provide procedures for consultation between the parties before leniency is granted, in cases such as international cartels.

Article 40 should be bolstered by including time lines for notifications between SA and the EU, harmonising the notifications procedures, setting out procedures to facilitate the exchange of information, and for the treatment of confidential information. The existing provisions for exchange of information and the "limitations of professional and business secrecy" seem to anticipate that the exchange of information will not be possible where firms claim confidentiality. A more detailed procedure might be preferable, like that found in Article 177 of the EU/Chile Agreement. The EU/Canadian bilateral agreement (Articles VII – X) also goes into some detail around the exchange of information, the process regarding confidentiality, and the methods of various communications between the parties (for example: oral, telephonic, fax or diplomatic channels).

Article 41 concerns state aid or 'public aid'. Article 41 might be too lenient; perhaps there is a case for amending this Article to allow for defined elements of public aid only; and to stipulate that the Parties update each other regularly on changes to public aid. These limitations apply to other bilateral agreements, for example the EU/ Chile agreement (Article 177) stipulates annual updates.

Consideration should perhaps be given in the TDCA to provisions for the treatment of state-owned enterprises. The EU/Mexico bilateral agreement states very simply in Article 5(2) that the parties shall decide on "(d) State monopolies of a commercial character; and (e) public undertakings and undertakings to which special or exclusive rights have been granted". Article 179 of the EU/Chile agreement specifically allows the parties to designate or maintain public or private monopolies, but does constrain the parties from enacting future measures that would allow public or private enterprises to distort trade or competition. The importance of state-owned enterprises in the SA economy might need to be dealt with directly in the agreement.

Conclusion

The Commission adopts the position that further co-operation with the EU Commission on competition issues is desirable and will be of great assistance to the activities and objectives of the SA competition authorities. To this end, the Competition Commission will participate in future co-operation around the implementation and reviews of the TDCA.

Contributed by Junior Khumalo and Geoff Parr

10 Department of Foreign Affairs

11 European Commission

Cases

Harmony/Goldfields merger given the go-ahead conditionally

The Commission has made a recommendation to the Tribunal to approve the proposed merger between Harmony Gold Mining Company Ltd (Harmony) and Gold Fields Ltd (Gold Fields), subject to certain conditions aimed at addressing the employment concerns that arise from the proposed merger.

The proposed merger follows a process initiated in October 2004, in terms of which Harmony intends to acquire 100% of the issued share capital in Gold Fields. Harmony's stated reasons for the proposed acquisition include the need to create significant value, to revitalise Gold Fields South African asset portfolio, to create a new international major with a compelling equity story and enhanced investor appeal and also to access the value of Gold Fields' exploration portfolio. Gold Fields objected to the proposed merger.

Both Harmony and Gold Fields are involved in the production and supply of gold in the global market. In its assessment, the Commission found that South Africa accounts for approximately 14% of the world gold production, with

Harmony and Gold Fields accounting for 5.2% and 4.3% respectively. Thus given the low market shares of the two firms combined, the Commission found that from a competition perspective, the proposed merger is unlikely to raise significant concerns in the relevant market. This is more so because a change in the production of gold does not necessarily affect its world price, as this is determined at the daily gold fix. It appears therefore that no gold mine can influence the price of gold.

Gold Fields raised concerns that the proposed merger may affect some of its suppliers negatively. The Commission investigated this and found that it would not be in the best interest of Harmony to exclude suppliers post merger as they currently supply them as well. Also, Harmony's contracts are awarded on a tender basis or a basis of the best three quotes and there is no indication that other suppliers would be excluded from tendering or competing for the business of the merged entity post merger.

The Commission, however, found that the proposed merger raises serious employment concerns. Since this is a hostile takeover, it has not been easy to establish with certainty what the impact of the proposed merger would be on employment. Harmony anticipates that about 1 500 employees will be retrenched while interested parties, including trade unions, estimate between 1000 and 14 000 job losses.

In view of the discrepancies in the number of potential job losses, the Commission found it appropriate to attach the following conditions to address employment concerns:

- A moratorium, which shall apply for the period of 24 months, shall be placed on retrenchments at the merged entity to the effect that there shall be zero retrenchments at the merged entity below the level of corporate, management and supervisory positions as a result of the merger.

- That the merged entity may retrench up to a maximum of 1 500 employees in corporate, management and supervisory positions which shall mean positions from shift-boss level to the chief executive.

The Commission also recommended monitoring measures to ensure that these conditions are adhered to. These measures include submission by the merged entity of quarterly reports regarding the effects of the merger on employment. Reports must include, amongst other factors, current levels of employment per job category at the merged entity, the number of actual retrenchments per job category in the quarter reported on and the status of further retrenchments.

Although this merger does not raise competition concerns, it is the duty of the Commission to ensure that public interests such as employment are not adversely affected by it. Where such adverse effects are likely to occur, the Commission has to find a balance, because public interests are equally important in the Commission's analysis. In this case, it is the Commission's view that the conditions recommended herein will address the concerns without hampering the ordinary running of the merged entity's business.

The inconsistency in the information given by the various parties regarding the potential job losses in this merger did not make the Commission's investigation easy. However, the Commission is confident that this recommendation addresses all potential concerns in this regard.

Merger in furniture industry referred for approval

The Commission has made a recommendation to the Competition Tribunal to approve the large merger between Ellerines Holdings Limited (Ellerines") and Reylant Retail Limited (Reylant) without conditions. Though the merger will bring together two furniture groups in the already concentrated market, it is unlikely that it will substantially prevent or lessen competition.

Ellerines operates in the retail furniture and appliance sector and trades through five primary stores nationally. These are Ellerines, Furn City, Town Talk, Wetherelys and Osiers. The first three stores predominantly trade on credit whereas the last two are cash only stores. Reylant operates a wide range of stores, which includes Bears, Geen & Richards, Lubners, Savells/Fairdeal, Furniture City, Glicks, Mattress Factory, Dial a Bed and Early Bird. The Relyant stores can similarly be split into cash and credit stores where the first four aforementioned stores are known for primarily trading as credit facilities and the remainder primarily cash.

The merger will see Ellerines control the business of Reylant and as consideration Reylant shareholders will receive shares in Ellerines. The merged entity will compete with the JD Group, the newly listed Lewis Group and the furniture division of Shoprite which trade as OK Furniture and House & Home.

The parties to the merger target consumers across all income ranges. Although the Tribunal has in previous transactions found that particular LSM categories are regarded as relevant product markets, the Commission's investigation revealed that the markets have sufficiently changed to an extent that no clear or accurate distinction can be drawn between LSM groups identified in previous mergers in this sector. Furthermore, it is unlikely that the merged entity would be able to unilaterally abuse its position or behave in any coordinated manner with other market participants.

The Commission also found that the merger does not raise any significant public interest concerns.

Conditional approval of Afrox/Bidco merger recommended

The Commission has recommended to the Tribunal that the large merger between Business Venture Investments No. 790 (Pty) LTD. (Bidco) and Afrox Healthcare Limited (Ahealth) be approved subject to certain conditions. This follows a decision made last year by the Commission wherein a similar transaction was also conditionally approved. The parties restructured the initial transaction in an attempt to offset the competition concerns it had raised.

As a result of the significant changes made to the initial transaction, the Commission requested that the parties re-file so that it is analysed to address any competition issues that could be raised.

Bidco is a special purpose vehicle created to acquire A health. It comprises of shareholders who have indirect interest in the hospital industry, save for Mvelaphanda and IDC who have shares in Tshwane Hospitals (through Curamed) and Clinix respectively. Ahealth is a firm, which operates in the healthcare industry in the private hospital and healthcare services industries.

The transaction raises some competition concerns, therefore the Commission recommended that it be approved subject to the following conditions:

With regards to Mvelaphanda, that:

- It disposes of its entire share holding in Tshwane Hospitals within three months from the date of approval.
- All Mvelaphanda directors on the boards of Curamed and Tshwane Hospitals must resign.
- Dr Jackie Mphafudi, who is a director on the board of Medi Clinic and also a director of Mvelaphanda must also resign from the board of Medi Clinic.

With regards to IDC:

- The IDC dispose of their entire share holding in Clinix within six months from the date of approval.
- Any employee of IDC who is a director on the boards of Clinix must resign.

According to the Commission this transaction enables a BEE consortium to become a significant player in the South African hospital industry, without significant anti-competitive effects.

Furthermore, the Commission found that the transaction does not raise significant public interest issues.

Intellectual property rights exemption on appeal

The Commission recently finalised its decision on the first ever application for exemption based on the exercising of intellectual property rights.

This application relates to a request for an exemption in terms of Section 10(4) of the Competition Act 1998 (the Act) that provides that a firm may apply to the Commission to exempt from the application of Chapter 2 an agreement or practice, or category of either agreements or practices, that relates to the exercise of intellectual property (IP) rights.

The applicant is VISA South Africa, a branch of VISA International Services Association Incorporated, a corporation incorporated under the laws of Delaware in the United States of America (VISA). VISA is a membership association comprised of banks that become members on payment of the applicable membership fees. It is intended that a new entity, VISA National Organisation (VISA NO), which will be a South African run entity, will be established to provide the services currently provided by VISA.

VISA provides a payment processing system in terms of which the member banks that belong to VISA effect payment between themselves in respect of goods and services purchased by members of the public through the use of VISA credit cards. Currently VISA operates on the basis of a vertical agreement between itself and its member banks in South Africa.

VISA now proposes to set up VISA NO so that its members may have more autonomy in determining issues that relate to payment cards in South Africa (a function currently performed by VISA through a vertical agreement between it and its member banks). The banks that are presently members of VISA will be the shareholders of VISA NO and will appoint its board of directors and control VISA NO. In assuming the function of effecting payment between the member banks for goods and services purchased through the use of credit cards, VISA NO will utilise computer software used to operate the payment system (in respect of which VISA holds copyright) and other intellectual property rights like the VISA brand.

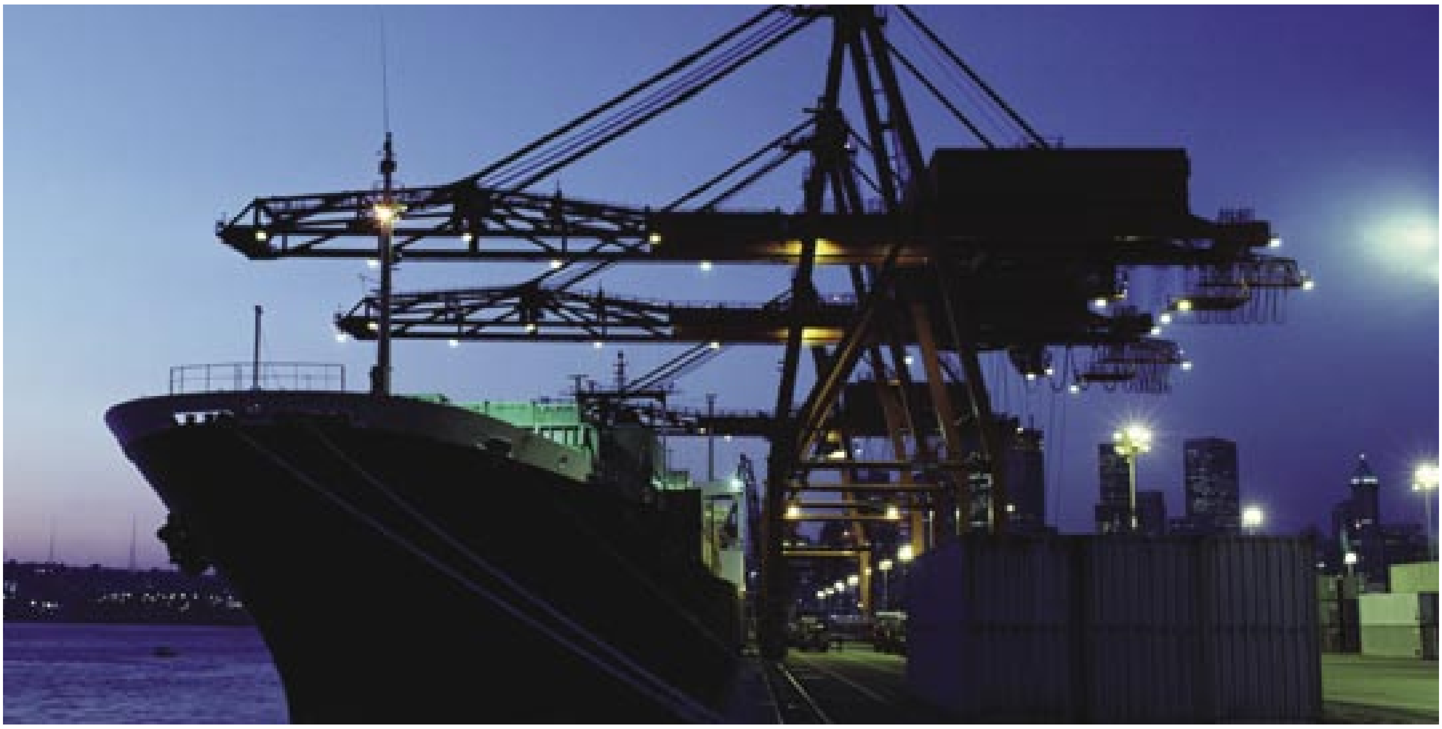
The member banks are in a horizontal relationship as shareholders in VISA NO and will effectively control the determinations which VISA NO makes and which would involve prices and could involve other trading conditions. In the absence of an exemption, the agreement would constitute a contravention of Section 4(1)(b)(i) of the Act.

After considering all submissions and the views of experts in the field of IP rights, the Commission concluded that the agreement relates to the exercise of an IP right and granted the applicant exemption until 30 April 2013.

In terms of Section 10(7) of the Act, any person with a substantial financial interest affected by a decision of the Commission in terms of Subsection (2), (4A) or (5), may appeal that decision to the Competition Tribunal. The Payment Issues Forum of South Africa (SARPIF) and eleven other applicants decided to appeal against the decision of the Commission.

The date for hearing the Appeal is not set, but it promises to be a very interesting case with ground breaking guidelines on the interpretation of issues relating to the exercise of intellectual property rights and the application of Section 10(4) expected.

The Commission refuses to grant exemption to South African Port Operations Division



In February 2004 Transnet Limited, acting through its South African Port Operations Division (SAPOD), applied in terms of Section 10 of the Competition Act 89 of 1998 (the Act), for exemption from the provisions of Chapter 2 of the Act in respect of a single agreement (the agreement).

The agreement is contained in a Memorandum of Agreement entered into in 2002 by SAPOD with Central Timber Co-operative Limited (CTC) and Mondi Limited trading as Silvacel (Silvacel). It commenced on 1 July 2002, and (subject to certain provisions allowing for earlier termination) is to endure for ten years.

The agreement records that a conveyor system, defined as the Link, has been constructed in the Port of Richards Bay and is being operated by SAPOD under a Memorandum of Understanding between SAPOD, CTC and Silvacel. The agreement thus takes the place of the Memorandum of Understanding. CTC and Silvacel are exporters of woodchips in large volumes via the dry bulk terminal in the Port of Richards Day.

In terms of the agreement the Link (which is to be operated and maintained by SAPOD) is for the exclusive use of CTC and Silvacel, and will convey woodchips only, for so long as certain minimum volumes are maintained.

CTC and Silvacel pay for the use of the Link on the basis of a rate per metric ton, subject to certain adjustments.

In the event that the minimum volumes specified are not maintained, SAPOD is entitled to secure other customers to use the Link, subject to the exercise of due care to prevent contamination of woodchips by other products conveyed. However, CTC and Silvacel have the right to make up the monetary shortfall to SAPOD resulting from their failure to maintain minimum volumes, in order to maintain their exclusive use of the Link.

The Commission has, after consideration of the agreement and investigation of the effects of its operation, come to the conclusion that the agreement does not constitute a prohibited practice in terms of Chapter 2 of the Act.

In terms of Section 10(2)(b)(ii) of the Act, the Commission must refuse to grant an exemption if the agreement for which the exemption is sought “does not constitute a prohibited practice in terms of this Chapter”, in other words Chapter 2.

Accordingly, SAPOD’s application for exemption must be refused and it is therefore unnecessary and it would be inappropriate for the Commission to go on to consider the ground advanced for exemption, namely that the agreement contributes to and is required to attain the objective of 'maintenance or promotion of exports' referred to in Section 10(3)(b)(i) of the Act.

The reasons for the Commission's conclusion that the agreement does not constitute a prohibited practice in terms of Chapter 2 of the Act may be stated briefly as follows:

It follows that there is a possibility that the Link may, at some point during the existence of the agreement, have significant idle capacity that could be maintained on the basis of the agreement while other exporters or handlers of export cargoes wishing or needing to use that capacity are excluded from using it. This, however, remains only a possibility. It is not the reality of the situation at the present time.

After investigating the physical and operational circumstances which have existed since the inception of the agreement and which now exist at the Port of Richards Bay, the Commission has concluded that the agreement does not constitute an abuse of dominance by SAPOD within the meaning of the Act, nor does it have the effect of substantially preventing or lessening competition in the relevant market i.e. the market for conveyor-driven harbour facilities for export commodities at the Port of Richards Bay.

In the Commission's view, the agreement does not entail a refusal by SAPOD to give a competitor access to an essential facility when it is economically feasible to do so, as contemplated in Section 8(b) of the Act. The Link cannot properly be regarded as an infrastructure or resource that cannot reasonably be duplicated; nor is it one without access to which competitors cannot reasonably provide goods or services to their customers. In any event, there has not been any refusal by SAPOD to give access to the Link to any competing cargo handler or indeed to any exporter wishing to use it.

In the Commission's view, under the circumstances prevailing at the Port of Richards Bay, the agreement does not entail engagement by SAPOD in an exclusionary act having an anti-competitive effect which outweighs its technological, efficiency or other pro-competitive gain as contemplated in Section 8(c) of the Act. The construction of the Link and its operation by agreement between SAPOD and CTC and Silvacel has had the effect of expanding woodchip-exporting capacity at the Port. The only other woodchip exporter currently operating at Richards Bay is located in a position where it would not be feasible for it to make use of the Link, and the same will apply in the case of another such exporter due to be established at the Port. There is no indication that any firm has been, is being or will be prevented or impeded by the agreement from entering into or expending within any market. In fact, the construction of the Link and its operation in terms of the agreement has reduced pressure on alternative conveyor facilities at the Port and has thus potentially made it easier for firms other than CTC and Silvacel to enter or expand their exports or the handling of exports through that Port.

In the Commission's view, for essentially the same reasons, the agreement has not had and does not now have the effect of substantially preventing or lessening competition in any market as contemplated in Section 5(1) of the Act. In any event, at least under the circumstances prevailing at present, it would not be difficult for a party to the agreement to prove that anti-competitive effects of the agreement (if any) are outweighed by technological, efficiency or other pro-competitive gains.

While, for these reasons, the Commission has come to the conclusion that the agreement does not constitute a prohibited practice in terms of Chapter 2 of the Act - and must therefore refuse the application for exemption - it should be noted that this does not necessarily mean that the continuation of the agreement could not come to constitute a prohibited practice in the future if the circumstances upon which the Commission's present conclusion is based were to change in vital material respects.

A complaint lodged in watch industry

In April 2004, a complaint was lodged by a group of independent watchmakers against certain of the manufacturers and distributors of high priced/quality watches. Specifically it was alleged that the respondents are abusing their dominant positions in the market in that they have recently stopped supplying the complainants with spare parts to effect watch repairs. Instead they require that the complainants send the watches to the respondents for repairs. As a result, the complainants cannot provide a service to their clients who own watches manufactured or distributed by the respondents.

- The first aspect considered at a very early stage of market definition analyses was substitutability, whether, local or national, and it was decided to compare the factors laid down by the Courts in various matters pertaining to substitutability, exclusionary behaviour and tying. It was established that import substitutability does exist on original and generic parts and imports are freely available at very competitive prices. In light of the aforesaid, no further analysis was required under Sections 8(c) and 8(d)(iii) of the Competition Act.

- The second aspect considered during the analyses was Section 5(1). However, the possibility of a successful prosecution under Section 5(1) seemed very slim as the efficiency arguments weighed strongly in favour of the exclusive distribution agreements. The respondents averred that due to the nature of the brands they sell, good workmanship on all repairs is essential. Therefore, it is averred that due to numerous complaints received on repairs done by independents, the decision not to supply original spare parts to independents was done to protect the brand and investment of the customer. Further to this, it was argued that there is no substantial lessening or prevention of competition due to the availability of substitutes.

In light of the above, the Commission decided not to refer the matter to the Tribunal for further determination and decision.

Tobacco industry case referred

The Competition Commission investigated the complaint lodged in October 2003 by JT International South Africa (Pty) Ltd. (JTI) alleging various anti-competitive practices by British American Tobacco South Africa (Pty) Ltd. (BATSA). The Competition Commission's investigation revealed that BATSA had engaged in practices that are prohibited in terms of the Competition Act 89 of 1998 and has referred the complaint to the Competition Tribunal for adjudication.

The Tobacco Products Amendment Act of 2000, which came into operation in 2001, prohibits any form of advertising by tobacco companies, allowing them only to indicate availability of products at point of sale. Subsequent to this regulation, BATSA has, since January 2001, concluded various trade investment agreements with retailers, merchandisers, outlet and/or venue owners and cigarette vending machine operators, which allow BATSA exclusive display rights at point of sale. In addition, BATSA implemented two retailer incentive programmes namely the Vecta and Sprint programmes aimed at the independent convenience channel. These programmes provide a personal incentive to retailers in the independent convenience channel to market and sell BATSA branded cigarettes irrespective of the price, quality advantages and consumer demand that competitor brands may offer.

As BATSA is dominant in the relevant market with over 90% market share, and because retailers are rewarded in terms of the trade investment agreements and the Vecta and Sprint programmes, it is beneficial for the retailers, merchandisers, outlets and/or venue owners and cigarette vending machine providers to participate in BATSA's strategy and, as far as possible, comply with BATSA's requirements to secure preferential and exclusive use of point of sale by BATSA.

This conduct raises barriers to entry, as prospective new entrants into the relevant market find it difficult to advertise, promote or indicate the availability of their products to end consumers.

Through the conclusion of the trade investment agreements and the Vecta and Sprint programmes, BATSA requires and/or induces retailers, merchandisers, outlet and/or venue owners and vending machine providers not to deal with JTI or other competitors in the relevant market.

It also appears that the conclusion of these trade investment agreements and the Vecta and Sprint programmes give rise to anti-competitive effects, either explicitly or as a result of their inherent potential effects in that it impedes or prevents JTI and other competitors of BATSA from entering into or expanding within the relevant market.

Comments to the Editor

The editor of Competition News received a comment from one of the readers regarding the article 'Settling the dispute with BHF' which appeared in the October 2004 edition.

The reader commented that it was technically incorrect for the Commission to state that "It must be emphasised that price fixing by professional associations and firms in the healthcare sector has been dealt with and prosecuted vigorously in other jurisdictions such as the United Kingdom, Canada and the United States, over 10 years ago. Until 1998, South Africa did not have a competition regime to address issues of this nature and as a result, they continued to exist as a norm."

The Editor's response: We agree that South Africa has a long history of competition law. However, the regime prior to 1998 was not designed in such a manner that effectively addressed the issues.

This is the reason why companies have continued unpunished in all the years prior to 1998. This is what the statement sought to convey, and we apologise if it appeared to suggest that South Africa did not have a competition law regime.

Towards a free and fair economy for all

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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