

Regulation of dominant firms in South Africa

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Abstract

This research report considers how dominant firms can establish when their competitive strategies are not anti-competitive. It argues that a dominant firm's actions can either be pro-competitive, thus conduct which competition law is designed to protect; or, anti-competitive and therefore prohibited. It questions whether there are any key principles that are emerging from South African competition law practice and decided cases that can provide some guidelines to dominant firms on whether planned action is prohibited conduct? It also questions whether the enforcement of the South African Competition Act's abuse of dominance provisions may have led to the chilling of competition. The research utilised the following methodologies: expert interviews; case studies; and, review of the competition authorities' enforcement actions. The report concludes that abuse of dominance cases are highly fact-intensive, industry specific and outcomes are effects-based. As such, it is difficult to prescribe a general rules-based compliance program to guide dominant firms in their development of competitive strategies.

Key words

competition, competitive, strategies, dominance

Declaration

I declare that this research project is my own work. It is submitted in partial fulfilment of the requirements for the degree of Master of Business Administration at the Gordon Institute of Business Science, University of Pretoria. It has not been submitted for any degree or examination in any other University. I further declare that I have obtained the necessary authorisation and consent to carry out this research.

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CHAPTER 1: INTRODUCTION TO THE RESEARCH PROBLEM

1.1 Introduction

Regulation of dominant firms is concerned with the prevention of abusive conduct by a monopoly or dominant firm. It is argued that a market in which there is only one economic actor (monopoly) tends to be complacent and lethargic (Brassey, 2005). While some may view monopolies as bad in themselves, competition law (including the South African Competition Act) is concerned with the conduct of the dominant firm (including a monopolist), not its existence. Furthermore, the conduct must constitute an abusive exploitation of the power conferred by dominance (Brassey, 2005).

The problem with monopolies is that they can choose to increase their profits by raising price and restricting output, or act in ways that forestall potential competitors. A monopolist's or dominant firm's choice of price and quantity can be based on a strategy for profit maximisation by sacrificing current profits (Simkins, 2005). In the short run, such firms may price below cost to drive out actual or potential competitors, but only if they are then able to recoup losses by charging a supra-competitive price.

While all monopolies are dominant firms, not all dominant firms are monopolies. The term monopoly refers to a single economic actor or firm in a specific market. A

dominant firm is one which has a large share of a specific market. A monopoly can therefore also be described as a dominant firm.

This paper will examine the approach that has been taken by South African competition law authorities in the regulation of dominant firms, and given this approach, how such firms can pursue competitive strategies that ensure long term profitability and sustainability. How can dominant firms ascertain whether their conduct is competitive or anti-competitive? Have the South African competition authorities been over-zealous in their enforcement of competition law in the area of abuse of dominance? It is expected that the research will uncover some general principles that will guide dominant firms in their decision making.

Chapter one will provide background information; chapter two will review the literature on the regulation of dominant firms; chapters three and four will discuss the research questions and methodology; chapters five and six will discuss and analyse the research findings, respectively; and finally, the conclusion will be in chapter seven.

1.2 Background

South African Competition Act

The South African Competition Act (“the Act”) can be broadly categorised as dealing with restrictive practices (chapter 2) and merger regulation (chapter 3). Restrictive practices are then divided into bilateral (restrictive vertical and

horizontal agreements which may involve more than two firms) (Part A) and unilateral (Part B). In terms of the Act, unilateral restrictive practices are tantamount to require the abuse of a dominant position in the market (Brassey, 2005).

Dominant firms are subject to constraints upon their conduct that do not apply to non-dominant firms. A special responsibility is thus placed on dominant firms not to perform certain activities which non-dominant firms are free to perform. It is argued that this treatment is justified because in the presence of a dominant firm, the degree of competition is already weak, and any interference with the market structure may eliminate all competition (Rousseva, 2006).

A key component of the Act's abuse of dominance provisions is the definition of the relevant market in which the dominant firm operates. It is important to note that the Act's abuse of dominance provisions will not apply to a big firm that operates as a small player in several markets, as such a firm is not dominant in any particular market. A relevant market is one in which a small, but significant, non-transitory increase in price would lead to an increase in profit because of the absence of substitutes in the product or geographic market. A relevant market can also be defined by identifying what products consumers could switch to if a specific product became more expensive and if suppliers entered the market with little time delay (Messina, 2005).

Section 8 of the Act prohibits a dominant firm from charging an excessive price (8(a)), refusing to give a competitor access to an essential facility when it is economically feasible to do so (8(b)), and engaging in an exclusionary act, “if the anti-competitive effect of that act outweighs its technological, efficiency or other pro-competitive, gain” (8(c)). Section 1 of the Act defines an exclusionary act as “an act that impedes or prevents a firm from entering into, or expanding within, a market”.

Section 8(d) prohibits the following specific exclusionary acts:

- i) requiring or inducing a supplier or customer to not deal with a competitor;
- ii) refusing to supply scarce goods to a competitor when supplying those goods is economically feasible;
- iii) selling goods or services on condition that the buyer purchases separate goods or services unrelated to the object of a contract, or forcing a buyer to accept a condition unrelated to the object of a contract;
- iv) selling goods or services below their marginal or average variable cost;
- v) buying-up a scarce supply of intermediate goods or resources required by a competitor.

Exclusionary acts in both sections 8(c) and (d) are subject to a balancing test, to determine whether any claimed technological, efficiency or other pro-competitive gains outweigh their anti-competitive effects. In section 8(c) the burden of proof rests with the Commission or complainant, while in section 8(d) the burden of proof rests with the dominant firm (Unterhalter, 2005). In section 8(c) the onus is on the complainant to prove that the harm to competition outweighs the pro-competitive gains, while in section 8(d) the onus with regard to the balancing is reversed. However, in both sections, the complainant must still prove the conduct.

1.3 Research Problem

There have been debates on the approach taken by competition law authorities in their treatment of dominant firms. It is in the approach to dominant firm conduct that the role of competition law comes under intense scrutiny. This has led to numerous questions being asked, for example, does the regulation of dominant firms lead to the protection of such firms' competitors from competition itself (Fox, 2003)? Is there any benefit to such regulation, other than to weaker competitors (Fox, 2003)? It is argued that the loss of competitive opportunity by non-dominant firms on the merits should not be deemed anti-competitive (Fox, 2002).

There are arguments on whether the prohibited conduct by dominant firms has pro-competitive or anti-competitive effects. Beard, Ford and Kaserman (2007) argue that there are pro-competitive benefits of quantity discounts (covered under the Act's section 9 prohibitions on price discrimination). However, Elhauge (2009)

argues that contrary to arguments by Chicago School theorists and some Harvard School theorists, tying (prohibited under section 8) can indeed have anti-competitive effects.

It is important to have clear substantive principles that distinguish dominant firms' pro-competitive and anti-competitive conduct, otherwise competition law's abuse of dominance provisions could become ad hoc and unpredictable rules (Vickers, 2005). The challenge is distinguishing between exclusionary actions, which reduce social welfare, and competitive actions, which increase it (Fox, 2002).

The main issue for dominant firms is the ability to clearly distinguish when their conduct is pro-competitive or anti-competitive (Evans & Padilla, 2005). However, there is a thin line between dominant firm conduct that is robust pro-competitive and exclusionary anti-competitive. It is sometimes difficult for dominant firms to establish exactly when their proposed competitive actions would not fall foul of the Act's abuse of dominance provisions. The difficulty is that competitive conduct, if successful, naturally prevents firms entering and expanding within a market – which is the same effect that anti-competitive conduct has (Unterhalter, 2005). The challenge for a dominant firm is to develop its strategies and practices in such a way that gives it a greater chance of falling on the lawful rather than the unlawful side of the line.

1.4 Research Aim

Dominant firms should be able to ascertain from the onset whether or not their conduct is anti-competitive, and the approach that competition authorities would take in enforcement of the Act's provisions. This would enable the firms to compete effectively. It is however argued that lack of clarity on the anti-competitive nature of dominant firms' actions and the treatment of unilateral conduct in South Africa, may have had potential "chilling" effects on dominant firms' competitive conduct.

The purpose of the research is to understand how dominant firms can pursue competitive strategies which would not be found to be anti-competitive. It is hoped that the research will discover general principles that can guide dominant firms in their decision making on competitive strategies.

1.5 Research Scope

This paper focuses on competitive actions of dominant firms and how such firms can steer clear of the Act's prohibition of exclusionary conduct. The context of the study is the enforcement actions of the South African Competition Commission ("Commission") and Competition Tribunal ("Tribunal") on exclusionary acts by dominant firms.

As mentioned above, the term exclusionary act refers to conduct by a dominant firm that prevents actual or potential rivals from expanding within, or entering into,

a market. Exclusionary acts are covered in sections 8(c) and (d) of the Act. The Commission's enforcement actions and Tribunal's decisions are examined in light of these specified legislative provisions.

It is important to recall that the regulation of dominant firms extends beyond the Act's sections 8(c) and (d) provisions on exclusionary acts. While dominant firm's exploitative acts (such as excessive prices, covered in section 8(a) of the Act) directly harm consumers, exclusionary acts are indirectly harmful to consumers through their impact on the competitive structure (Gormsen, 2005). Exclusionary acts are geared towards enhancement of a firm's dominant market position, and can therefore lead to the creation or maintenance of monopolies. It is for this reason that the regulation of exclusionary acts was chosen as the focus of this research.

CHAPTER 2: THEORETICAL BASIS AND LITERATURE REVIEW

2.1 International Competition Policy on Dominant Firms

Protecting competition from distortion is achieved in different ways. In the United States of America (“US”), the antitrust laws ultimately seek to promote consumer welfare, while in Europe, protecting competition has been interpreted to mean protecting the economic freedom of market players (Gormsen, 2005). It has been argued that in the US, actions (based on competitive merits) of a dominant firm in increasing its market share may be more helpful than hurtful to consumers, and the consumer is therefore best protected by respecting the freedom of action of the dominant firm (Fox, 1986). European Union (“EU”) law arguably presumes the actions of a dominant firm with exclusionary tendencies to be against consumer interest (Fox, 1986). The difference between the US and EU where exclusionary conduct is concerned, though important, is more one of degree than substance. The US is more inclined to allow considerable latitude to dominant firms, although US law and enforcement practice does still proscribe exclusionary conduct.

There are opposing views over the role of competition law. In the US, the structure – conduct – performance paradigm of the Harvard School states that the structure of the market determines a firm’s conduct, and that conduct determines the market’s performance (Messina, 2005). Accordingly, it was felt that antitrust law should be concerned with structural, rather than behavioural, remedies – leading to an interventionist antitrust enforcement policy in the US in the 1960s (Messina,

2005). The Chicago School has no sentimentality for small business and considers the role of antitrust as the pursuit of efficiency, and trusts that the market is able to correct and achieve efficiency without interference from government and antitrust laws (Messina, 2005; Kovacic & Shapiro, 2000; Posner, 1974). It is argued that where antitrust policy is effectively implemented, direct regulatory intervention is unnecessary as competitive market forces drive efficiency (Hemphill, 2004).

Fox (1986) compares antitrust provisions in the US and in Europe. Section 2 of the US Sherman Act uses general language to declare it a felony to monopolise, to combine or conspire to monopolise, or to attempt to monopolise (Fox, 1986; Areeda, 1987). Fox (1986) described the then article 86 of the Treaty of Rome (now article 102) as more specifically spelling out examples of abuse of a dominant position, namely: imposing unfair prices, limiting production, applying dissimilar provisions to equivalent transactions and unrelated tying. Fox (1986) argues that the power to raise price and limit output is the core economic evil which antitrust is designed to deter. While this is the position in Europe, there is no similar provision in US law where it is not illegal for a firm acting unilaterally to restrict its output and charge monopoly prices (Fox, 1986). European antitrust law, and not US law, thus envisions a role for government in regulating firm performance (Fox, 1986).

European cases show that conduct that hinders the production of competitors constitutes abuse (Gormsen, 2005). The European Court of Justice's (ECJ)

decision in the 1973 case of *Commercial Solvents v Commission* shows that the court was concerned about harm to a competitor (Gormsen, 2005). In the 1977 German *Kombinationstarif* case, it was stated that an abuse could be presumed if the conduct of the dominant firm “is not within the boundaries of competition on the merits and if the market structure is further worsened by the undertaking profoundly restricting or even eliminating the competition remaining on the market” (Gormsen, 2005, p. 17). In the 1976 case of *Hoffmann-La Roche v Commission*, the ECJ stated that the concept of abuse was objective and related to whether the dominant firm’s behaviour “...is such as to influence the structure of the market where, as a result of the very presence of the undertaking in question, the degree of competition is weakened ...” (Gormsen, 2005, p.18).

While the earlier European cases focused on the market structure, later cases focused on possible effects of dominant firms’ conduct (Gormsen, 2005). In the 1981 and 2001 *Michelin v Commission* cases, it was stated that to establish an infringement of competition law, it was enough to show that the dominant firm’s conduct tends to restrict competition or is capable of having that effect, not necessarily related to the actual effect (Gormsen, 2005). In the 1999 case of *British Airways v Commission*, it was found that British Airways’ rewards scheme was likely to have a restrictive effect on competition, notwithstanding British Airways’ assertion of its declining market share, noting further that competitors’ market shares would have grown more significantly in the absence of the anti-competitive practice (Gormsen, 2005).

In Europe, Vickers (2005) argues that based on the then article 82 of the EC Treaty (now article 102), conduct by dominant firms can be abusive, even if it does not maintain or strengthen market power (Vickers, 2005). This differs from US antitrust law, where there needs to be a causal link from the conduct to the market power (Vickers, 2005). Market power refers to a firm's ability to raise prices above the competitive level, without a significant loss in sales that renders the price increase unprofitable (Landes & Posner, 1981; Pitofsky, 1990); and to restrict output (Krattenmaker & Salop, 1986).

In the US, from 1940s to 1970s, antitrust doctrine was intervention-minded. Over the past 30 years, the trend has been to give dominant firms greater freedom to select pricing, product development and distribution strategies that improve consumer welfare (Kovacic, 2007).

Klein (2001) argues that a dominant firm should only be prevented from abusing its market power in a way that places its rivals at a significant competitive disadvantage, without any reasonable business justification. This argument is in line with the above trend observed by Kovacic (2007), and Fox's (1986) view that US antitrust law concentrates on preserving conditions where free market forces constrain price and induce optimal production.

Vickers (2005) argues that saying conduct is exclusionary if it does not make business sense but for distorting competition, requires independent specification of what is substantively exclusionary.

Vickers (2005) states that European case law has established the following general principles on abuse of dominance:

- A dominant firm has a special responsibility to ensure that its conduct does not distort competition.
- A dominant firm may not eliminate a competitor or strengthen its dominant position by means other than 'competition on the merits'.
- Abuse involves recourse to methods other than those considered normal competition.
- The concept of abuse is objective and does not require anti-competitive intent (though evidence on intent can be relevant in finding abuse).

2.2 Role of Competition Law

2.2.1 Consumer Welfare

In the US, the guiding economic principle in deciding whether behaviour by a dominant firm involves "competition on the merits" is whether such behaviour benefits consumers (or produces efficiencies) (Klein, 2001). While Vickers (2005) mentions a distinction between exclusionary and directly exploitative abuses of market power; Fox (2002) queries whether there is an exclusionary practices violation that does not lead to the exploitation of consumers. It is argued that the

point of competition policy is to serve the needs of the general public of consumers, not some abstract notion of competition for its own sake (Vickers, 2005). However, protection of the competitive process is indeed likely to promote incentives to compete and to therefore serve both consumers and progressive market players, whose interests are arguably symbiotic (Fox, 2003).

It is argued that the purpose of competition law policy can be reduced to one economic objective, the maximisation of consumer surplus (Simkins, 2005). Gormsen (2005) argues that keeping competition law's concern with protection of a competitor can benefit consumer welfare (allocative efficiency) in the short run (if it increases choice), but in the long run, it can reduce productive efficiency as other competitors would have less incentive to innovate. Allocative efficiency occurs where price equals marginal cost and consumer welfare is maximised, while productive efficiency is the ratio of a firm's output and input – a higher ratio indicates a more efficient firm (Unterhalter, 2005). Brassey (2005) refers to protection of competition as a means of promoting economic efficiency, as opposed to merely protecting rivalry.

Enforcement of abuse of dominance provisions can ensure that consumers are not deprived of choice through a dominant firm's anti-competitive conduct (Messina, 2005). Consumers benefit from competition through lower prices, better quality and a wider choice of goods and services (Commission of the European Communities, 2009).

2.2.2 Protect Competition or Competitors?

There are debates on whether the approach to dominant firm conduct is intended for 'protecting competition' or for 'protecting competitors' (Gormsen, 2005). Fox (2003) argues that competition law protects competition and consumers, and not competitors. Economic commentators propose that this debate can be avoided by adopting an economic-based approach that carefully considers how competition works in each particular market, in order to evaluate how specific company strategies affect consumer welfare (Gormsen, 2005).

Klein (2001) argues that detrimental effects to competitors are not enough to support a conclusion that a dominant firm's conduct is anti-competitive. This is because successful competitive actions that benefit consumers can negatively affect competitors (Klein, 2001).

Vickers (2005) proposes an 'as-efficient' competitor test for determining which rivals' exclusion should be prevented. It is argued that when competition is effective, more competitive firms gain at the expense of less competitive firms, therefore only those rivals that are no less efficient than the dominant firm should be protected (Vickers, 2005; Hovenkamp, 2005). This test would ensure that competition is protected, as distinct from protecting competitors (Vickers, 2005).

Fox (2003) considers categories of harm to competition: action that undermines the market mechanism (openness and access to markets on the merits); and, harm

from competition – low prices and other dominant firm strategies that directly benefit consumers. Fox (2003) concludes that conduct which does not lead to a reduction in output or an increase in price is efficient, and therefore any antitrust action against it protects competitors.

As discussed above, US antitrust jurisprudence moved from proscribing conduct that harmed the competitive process, to a rule of non-intervention unless the conduct artificially reduced output and raised prices (Fox, 2003). It was assumed that markets and businesses were efficient, and thus efficient competitors could manoeuvre around any restraint (Fox, 2002). In the US, there is great reliance on the output (reduction) test, due to fear that any other test would result in the protection of competitors at the expense of consumers (Fox, 2002).

The case of *Verizon v Trinko* illustrates the US perspective of non-intervention against dominant firms (Fox, 2007). In this case, Verizon, an incumbent local telephone service provider, used its ownership of elements of the local telephone loop to gain advantage over new competitors (Fox, 2007). The court held that the use by a dominant firm of leverage to gain advantages in the local telephone market was not an antitrust violation (Fox, 2007).

The EU's competition laws protect openness and access to markets, and "the right of market actors not to be fenced out by dominant firms strategies not based on competitive merits" (Fox, 2003, p. 7). Preserving this freedom of non-dominant

firms to trade without artificial obstacles constructed by dominant firms is important to the legitimacy of the competition process (Fox, 2002). Fox (2003) argues that article 82 (now article 102) was intended to regulate dominant firms' conduct and to prevent them from unfairly using their power. Indeed, in the 1983 decision in *Michelin v Commission*, the Court of Justice stated that a dominant firm had a special responsibility not to allow its conduct to impair undistorted competition (Fox, 2003). It can be argued that markets are more likely to reward merit if not clogged by substantial unjustified exclusions (Fox, 2002). Furthermore, it is preferable to rely on the competitive process, rather than the strategies of dominant firms (Fox, 2002).

Fox (2003) concludes that jurisdictions should decide, based on their history, culture and context, whether competition law should only protect against output limiting outcomes or ensure open markets and freedom of access on the merits. On the one hand, mature market jurisdictions consider an unfair competition component of competition policy an anathema to policy makers (Fox, 2002). On the other hand, developing countries may not want *Trinko* law (Fox, 2007). Instead they may choose to protect small or indigenous competitors from monopolisation (and unfair competition) by big players in already distorted (through import restrictions) domestic markets (Fox, 2003). This results in competition law playing the dual role of raising the power of underprivileged firms and of establishing the rules of fair and free competition (Fox, 2003).

2.3 The Concept of Dominance in South Africa

South African competition law is clear that a finding of abuse of dominance first requires an establishment of dominance by the firm as defined in the Act (Lewis, 2008). Section 7 of the Act lays down the requirements for the establishment of dominance. Firms with market shares beyond 45% are presumed to be dominant (Lewis, 2008), while those with market shares between 35% and 45% will be presumed to be dominant unless they can show that they lack market power. Those firms with market shares below 35% are presumed to not be dominant, unless they have market power. Thus, for firms with market shares beyond 45%, there is an irrebuttable presumption of dominance, while for firms with market shares between 35% and 45% there is a rebuttable presumption of dominance. For firms with market shares below 35%, there is a rebuttable presumption of a lack of dominance.

Section 1 of the Act defines market power as “the power of a firm to control prices, to exclude competition or to behave to an appreciable extent independently of its competitors, customers or suppliers”. While 45% of a market is not a large enough market share to indicate the existence of market power, the presumption of dominance closes from scrutiny the question of whether a firm in fact enjoys market power. It is argued that presumption of a firm’s dominant position by recourse to market share alone is too crude an approach, and has the danger of being over-inclusive (Unterhalter, 2005; Elhauge, 2003).

2.4 Chilling Competition?

The line between conduct that has pro-competitive effects or anti-competitive effects is most blurred in the unilateral actions of dominant firms (Lewis, 2008). There is controversy on how competition law should deal with anti-competitive behaviour of dominant firms (Vickers, 2005). While lax policy would jeopardise competitiveness of markets, rigid policy would chill pro-competitive (and pro-consumer) conduct (Vickers, 2005; Evans & Padilla, 2005).

There is fear that erroneous enforcement of competition law's provisions on dominant firms may lead businesses to forego pro-competitive conduct, for fear that such conduct may be erroneously found to be anti-competitive (Lewis, 2008). It is argued that the application of legal rules in enforcement decision-making leads to 'over-enforcement', as opposed to the application of economic standards and evaluation of economic effects on a case-by-case basis (Lewis, 2008). Enforcement agencies in some jurisdictions propose that an effects-based approach would serve as a check to inappropriate interventions, as there would first be a need to establish that the alleged abuse has resulted, or is likely to result, in consumer harm (International Competition Network, 2007; Theron, 2009).

Lewis (2008) argues that in South Africa, and in economies with similar historical and structural features, 'over-enforcement' has not occurred, and 'under-enforcement' is a more likely outcome of enforcement action, where anti-competitive conduct of dominant firms is erroneously permitted. In addition, South

African competition law adopts an approach that interfaces legal rules and economic standards, providing greater deterrence, certainty and ease of administration than an approach based on legal standards alone (Lewis, 2008).

2.5 Conclusion

In view of the different approaches to dominant firm conduct pursued across various jurisdictions, there is need to examine what approach the South African competition authorities have taken. This examination should assist dominant firms to assess when their conduct would be found to be exclusionary and anti-competitive; and whether the competition authorities' approach may hinder their competitiveness.

CHAPTER 3: RESEARCH QUESTIONS

This research seeks to answer two key questions.

Research Question 1

When are competitive actions and conduct of a dominant firm categorised as exclusionary, and thus anti-competitive?

A dominant firm's actions can either be pro-competitive, and thus conduct which competition law is designed to protect; or, anti-competitive and therefore prohibited. As has been discussed, competitive actions are by nature designed to obtain certain advantages to the exclusion of competitors. How then can a dominant firm be able to distinguish between allowable competitive conduct and prohibited abusive conduct? Are there any key principles that are emerging from competition law practice and decided cases that can provide some guidelines to dominant firms on whether planned action is prohibited conduct?

Research Question 2

Are the enforcement actions of the Commission and the decisions of the Tribunal arising from Sections 8(c) and (d) of the Act likely to cause dominant firms to eschew robust pro-competitive conduct for fear of erroneous or overly-zealous prosecution?

This question seeks to elucidate how the South African competition authorities have interpreted the Act's provisions on exclusionary acts. The principle purpose of any competition law is to promote competition. In South Africa, has the enforcement of competition law led to the chilling of competition?

CHAPTER 4: RESEARCH METHODOLOGY

4.1 Research design

The research design was mainly qualitative and exploratory in nature, with a minor quantitative component. The exploratory research method was used to diagnose what was happening in practice (Zikmund, 2003).

The qualitative research was conducted using two methods. The first exploratory research method was experience surveys (Zikmund, 2003). Seven competition law experts were selected for personal interviews, based on their extensive experience and expertise in the area of competition law or economics.

The researcher approached each of the identified experts via email and requested for a confidential face-to-face personal interview of 30 minutes to one hour duration. All the seven experts agreed to an interview and suitable dates and time were scheduled. There was need to approach the experts early as their availability could be restricted by involvement in tribunal hearings. Indeed, as a result of the experts' varying work schedules, the seven interviews were conducted over a period of two months. Each interview lasted an average of 45 minutes, and was held at the expert's office. The researcher chose not to record the interviews to ensure that the experts were assured that confidentiality would be maintained. The lack of a voice recorder enabled the experts to speak more freely. However, the researcher took notes of the verbatim responses during the interviews.

A list of questions (see Appendix 1) was posed to each of the experts. The questions were designed to indicate whether South African legislation and jurisprudence cause respondents to err on the side of conservatism when providing competition law advice to dominant firms. The questions were broken down into several components to try and fully solicit the experts' views on the approach taken by the South African competition authorities. The interview questions were also designed to uncover the main abuse of dominance cases, and the experts' assessments of these cases.

As experience surveys attempt to describe what is happening (Zikmund, 2003), this research method was appropriate. It enabled the researcher to describe whether uncertainty in enforcement decisions may have led dominant firms to avoid pro-competitive actions due to fear that such actions could be found to be anti-competitive (Lewis, 2008).

During the two-month interview period, the results of each of the seven interviews were collated per interview question. Upon finalisation of the interviews, the interview results were then grouped per research question. Common themes were then extracted and analysed.

The second exploratory method was scrutinizing decided cases (Zikmund, 2003). The case study method was also appropriate for the research problem. Selected

key decisions of the Tribunal were examined to discover how the Act's relevant abuse of dominance provisions had been interpreted, and whether there were any emerging principles that could be applied by dominant firms when reviewing their competitive strategies.

The researcher was influenced by the experts in the selection of the key cases. During the interviews, each expert identified the cases they considered key in the area of abuse of dominance. In addition to this, the researcher reviewed the entire population of decisions published on the Tribunal's website and identified all the abuse of dominance cases that dealt with the Act's sections 8(c) and (d). Six of these decisions were then selected as the most relevant and these were studied in-depth, with a view to answering the first research question – on when dominant firms' conduct would be found to be exclusionary and anti-competitive.

Some of the Tribunal decisions were very lengthy, extending to between 80 and 100 pages. All the key facts and issues in the Tribunal decisions were summarised (included in Appendix 2). The length of the summaries ranged from three to five pages. The duration of the cases' investigations and hearings was also examined to illustrate the difficulties involved in prosecuting abuse of dominance cases.

Where the Tribunal's decision was considered on appeal by the Competition Appeal Court, the subsequent decisions were also examined. These decisions

were also obtained from the Tribunal's website. The outcomes of the appeals are included in the relevant Tribunal decisions' summaries.

The quantitative research was descriptive in nature. The unit of analysis for the quantitative research was a single referral by the Commission to the Tribunal on the Act's sections 8(c) and (d) prohibitions. The research identified the number of sections 8(c) and (d) referrals, and the total referrals on the entire Chapter 2 of the Act (all anti-competitive agreements and unilateral restrictive practices) made by the Commission between 2002 and 2009. This research method was intended to describe whether the Commission's enforcement actions were over-zealous.

4.2 Population

The population for the qualitative experience surveys was competition law and economics experts in South Africa who have been involved in the area of abuse of dominance in the last ten years.

The population for the qualitative exploratory case studies was the decisions of the Tribunal on the Act's sections 8(c) and (d) abuse of dominance provisions in the last ten years.

The population for the quantitative descriptive research was the Commission's referrals on the Act's sections 8(c) and (d) abuse of dominance provisions in the period 2002 to 2009.

The information on the experience surveys was sourced from personal interviews, while that on the enforcement actions and decisions was sourced from the Commission and Tribunal websites.

4.3 Sampling

For the qualitative research, judgement samples were used for both the experience surveys and case studies. A judgement sample is a non-probability sampling technique in which an experienced individual selects the sample based on his judgement of some characteristics required of the sample members (Zikmund, 2003).

For the experience surveys, a list of several experts was obtained from a highly experienced individual, with more than 15 years interaction with leading competition law and economics experts in South Africa. Where two or more experts worked in the same firm, the most senior partner or director was selected. The reason why only one expert per firm was selected was to ensure that the researcher obtained divergent views. From the list, seven experts were selected, all of whom were actively involved in competition law or its enforcement in South Africa.

For the qualitative exploratory case studies, a judgement sample of the most important decisions was selected based on relevance to the study and the experts' views on which were the prominent abuse of dominance cases.

For the quantitative descriptive research, the entire population of the Commission's referrals in the last ten years was reviewed.

4.4 Limitation of the Research

- The scope of the research was limited to abuse of dominance provisions on exclusionary acts, covered in sections 8 (c) and (d) of the Act.
- The research did not consider the abuse of dominance provisions in sections 8 (a) and (b) of the Act that deal with excessive pricing and provision of essential facilities.
- The research did not consider the abuse of dominance provisions in section 9 of the Act that deal with price discrimination.
- The research did not consider decisions made by the Tribunal in respect of other provisions of the Act.
- Qualitative research is subjective in nature and conclusions drawn may be subject to considerable interviewee and interpreter bias (Zikmund, 2003). Interviewee bias was particularly likely where individuals were personally involved in the cases discussed. Bias was also likely where, as mentioned by one interviewee, individuals may be tempted to exaggerate their responses so as to promote their advisory roles.
- There were few relevant cases, and they did not address similar facts. Thus the decisions are of limited general application.
- Although the Competition Tribunal is guided by its previous decisions, it is not bound by them. This limits the Tribunal's cases precedential authority. As a result, there is no certainty that even when faced with substantially similar facts, the Tribunal would make a similar decision. This limits the benefits of the research.

- While the interviewees had significant expertise in competition law, as outsiders, they could not be certain whether in practice, dominant firms have tempered their competitive actions.
- The choice of experts was determined by a judgement sample, which is subjective in nature.
- Abuse of dominance cases are very fact and industry specific, with outcomes varying widely depending on circumstances of each case. Therefore, it is difficult to establish general principles.

CHAPTER 5: RESULTS

5.1 Introduction

A sample of seven competition law experts was interviewed. The responses received have been presented below based on both research questions. Some emergent themes which were not part of the research questions have also been presented.

Six cases were examined and their summaries (numbered from Case 1 to 6) are included in Appendix 2. These were the key abuse of dominance cases that dealt with exclusionary acts. All the six cases studied dealt with section 8(c) of the Act. Three of the cases dealt with both sections 8(c) and 8(d)(i), while one case dealt with both sections 8(c) and 8(d)(ii). The results of the case studies have been presented in answer to research question 1.

5.2 Research Question 1

When are competitive actions and conduct of a dominant firm categorised as exclusionary, and thus anti-competitive?

5.2.1 Interview Results

Two of the seven respondents felt that the first step in examining whether conduct is exclusionary and anti-competitive is to ascertain whether the firm is indeed dominant. *“In practice, firms do not know that they are dominant, as this requires an analysis of the market.”* While some firms may accept that they are dominant, other firms have multiple products in multiple markets, and the extent of their dominance is open to question. Once past this hurdle and the answer is in the affirmative, the next step is analysis of the conduct and its potential effects.

Two respondents stated that it is important to consider whether the conduct falls within the scope of the wording of section 8(c) or (d) of the Act, as if it does not, then it is not exclusionary.

One respondent felt that it was important to examine the reasons why the firm was engaging in the conduct. *“The rule of thumb should be that if the principle reason for engaging in the conduct is pro-competitive benefits, other than impact on competitors and consumers, then the conduct can be defended.”*

Five of the seven respondents stated that an analysis of the effects on competitors or consumers was critical. It is important to consider whether the dominant firm has entered into arrangements that may exclude other firms, and must specifically assess whether:

- distribution and supply agreements are exclusive and of long duration,
- marketing and sales practices are exclusionary, or
- discounts and rebates policies amount to unlawful inducement.

According to one of these five respondents, a simple question to ask is *“does the conduct have an adverse effect on pricing or competitors?”*

Three of the seven respondents felt that it was important to assess the impact of the conduct on competition in the market. *“Is there substantial commercial benefit with little impact on consumers (negative or positive)? Will it only impact one of their competitors or all of them? If the conduct does not raise barriers to entry, and all competitors are able to compete, then it would not be anti-competitive. In CC v Senwes (Case 4), the dominant firm’s conduct made it more difficult for new entrants. Therefore, long-term, the conduct would shelter the dominant firm.”*

One respondent explained that in reviewing a firm’s conduct, there is need for an assessment of the competitive landscape; competitors’ sizes, what alternatives are available apart from the dominant firm, and whether there is an effect on competition itself. He further stated that *“this requires you to get into the real facts of the industry. Is the complainant’s competitiveness reduced to a material effect?”*

The real test is the effect on consumers and foreclosure. Does the conduct cause the complainant to stop trading, or does it just make its business more difficult? There is need for analysis and interrogation of the business to get objective facts on the conduct.”

One of the seven respondents highlighted that even if effects are exclusionary, it is important to consider whether there are efficiency justifications in those section 8 provisions which are subject to a rule of reason analysis. He stated that the two SAA cases (Case 1 and 2) and *CC and JTI v BATSA* (Case 3) make clear that the Commission will only succeed in an abuse of dominance case if it can clearly show anti-competitive effects beyond hypothetical effects. *“The BATSA case significantly raised the bar for a successful prosecution of an abuse of dominance case. After BATSA, dominant firms feel they have more flexibility than before. While some actions of BATSA appeared to be open to question, the Tribunal said that in reality you could get any cigarette on the display unit.”*

5.2.2 Case Studies

The case studies provide insight into when a dominant firm’s conduct would be found to be exclusionary and anti-competitive. (See summaries in Appendix 2.)

Dominance

A firm will only be found to have abused its dominance if such firm is, first and foremost, dominant as set out in the Act. In five out of the six cases studied, the

respondent firms were found to be presumptively dominant, with market shares well in excess of 45%. BATSA had 96% of the total sales of manufactured cigarettes in South Africa, while Senwes had over 80% market share for grain storage in the relevant geographical region. Senwes was however not dominant in the downstream grain trading market. This illustrates that it is not necessary for a firm to be dominant in the market where the effects are felt, so long as it is dominant in a related market.

Abuse

In Case 1 (*CC (Nationwide) v SAA*), the Tribunal explained that the Act requires an examination of the conduct complained of to determine whether it falls under the section 8(d) list, or that it meets the Act's definition of "exclusionary act" and thus falls under section 8(c). The next step is to enquire whether the exclusionary act has an anti-competitive effect. An exclusionary act is conduct other than competition on the merits which impedes or prevents the growth of rivals in the market. Such acts can lead to the creation or enhancement of a dominant firm's ability to exercise market power.

Critically, the Tribunal explained that an exclusionary act has an anti-competitive effect if there is evidence of actual harm to consumer welfare, or the exclusionary act is significant in terms of foreclosing the market to rivals. The Tribunal explained that a requirement to also prove consumer harm is unnecessary and would be under-deterrent. A finding of an exclusionary act alone is also not

sufficient as it would outlaw competitive non-predatory behaviour, and be over-deterrent. This explanation is key to understanding the Tribunal's approach to exclusionary acts.

SAA's override incentive and trust agreements (see Case 1 and 2) induced travel agents to deal with SAA at the expense of its rivals and had therefore foreclosed the rivals in the market for scheduled domestic airline travel. (See further discussion on 'foreclosure' in the case summaries, Appendix 2). SAA's amended incentive schemes in Case 2 (*Nationwide and Comair v SAA*) had an even greater exclusionary effect as travel agents' targets had become increasingly more difficult to meet. Travel agents were thus put under immense pressure to achieve their targets at the expense of SAA's competitors. The trust payments were lump sum payments made to travel agents for achieving specific targets, and particularly in the case of large travel agents, for maintaining revenue targets of the previous year. By concluding the agreements with travel agents, SAA had sought to extend or maintain its dominance through aggressive override incentives, rather than engaging in competition on the merits.

In Case 2, the Tribunal explained that Section 8(d) acts are not presumed as having anti-competitive effects. There was a two-stage enquiry, as had been explained in Case 1 – whether travel agents were incentivised to move customers away from rivals, and, whether they had the ability to do so. While internet and direct sales channels had been developing, travel agents remained the most

significant sales channel, distributing approximately 70% of the total domestic airline market. SAA had concluded agreements with approximately 70-90% of the market, which suggested that the foreclosure effect was potentially substantial. Asymmetry of information between travel agents and customers prevailed during the relevant period, and customers continued to rely on the agents' expertise and advice. Travel agents therefore had both the financial incentives and the ability to influence their customers' preferences, to the detriment of SAA's competitors. The Tribunal concluded that the SAA incentives foreclosed rivals and had a significant anti-competitive effect on both Nationwide and Comair.

On the issue of consumer harm, the Tribunal stated in Case 2 that although there was no evidence of consumer harm, it could be inferred that the SAA incentives, coupled with travel agents' ability to influence consumers' preferences, harmed consumers through higher prices or reduced choice. This inference could be made as a result of the significant foreclosure (discussed above).

CC v Senwes (Case 4) is a good illustration of a firm's attempt to leverage its market power from one market to an adjacent market. Senwes had raised its rivals' costs, with the effect that traders would be foreclosed. (See Case 4 discussion on 'raising rivals costs' and 'margin squeeze' in Appendix 2). A margin squeeze occurs when a vertically integrated dominant firm sets its wholesale price to its downstream rivals and its retail price, such that the margin between them is unduly low (Vickers, 2005).

The Tribunal explained that the relevant conditions for the existence of a margin squeeze were: the dominant firm supplied an input to downstream rivals; the input was essential for the rivals to compete; and, the input formed a substantial part of the rivals' fixed expenditure. It was then important to test whether the dominant firm's downstream operation could trade profitably on the upstream price charged to its rivals. An alternative test was whether the margin between the dominant firm's upstream price and the price that the downstream firm charges, would allow a reasonably efficient firm to obtain a normal profit. From the evidence, Senwes' storage pricing rendered an equally efficient trading rival uncompetitive, and therefore amounted to an exclusionary act that impeded or prevented rival traders from competing with its downstream trading division.

In *CC and JTI v BATSA* (Case 3), the Tribunal could not identify any harm to consumers or find significant foreclosure of rival manufacturers as a result of BATSA's conduct. The Tribunal identified 11 reasons (see details in Appendix 2) to support this finding. The Tribunal clearly stated that aggressive pursuit or defence of market shares by dominant firms is not necessarily anti-competitive. This decision confirms that dominant firms are entitled to remain competitive, notwithstanding the unique burdens placed on them by the Act.

In *Mandla-Matla v Independent Newspapers* (Case 5), it was alleged that Independent Newspaper had foreclosed Mandla-Matla from the market.

However, the fact that a competing distribution network was set up in two months for Mandla-Matla's newspaper, demonstrated that the duration of the alleged foreclosure was minimal. This case reiterated the position in *CC (Nationwide) v SAA* (Case 1), that sections 8(c) and 8(d) of the Act require that both the exclusionary act and its alleged anti-competitive effect must be proved. There was no evidence that either Mandla-Matla or competition itself suffered as a result of Independent Newspaper's conduct.

York Timbers v SAFCOL (Case 6) demonstrates that the act complained of must be exclusionary, as provided in the Act. Although a reduction in supply can amount to a refusal to supply, the Tribunal found that SAFCOL had merely reduced the guaranteed volume of saw logs. (Section 8(d)(ii) prohibits dominant firms from refusing to supply scarce goods to a competitor when supplying those goods is economically feasible.) York Timbers was able to compete for supply of logs with other sawmills at the prevailing market price. As there was no evidence that York Timbers had failed to procure logs on the amended terms, the dispute was contractual in nature. Critically, SAFCOL's conduct did not extend or create its market power in the downstream sawmilling market and was therefore not anti-competitive.

Pro-competitive justification

In both *CC and JTI v BATSA* (Case 3) and *Mandla-Matla v Independent Newspapers* (Case 5), the Tribunal stated that the conduct complained of led to pro-competitive outcomes.

BATSA's incentive payments to vending machine operators led to growth of that distribution mechanism, which was a pro-competitive gain. Also, as category captain (see discussion in Appendix 2 on category management), BATSA did a lot of work to ensure orderly displays of all cigarette categories, including those of rival manufacturers. It also provided free display units to the benefit of itself, its rivals and retailers. Indirectly, consumers benefitted from these free benefits to retailers. It was also more efficient for a manufacturer to organise the displays because retailers found it difficult to understand the detailed aspects of thousands of categories.

In Case 5, Independent Newspapers' conduct had indirectly led to significant improvement of the competitive structure of three markets, namely, the market for newspaper printing, distribution and publishing. There was a ten-fold increase in printing capacity; growth in the market for Zulu newspapers; and, development of a parallel distribution network which intensified rivalry in the distribution market. The Tribunal pointed out that these were all pro-competitive outcomes.

On the contrary, the Tribunal found that SAA's incentive schemes and trust payments to travel agents had no real efficiencies in ticket distribution, nor that the efficiencies outweighed the foreclosing effects. These agreements were instead designed to promote loyalty to the dominant carrier, to the exclusion of its rivals (Case 1 and 2). Senwes also failed to establish any efficiency or other pro-competitive defence for its conduct (Case 4).

Finding

In three cases, the Tribunal found that the respondent firms had abused their dominance, while in the remaining three cases, no abuse was found.

The Tribunal found that SAA's override incentive and trust agreements (and payments) required or induced customers not to deal with a competitor and therefore contravened section 8(d)(i) of the Act. It was the nature of the schemes, and not their existence, that was abusive. By lowering the standard commission and increasing the override and incentive commissions, SAA had materially altered travel agents' incentives, leading to the anti-competitive nature of the scheme (see further discussion in Case 1, Appendix 2).

The Tribunal also found that Senwes' (Case 4) conduct amounted to a margin squeeze which contravened section 8(c) of the Act. The conduct had a substantial anti-competitive effect that foreclosed rival traders from the market in the relevant period. This finding was confirmed by the Competition Appeal Court, which added that if Senwes' trading division had incurred similar storage costs, it could not have operated profitably at its pricing levels.

On the contrary, the Tribunal found that no anti-competitive effects were established in *CC and JTI v BATSA* (Case 3). In this case, the Tribunal re-iterated that competition law is concerned with ensuring that there is robust competition. Interestingly, the Tribunal noted that BATSA was not obliged to provide any free

service to its smaller rivals, and the firm's failure to comply with pure category management principles (as explained in Appendix 2) was a predictable outcome for a profit maximising dominant firm.

Similarly, the Tribunal found that Mandla-Matla (Case 5) had failed to establish an anti-competitive effect. In *York Timbers v SAFCOL* (Case 6), the Tribunal (and the Competition Appeal Court) found that SAFCOL's reduction of guaranteed supply of logs was not an exclusionary act, but a contractual dispute that was of no concern to competition law.

5.2.3 Assessments of cases

The respondents' assessments of the key cases varied. Two out of seven respondents felt that the decision in *CC (Nationwide) v SAA* (Case 1) was good, while one respondent felt that it was a bad decision. One respondent was of the view that the decision in *Nationwide and Comair v SAA* (Case 2) was good, while another respondent said that it was bad. On *CC and JTI v BATSA* (Case 3), two respondents stated that it was a good decision, while two respondents stated that it was a bad decision which raised the bar for proving abuse of dominance.

One respondent stated that there was no basis for distinguishing *CC (Nationwide) v SAA* (Case 1) from *CC and JTI v BATSA* (Case 3). *“In CC and JTI v BATSA, the Tribunal recognised that BATSA had developed a national strategy to exclude its competitors and had spent money implementing its strategy over a period of years. No commercially rational firm would engage in this over an extended period. Despite this, the Tribunal focussed on the fact that BAT was overwhelmingly dominant (94% of the market). The Tribunal focussed on market share, rather than BAT’s engagement in exclusionary conduct, and was not prepared to take the CC (Nationwide) v SAA view that it must have had an effect, rather than expecting demonstration of effects.”*

One respondent stated that *CC v Senwes* (Case 4) was very factually specific. As it related to ‘margin squeeze’ (see discussion in Appendix 2), it must be looked at by dominant firms when assessing how to treat competitors operating in one of the

layers of a supply chain. There however remained an unresolved issue on distribution. *“If you choose to go through direct distribution, are you obliged to consider services offered by an intermediary because under CC v Senwes it can be regarded as a margin squeeze if you do not allow someone to distribute your products? In CC v Senwes intermediaries already had a role. Does this apply to cases where someone wants to be an intermediary and do they have a right to be an intermediary?”*

One respondent observed that following *Mandla-Matla Publishing v Independent Newspapers* (Case 5), if a market is growing as a result of conduct, it is very difficult to find the conduct anti-competitive.

Four respondents felt that there were consistent principles emerging from the Tribunal decisions, while the remaining three respondents stated there were none. Two respondents felt that there were too few abuse of dominance cases, and the existing cases were very fact intensive. Below are verbatim comments made by the respondents in their assessment of the key abuse of dominance cases:

- *“The two SAA cases (CC (Nationwide) v SAA (Case 1) and Nationwide and Comair v SAA (Case 2)) were incorrectly decided and took very logical leaps to get to their decisions. CC and JTI v BATSA (Case 3) was favourable for business, but very confusing. There is no clear guidance on*

why the principle of merchandising is working. There is no logical coherence or precedential value.”

- *“We have not seen enough decisions to start building a precedent of cases. On the facts, each case may have reached the correct outcome, but it remains unclear how they got there.”*
- *“It is difficult for dominant firms to determine what test would apply.”*
- *“The cases have been very disappointing in precedent setting value.”*
- *“The cases are not on the same sections.”*
- *“There are inconsistencies from the Tribunal, which impact advisors’ ability to make clear assessment of the risk, and therefore lead to conservatism.”*
- *“The reason for the lack of clear principles is not inconsistency, but rather fundamentally because the cases deal with different principles and are severely fact intensive.”*
- *“There is no level of maturity in our law. It is too early. There is however consistency, as effects based standards are applied, based on the facts, the analysis and case specificity. With effects base, you can get more to the details and the decisions have been very thorough.”*

Three out of seven respondents saw that an effects-based approach was being consistently applied. On the issue of effects, these three respondents stated that one had to look not merely at hypothetical or intermediary effects, but the actual effects on prices to consumers, and impacts on customers or consumers.

One respondent explained that two themes were clearly emerging:

- Protection of competition and not competitors; and
- Abuse of dominance must have an anti-competitive effect in order to be unlawful.

An emerging theme was that the Commission and Tribunal should do more in establishing clear guidelines that could guide dominant firms, as evidenced by the following verbatim comments:

- *“We would like to see the Tribunal refer explicitly to previous decisions and specify why it is taking a different approach.”*
- *“It is admitted that in competition law it is difficult to lay down definitive principles. But there is an absence of clear principles.”*
- *“The Tribunal should take all the existing cases and try and explain the principles emerging.”*
- *“It would help if the Commission set guidelines, and the Tribunal stated the general rules even though a case was fact intensive.”*

5.2.4 Research Question 1: Conclusion

A key observation that was made by the interviewed competition experts was that there had been too few cases on exclusionary acts. Furthermore, abuse of dominance cases were very fact intensive and the cases did not deal with the same sections of the Act. These factors limited the cases' precedential value. As such, it was still too early to identify a clear pattern of principles that could be of general application.

5.3.1 Research Question 2

Has there been a chilling effect from the prosecutorial approach of the Commission and the Tribunal's decisions on sections 8(c) and (d)?

Only one of the seven respondents stated that there had definitely been a chilling effect, while five of the respondents stated that there had been no chilling effects. This one respondent stated that he advised his clients to factor competition law risk as a business risk, and often told them *“you cannot afford not to be aggressive.”*

One of the five respondents who felt that there had been no chilling effects pointed out that only very few cases had been prosecuted, and *“firms would be simply irrational if they changed their strategies based on the prosecutions. If firms have changed their conduct, it is not necessarily chilling competition. Where the intended conduct was abusive, then the result of the change is pro-competitive.”*

One respondent's view was that while dominant firms had not become overly cautious, they had become more responsible. *“The firms now consider their strategic behaviour carefully. Responsible firms now take a more considered and prudent approach to pricing policies and marketing. Irresponsible firms however still take a cavalier approach to competition law.”* Another respondent felt that although no clear pattern had emerged to make firms chill their conduct, *“firms go*

to lawyers who influence them on issues to look at. Firms, based on their assessment, may then choose to act more conservatively.”

One respondent summed up the issue by stating *“there is no chilling effect. Dominant firms are more cautious, but they still have an immense amount of flexibility. A disappointment of the abuse of dominance jurisprudence is we do not have many cases that give us clear guidelines. The two South African Airways cases (Case 1 and 2) and JTI v BATSA (Case 3) however give some direction.”*

One respondent split the effect of the various sections and stated that while section 8(d) had not had a chilling effect, the rest of section 8, including 8(c), had tremendously increased the costs of compliance, and this may have had a chilling effect. *“While people clearly understand what competitors cannot do, namely, price fixing, bid rigging and allocation of customers, compliance in abuse of dominance is very case specific and one cannot simply give a view on legality of what the firm is doing. Compliance views need to be given regularly, or you put in place ‘rules of thumb’ of what cannot be done. This can become very complicated and middle management may choose to steer clear of the action completely.”*

Section 8(c) was further complicated by the fact that the notion of a margin squeeze is embedded in it. South Africa has many vertically integrated firms due to its history where firms had to expand internally into all areas. In advising firms

on compliance, *“it is extremely difficult to put an implicit prohibition on margin squeeze in a tractable form for a manager. Two ways can be:*

- *To restructure the company to a separate downstream company and then sell services or products to this company.*
- *Then the downstream company must make a profit. Then you know you are fine.*

Many problems can however occur. Prices and their bases change over time in the market. Production changes over time. Competitors act aggressively lowering prices. If the dominant integrated firm does not match the lower prices, it will not sell.”

On the issue of the Act’s irrebuttable presumption of dominance at 45% market share, four of the seven respondents felt that the presumption was good in a country such as South Africa, and further that it did not have a chilling effect. They argued that the benefit of the presumption was that it created certainty for both the Commission and firms, and prevented debates on whether or not a firm was dominant. One respondent clearly stated that *“the need to prove market power in every case would increase the litigation burden.”* (See the Act’s section 1 definition of ‘market power’ included in Chapter 2 above).

One respondent explained that a 45% market share was a reasonable indicator of dominance, and a reasonable proxy for firms to start considering their conduct. Two respondents pointed out that in the cases considered by the Tribunal, the

firms have had market shares well in excess of 45%. They further argued that these firms with huge market shares must have had substantial market power, without which their conduct could not have had an anti-competitive effect.

Two respondents felt that the lack of flexible application of the abuse of dominance rules was the problem, rather than the presumption of dominance. One respondent stated that while the 45% threshold was in line with other jurisdictions' 50% thresholds, the real threshold which firms were concerned with in South Africa was 35%, at which market share there was a rebuttable presumption of dominance. This respondent argued that this threshold was too low and led to chilling effects.

Only two respondents felt that the 45% threshold was not good. One respondent argued that a firm should always be entitled to disprove that it has market power. The other respondent stated that *"it is little solace to a firm that the Tribunal has found firms to also have market power, as the 45% market share alone causes firms to be more careful. This is one aspect that needs to be changed in the current Act. In practice, when conducting training, firms are asked which markets they are in, and their market shares; they are then advised to stop certain conduct. It is no defence that the firm is acting for the benefit of customers or the society. This presumption of dominance therefore has a chilling effect."*

5.3.2 New Role for Commission?

An emerging theme was that the Commission needs to take on a different role. Three of the seven respondents felt that although the prosecutorial approach of the Commission had not had a chilling effect, its lack of guidance may have done so. One respondent stated that the failure by the Commission to give clear advisory opinions that can guide dominant firms had led to uncertainty, “*and dominant firms do not want to be ‘guinea pigs’*”.

The second respondent explained that part of the problem with abuse of dominance cases is that the Commission is very reluctant to give dominant firms clear guidance on what it regards as acceptable conduct. “*I have examples where the Commission has engaged with my clients saying that they think that they are engaging in abusive conduct, and want them to stop. When you ask them what they want you to do, they say that you should comply with international precedents, which is like saying ‘comply with the law’. The firms will say that they are complying with the law. The underpinning of these cases is a rule of reason or efficiency analysis, and which side of the line you are on.*” For example, the South African Airways incentives to travel agents (Cases 1 and 2) were regarded as abuses, “*but that does not mean that every incentive is an abuse. It depends on each case. The role of the Commission could improve, by dealing with abuse of dominance cases more practically rather than hypothetically*”. This respondent further pointed out that in contrast to cartel activity where the Commission had

been very effective in pursuing a prosecutorial approach; the actions of the Commission itself had not driven conduct in the area of abuse of dominance.

The third respondent explained that while the concept of margin squeeze is incorporated in section 8(c) of the Act, there has been no clarity from the Commission on when you are margin squeezing. This respondent felt that for the economy to work well, it was imperative for the Commission to develop guidelines on what it will prosecute or not, or it needed to change the law to make it clear. *“It is absurd that there are thousands of dominant firms in the economy without clear guidelines. For example, in the case of exclusive distribution, it is very vague for firms to operate, and this is wrong, although competition professionals benefit. There is no easy compliance method, and this chills competition. Firms can also choose not to be vertically integrated, and yet vertical integration is good because it avoids double marginalisation. A further complication is that in South Africa, there is often a dominant firm and two or three competitors. It is important that the rule on predatory pricing (covered in section 8(d)(iv) of the Act) is not used by the dominant firm to signal to competitors. Therefore, there is need for guidelines.”*

5.3.3 Research Question 2: Conclusion

From the above, it is clear that the enforcement actions and decisions of the Commission and Tribunal, respectively, have not had a chilling effect on competition. Similarly, the presumption of dominance at 45% market share has not chilled competition. However, the lack of clear guidelines from the Commission on the type of conduct that would be considered exclusionary has created uncertainty, and this may have had some chilling effects.

5.4 Enforcement Actions

The table below shows the following information for the period 2002 to 2009:

- the number of referrals made by the Commission to the Tribunal in respect of sections 8(c) and (d) of the Act,
- the total referrals on all Chapter 2 provisions (anti-competitive agreements and unilateral restrictive practices), and
- the percentage of sections 8(c) and (d) referrals out of the total Chapter 2 referrals

Table 1: Commission enforcement actions

Number of sections 8(c) and (d) referrals	Total number of Chapter 2 referrals	Sections 8(c) and (d) referrals as percentage of total
34	149	23%

(Competition Commission & Competition Tribunal, 2009)

From the above, the Commission does not appear to have been over-zealous in its prosecution of exclusionary acts.

The table below illustrates the difficulties involved in conducting abuse of dominance cases. The information relates to the six cases included in Appendix 2.

Table 2: Tribunal decisions

	Complaint lodged at Commission	Referral to Tribunal by Commission or Complainant	Number of hearing days	Period of hearings	Tribunal decision
Case 1	13 October 2000	18 May 2001	-	-	28 July 2005
Case 2	13 October 2003	12 October 2004	23	March 2008 to May 2009	17 February 2010
Case 3	1 October 2003	10 February 2005	50	August 2007 to July 2008	25 June 2009
Case 4	2 December 2004	20 December 2006	22	November 2007 to July 2008	3 February 2009
Case 5	13 February 2003	25 June 2004	11	June to September 2006	6 November 2006
Case 6	-	-	-	-	9 May 2001

Competition Tribunal

From the information available for Cases 1 to 5, this table shows that investigations and hearings for each case lasted an average of five years. This illustrates that abuse of dominance cases can take a long time to defend, and can use up a lot of management time and considerable financial (litigation related) resources.

CHAPTER 6: DISCUSSION OF RESULTS

6.1 Research Question 1: *When are competitive actions and conduct of a dominant firm categorised as exclusionary, and thus anti-competitive?*

A firm must be dominant in a market before it can be found to have abused its dominance (Brassey, 2005). In the cases that were examined, the Tribunal first established the existence of dominance, as otherwise the Act's abuse of dominance provisions would be inapplicable. Dominant firms therefore have special responsibilities which their non-dominant rivals do not have (Fox, 2003).

Exclusionary actions by dominant firms are capable of restricting competition in a market, through the enhancement of the firm's dominance (Gormsen, 2005). For example, a dominant firm could choose to employ a long-term strategy of sacrificing current profits in order to deter entry or promote exit to and from the market, respectively, and thus ensure future monopoly profits (Simkins, 2005).

The test established in Case 1 can guide dominant firms to assess whether their conduct is exclusionary, and in contravention of the Act's abuse of dominance provisions. The following questions can be considered:

1. Is the firm dominant in the relevant market?

2. Does the conduct fit the description of acts listed in section 8(d)? If no, does the conduct fit the Act's definition of exclusionary act ("impedes or prevents a firm from entering into, or expanding within a market" (section 1))?
3. Does the conduct have a significant anti-competitive effect on either of the two grounds below:
 - a. conduct harms competitors through higher prices or fewer product choices;
 - b. conduct significantly prevents rival from expanding in a market?
4. Does the conduct bring any efficiency, technological or pro-competitive gains?
5. On balance, does the anti-competitive effect outweigh the gains? If yes, the conduct contravenes section 8(d) or (c).

Where a dominant firm operates in more than one market, Case 6 enumerated an additional test for exclusionary acts to be anti-competitive – does the conduct enable the dominant firm to extend or create its market power in a related market?

It is critical that the alleged exclusionary act also has an anti-competitive effect, as otherwise, it would lead to the prohibition of competitive conduct which is beneficial to consumers (Fox, 1986). Cases 1 and 5 highlighted the need to link anti-competitive effects to the exclusionary act in both sections 8(c) and (d), as the Act's definition of "exclusionary act" can include both competitive and anti-competitive conduct.

As very clearly illustrated in Case 3, dominant firms are encouraged to pursue competitive conduct. Indeed, several experts noted that this decision was a triumph for dominant firms. Importantly, the Tribunal clarified the position by stating that a dominant firm, which operates within the confines of the Act, can and should compete vigorously to increase or defend its market share. The Tribunal noted that even a powerful brand, such as BATSA's *Peter Stuyvesant*, cannot be popular forever; a dominant firm should therefore be entitled to defend its market share from upcoming brands.

6.1.1 Distinction between Cases 1 and 3

From the research, it was clear that Case 1 and 3 were the most prominent South African cases on exclusionary acts. These cases however had opposite outcomes, leading to some uncertainty on when in fact dominant firms' conduct would be exclusionary and anti-competitive. Case 3 clearly illustrates that the need for an anti-competitive effect is a pre-requisite for a finding that an exclusionary act amounts to prohibited conduct. Where an alleged exclusionary act does not harm consumers nor lead to significant foreclosure, the anti-competitive effect will not have been established. The term foreclosure refers to a situation where competitors' access to markets (or supplies) is hampered (or eliminated) as a result of the dominant firm's conduct (Commission of the European Communities, 2009).

While one respondent insisted that there was no basis for distinguishing Case 3 from Case 1, an analysis of the two cases revealed otherwise. The key distinction between the SAA incentive schemes with travel agents (Case 1) and the BATSA agreements with retailers and marketing practices (Case 3) was that in the case of the cigarette market there was no foreclosure. Principally, rival cigarette brands were not excluded from the display units. In addition, BATSA did not appear to be inducing or forcing the retailers to do anything. The retailers sought to make as much money as possible from the limited retail space, and therefore "sold" it to the highest bidder. Furthermore, it was the retailers who demanded payment for point

of sale data as a minimum requirement for category management participation. (See discussion on category management in Case 3.)

On the contrary, the SAA agreements with travel agents had more of a foreclosure effect. The incentives to travel agents were substantial and the payments often determined the travel agents' profitability. The incentives were also designed in such a manner that travel agents were penalised for selling rival airlines' tickets. Thus rival airlines were foreclosed from a key distribution channel, particularly at a time when the internet had not developed and there was asymmetry of information between travel agents and their customers. While in the airline tickets market travel agents would tell customers which flights were available and at what price, in the cigarette market, it was not contested that smokers knew that retailers stocked all manufacturers' cigarettes. The potential for foreclosure was therefore much higher in the domestic airline market during the period when the SAA agreements were complained of.

Critically, distribution was not foreclosed in the cigarette market. Promotional opportunities in the cigarette market were also not foreclosed. It was also demonstrated in Case 3 that where a rival manufacturer, JTI (the complainant) felt it was commercially justified to pursue specific retailers, it did so successfully.

Furthermore, in the South African domestic airline market, the travel agent channel accounted for a substantial 60-70% of sales (Case 1) during the relevant period,

while the organised retail chains accounted for only 19.5% of cigarette sales (Case 3). Thus, even if rival cigarette manufacturers were entirely foreclosed from organised retail, there were other retail options.

Interestingly, BATSA's advantage in the display units was as a result of its market share, and not due to the nature of the agreements with retailers. Indeed, had a smaller rival acted as category captain and applied pure category management principles, BATSA's brands would continue to enjoy more space and favourable positions in the display units.

This comparison of these two cases highlights how the nature of an industry can influence the effects emanating from a dominant firm's conduct. Due to the nature of the cigarette industry (and the limited market share of the distribution channel in issue), BATSA's conduct did not have an anti-competitive effect.

6.2 Research Question 2

Are the enforcement actions of the Commission and the decisions of the Tribunal arising from Sections 8(c) and (d) of the Act likely to cause dominant firms to eschew robust pro-competitive conduct for fear of erroneous or overly-zealous prosecution?

From the research, neither the Commission's enforcement actions nor the Tribunal's decisions appear to have chilled competition. As illustrated in Table 1, the evidence of referrals made by the Commission does not support an assertion that the Commission has been over-zealous in its prosecution of abuse of dominance cases (and particularly sections 8(c) and (d) of the Act).

Similarly, the Tribunal's decisions examined do not support a bias against dominant firms – 50% of the decisions were in favour of dominant firms. The Tribunal's decision in case 3 indeed supports the view that dominant firms must continue competing robustly. Furthermore, five of the seven respondents interviewed felt that there had been no chilling effects from the Commission's prosecutorial approach or Tribunal's decisions. This finding is consistent with the view expressed by Lewis (2008) that over-enforcement has not occurred in South Africa.

An emerging theme from the research was that the lack of clear guidelines from the Commission may have had some chilling effects, as there is uncertainty on what conduct is allowable. While Commission guidelines and Tribunal decisions can suggest standards to distinguish between exclusionary and pro-competitive behaviour for some types of dominant firm conduct, “the underlying substantive principles are not always easy to discern” (Vickers, 2005).

The research also considered whether the 45% market share presumption of dominance may have had chilling effects. It is important to recall that there is no examination of market power when this threshold is reached. An examination of market power would require, in addition to the definition of the relevant market and computation of the firm’s market share, other evidence such as the firm’s profitability or ability of market entry (Landes & Posner, 1981).

From the research, it was evident that in the cases which have been prosecuted by the Commission, the dominant firms have had market shares well in excess of the 45% threshold. Further, while the 45% market share presumes dominance, there is still need for an examination of an abuse of dominance, with an effects-based test. For anti-competitive effects to be felt in the market, this demonstrates that the firms had market power, as a firm without market power could not affect the market structure (Unterhalter, 2005).

While the determination of the relevant market and the dominance thereof is the first stage of enquiry in abuse of dominance cases, this merely establishes the applicability of the Act's abuse of dominance provisions. A determination of dominance, without more, does not establish abusive conduct, and this presumption alone can therefore not have chilling effects. Indeed, as indicated very eloquently by one expert, it merely puts the dominant firm on notice of the need to take cognisance of the Act's provisions to ensure that it does not tamper with the competitive landscape in the relevant market.

6.3 Implications for business

An emerging theme was that dominant firms must assess their competition compliance risk as a business risk. One respondent stated that because abuse of dominance cases involve an effects based analysis, businesses need to weigh up the risk that competition authorities may be of the view that the conduct was anti-competitive. In addition to administrative fines (where applicable) and potential third party damages, businesses need to also consider the risk of negative publicity. Reputational risk is particularly of concern to multinational companies.

Dominant firms should therefore take cognisance of the Act's provisions and consider structuring rebates, incentive schemes and any type of vertical arrangements, to avoid foreclosure. Dominant firms should also consider the necessity for exclusive arrangements.

As shown in Table 2, abuse of dominance cases take a long time to be resolved, and thus management and financial resources could be tied up in litigation. Also, one respondent pointed out that firms should note that these cases are enormously expensive, but unavoidable fact intensive, especially in discussions on the relevant market. Similarly, pro-active review of dominant firm conduct requires a considerable amount of economic analysis and management time, which small firms may choose not to expend. Where firms choose not to expend resources on market analyses, they may tend to be less aggressive.

Uncertainty on whether planned action could be anti-competitive, at best, leads dominant firms to incur unnecessary legal costs and waste managerial time. At worst, wrong conclusions on the anti-competitive nature of competitive actions lead dominant firms to inaction and foregone profits. Such consistent tempering of dominant firms' competitive conduct could lead to the firms' long-term unprofitability.

CHAPTER 7: CONCLUSION

7.1 Main findings

From the research conducted, it was found that there are insufficient cases to establish clear guidelines on when the competitive actions of a dominant firm will be found to be exclusionary and anti-competitive. However, certain themes are beginning to emerge from the cases that have been adjudicated by the Tribunal.

- Dominant firms are allowed to compete on the merits to grow and or defend their market shares.
- The alleged exclusionary conduct must have an anti-competitive effect.
- The purpose of competition law is to protect competition and not competitors. Non-dominant rivals are therefore not entitled to use competition law to protect themselves from robust competition by dominant firms, or to eschew commercial arrangements.
- Where competition law is focussed on protection of competitors, it could be subject to abuse. Non-dominant firms could choose to rely on the Act's protection, rather than competing effectively, and this would be to the detriment of consumers.
- The Commission and Tribunal have not been over-zealous in their enforcement of the Act's abuse of dominance provisions, and as such have not led to the chilling of competition. However, the failure by the Commission and Tribunal to publish guidelines and emerging principles, respectively, may have led competition advisors to give more conservative advice.

While the Tribunal's move towards an effects-based approach is laudable in curbing against over-enforcement, it places a heavier burden on dominant firms' compliance efforts. An evaluation of a particular conduct's effects can only be done on a case-by-case basis. As such, it is difficult to prescribe a general rules-based compliance program to guide dominant firms in their development of competitive strategies. Where proposed conduct is borderline (can be categorised as either pro-competitive or anti-competitive), the dominant firm should expend the resources required to assess the potential economic effects of such conduct. Alternatively, the firm can weigh up the potential legal risk, and treat it as any other business risk.

In conclusion, the Act's sections 8(c) and (d) abuse of dominance cases are highly fact-intensive, industry specific and outcomes are effects-based. Dominant firms must therefore test potential effects of their competitive strategies within the market structures in which they operate. While such an approach may seem to be overly expensive and perhaps unnecessary, it is clearly cheaper than eschewing the competitive action altogether, where the dominant firm erroneously concludes that the conduct is anti-competitive. In an ever-changing global competitive landscape, dominant firms can ill afford to consistently temper their own competitiveness.

7.2 Recommendations

The Commission should publish guidelines on the Act's abuse of dominance provisions. While it is recognised that these would not be definitive principles, by setting parameters on the type of conduct that would not fall foul of the Act, such guidelines would greatly assist dominant firms in their compliance efforts.

The Tribunal should, in its decisions, refer to previous similar cases and explain why it is taking a different approach. This would greatly assist in the development of South African competition law, and would also provide dominant firms with certainty on when their conduct would be anti-competitive.

7.3 Future research ideas

This research relied on the opinions and expertise of competition law experts. While these individuals had immense knowledge and experience in competition law and economics, a sample of representatives from dominant firms would have provided practical insights on such firms' decision making.

Future research can investigate the actual behaviour of dominant firms to determine what role, if any, competition law issues play in such firms' competitive strategies.

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APPENDICES

APPENDIX 1: Interview Questions

1. What is your assessment of the prosecutorial approach of the Commission and the decisions of the Tribunal in the area of abuse of dominance? Is this approach 'chilling competition', by making dominant firms overly cautious in their competitive strategies and conduct?
2. How do you go about advising your clients who are dominant to assess their conduct in relation to a possible violation of section 8 of the Act?
3. Are there any key questions that you advise your clients who are dominant firms to consider in relation to a possible violation of section 8 of the Act?
4. Which cases do you consider the key abuse of dominance cases?
5. What is your assessment of the key abuse of dominance cases?
6. Do you find consistent principles and approaches emerging from the key abuse of dominance cases?
 - a. If yes, what are these principles and approaches?

- b. If no, is this the result of manifest inconsistencies in the approach of the Tribunal?
 - i. If yes, what are these inconsistencies?
 - ii. If inconsistency is not the problem, does it arise because competition law cases are so fact intensive that it is difficult to arrive at a confident assessment of the outcome of a case without the expedient of a full trial and discovery, etc?
- 7. How do the resources required to prosecute and defend abuse of dominance cases influence your advice to dominant firms?
- 8. Does the 45% market share presumption of dominance have a chilling effect, as opposed to a market power examination?

APPENDIX 2: Case Summaries

Case 1: The Competition Commission v South African Airways (Pty) Ltd 18/CR/Mar01 (“CC (Nationwide) v SAA”)

South African Airways (“SAA”) had two incentive schemes (the override incentive and Explorer schemes) with travel agents. The Commission instituted a case against SAA, pursuant to a complaint by Nationwide Airlines Group (“Nationwide”), alleging that the incentive schemes constituted an abuse of dominance.

Dominance

The Tribunal found that SAA was presumptively dominant in the market for the purchase of domestic airline ticket sales services from travel agents in South Africa. The Commission successfully demonstrated that SAA’s market share was well over 45%, and went further to show that SAA enjoyed market power in relation to travel agents. Dominance was calculated using the relative flown revenue of the firms in the market. Flown revenue is calculated using boarding pass information.

The Conduct

The override scheme involved two types of commission, the override and incentive commission. These were paid to travel agents over and above the basic commission for sales up to a target figure. The override commission was paid if the agent met and exceeded the target on the total of all sales earned, even those below the target. The incremental commission was paid if the travel agent earned

a certain percentage of sales above the targeted amount. The incremental commission was paid only on the amount above the target. Travel agents did not have a common target. The target for each firm was set based on its previous annual sales figures with a negotiable percentage increment.

SAA had these types of agreements with travel agents since around 1980, and there had been no complaints. However, in October 1999, SAA adopted a more aggressive approach to the incentive scheme. SAA reduced the basic commission from 9% to 7%, and increased the rate of the override and incremental commissions. SAA also made the attainment of the override and incentive commissions more difficult by raising the targets annually at higher rates, and raising the point at which the incremental commission was paid. The result of these changes was that for travel agents to maintain their profitability levels, they would have to exceed their targets by sufficient margin to achieve the override and incremental commissions. However, those travel agents who achieved these additional commissions received very attractive rewards.

The Explorer scheme rewarded individual travel agents' employees with a free international ticket for achieving SAA's sales targets. The Explorer scheme also had a bonus pool that incentivised the staff generally by allocation of points to each agency.

Abuse of Dominance

The Commission alleged that SAA's incentive schemes constituted an abuse of dominance, in contravention of section 8(d)(i) or section 8(c). The Tribunal discussed the difference between sections 8(c) and (d). Section 8(d) lists exclusionary acts considered more blatant, and for these, an administrative fine is payable for a first contravention. Dominant firms must therefore behave with due caution in relation to these listed acts. In section 8(c) no acts are listed and the complainant would have to prove that the conduct is indeed exclusionary. As the dominant firm is not forewarned, it is placed in a more precarious position. The Tribunal explained this as the basis for the policy choice to place the onus on the complainant to negate efficiencies, and not to impose an administrative fine for a first contravention.

Exclusionary to anti-competitive effect

An exclusionary act is conduct other than competition on the merits which impedes or prevents the growth of rivals in the market. Such acts can lead to the creation or enhancement of a dominant firm's ability to exercise market power.

The Tribunal found that the Act requires an examination of the conduct to determine whether it falls under the section 8(d) list, or that it meets the Act's definition of "exclusionary act" and thus falls under section 8(c). The next step is to enquire whether the exclusionary act has an anti-competitive effect. The act will have an anti-competitive effect if there is evidence of actual harm to consumer

welfare, or the exclusionary act is significant in terms of foreclosing the market to rivals. The Tribunal explained that a requirement to also prove consumer harm is unnecessary and would be under-deterrent. A finding of an exclusionary act alone is also not sufficient as it would outlaw competitive non-predatory behaviour, and be over-deterrent.

Efficiency justification

The Tribunal explained that in both sections 8(d)(i) and 8(c), there can be an efficiency justification – technological, efficiency or other pro-competitive gains that outweigh the anti-competitive effect. In section 8(d)(i), the onus of proof of the efficiency justification is on the respondent, while in section 8(c) the onus to negate it is on the complainant. The Tribunal found that SAA did not prove that the incentive schemes had any efficiency justification. The Commission had shown that the target amounts for the override scheme were not based on volume of tickets sold, but on the proportion of tickets that were of SAA. The scheme was an inducement was not to sell tickets of the competitor, rather than to increase output. Therefore, the scheme was not efficiency enhancing, but designed to promote loyalty to the dominant carrier, to the exclusion of its rivals.

Finding

The Tribunal found that SAA's override scheme required or induced customers not to deal with a competitor and therefore contravened section 8(d)(i) of the Act. It was the nature of the scheme, and not its existence, that was abusive. By lowering the standard commission and increasing the override and incentive commissions, SAA had materially altered travel agents' incentives, leading to the anti-competitive nature of the scheme. Further, the use of the Explorer scheme contributed to the anti-competitive effects of the override scheme.

Case 2: Nationwide Airlines (Pty) Ltd and Comair Ltd v South African Airways (Pty) Ltd 80/CR/Sept06 (“Nationwide and Comair v SAA”)

SAA had two incentive schemes (the override incentive and Explorer schemes) and trust agreements with travel agents. Nationwide Airlines (Pty) Ltd (“Nationwide”) and Comair Ltd (“Comair”) sought a declaration order that the incentive schemes and payments pursuant to the trust agreements were exclusionary and in contravention of section 8(d)(i) or section 8(c).

Dominance

The Tribunal found SAA to be dominant in the two relevant markets: the market for travel agency services to airlines and the market for scheduled domestic air travel.

The Conduct

The two incentive schemes, although slightly amended and related to a subsequent period, were similar to the schemes that were considered in the earlier case (*CC (Nationwide) v SAA*). The incremental commission structure had been flattened so that the commission rate did not increase, irrespective of the sales in excess of the target.

In addition to these two schemes, SAA had introduced trust payments to compensate travel agents for the loss of revenue from the flattened commission structure. These were lump sum payments made to travel agents for achieving specific targets, and particularly in the case of large travel agents, for maintaining

revenue targets of the previous year. SAA retained considerable discretion in computation of the trust payments, and travel agents did not know whether or not they were eligible for payments. The payments were substantial and critical to travel agents, as they sometimes determined the profitability or otherwise of the agent.

Abuse of Dominance

By concluding the agreements with travel agents, SAA had sought to extend or maintain its dominance through aggressive override incentives, rather than engaging in competition on the merits.

Exclusionary to anti-competitive effect

The amended incentive schemes had an even greater exclusionary effect as travel agents' targets became increasingly more difficult to meet. SAA continuously fine-tuned its formulas for computing incremental growth and implemented a range of exclusions. Growth from acquisitions of new travel agent outlets and new corporate accounts was excluded from the computation. Travel agents were thus put under immense pressure to achieve their targets at the expense of SAA's competitors.

Section 8(d) acts are not presumed as having anti-competitive effects. There is a two-stage enquiry, as was explained in the *CC (Nationwide) v SAA* case – whether the travel agents were incentivised to move customers away from rivals, and,

whether they had the ability to do so. While the internet and direct sales channels were developing, travel agents remained the most significant sales channel, distributing approximately 70% of the total domestic airline market. SAA had concluded agreements with approximately 70-90% of the market, which suggested that the foreclosure effect was potentially substantial. Asymmetry of information between travel agents and customers prevailed during the relevant period, and customers continued to rely on the agents' expertise and advice. Travel agents therefore had both the financial incentives and the ability to influence their customers' preferences, to the detriment of SAA's competitors. The Tribunal concluded that the SAA incentives foreclosed rivals and had a significant anti-competitive effect on both Nationwide and Comair

The Tribunal stated that although there was no evidence of consumer harm, it could be inferred that the SAA incentives, coupled with travel agents' ability to influence consumers' preferences, harmed consumers through higher prices or reduced choice.

Efficiency justification

There was no evidence that the override incentive and trust agreements achieved any real efficiencies in ticket distribution for SAA, nor that the efficiencies outweighed the foreclosing effects.

Finding

The Tribunal found that SAA's override incentive and trust agreements (and payments) contravened section 8(d)(i) of the Act. The agreements induced travel agents to deal with SAA at the expense of its rivals and had foreclosed the rivals in the market for scheduled domestic airline travel.

Case 3: The Competition Commission and JT International South Africa (Pty) Ltd v British American Tobacco South Africa (Pty) Ltd 05/CR/Feb05 (“*JTI v BATSA*”)

British American Tobacco South Africa (“BATSA”) had concluded agreements with several cigarette retailers, vending machine operators and entertainment venue owners. The Commission instituted a case against BATSA, pursuant to a complaint by JT International (“JTI”), alleging that these agreements constituted an abuse of dominance.

Dominance

The Tribunal found that BATSA was presumptively dominant in the national retail market for the sale of manufactured cigarettes. The Commission successfully demonstrated that BATSA’s market share was well over 45%, with an enviable share of approximately 96% of total manufactured cigarette sales in South Africa. This was bolstered by BATSA’s Peter Stuyvesant brand’s market share of approximately 40%.

The Conduct

It was alleged that BATSA had, through its’ agreements with retailers, appropriated promotional opportunities to the detriment of its competitors. The case was principally concerned with the allocation of space and preferential positioning of BATSA cigarette brands and categories in cigarette display units. BATSA

purchased from retailers point of sale data and the right to be a category captain. The point of sale data was in principle used for space allocation.

As category captain, BATSA was tasked with the role of allocation of space and position across the different cigarette manufacturers' brands and categories, in accordance with the firms' market shares. In addition to this service, BATSA also provided the retailers with display units, and ensured that these units were not used for non-tobacco products. JTI complained that BATSA failed to comply with category management principles, by allocating more space to Dunhill (an upcoming BATSA brand) than was justified by that brand's market share, and by placing Camel, a JTI premium or popular brand, alongside cheap brands. This unfavourable position made Camel appear more expensive.

It was also alleged that the BATSA agreements limited competitors' ability to place secondary display units and advertising material at the retailers' point of sale. Further, allegedly BATSA secured compliance with the agreements through cash incentives and payments in kind, such as the free display units. BATSA was also alleged to have incentivised owners of selected entertainment venues to grant it access to these venues for promotional activities, in preference to competitors.

In practice, retailers demanded a fee for the data and the privilege to act as category captain, but as owners of the space, they were entitled to make the final decision on space allocation and position. Retailers required that all cigarette

manufacturers' brands and categories were stocked in the display units, and no out-of-stock situations occurred. JTI had initially chosen not to compete for the role of category captain, and had previously refused to purchase the point of sale data, which was the retailers' minimum requirement to participate in category management.

The Tribunal noted that the fundamental problem with category management is that it could be used as an organising arrangement for a collusive arrangement in an oligopolistic market, or dominance enhancing in a market dominated by a single firm which acts as the category captain. BATSA's alleged abuse of category management principles was therefore a predictable outcome for a profit maximising dominant firm.

JTI sought an order for BATSA to adhere to pure category management principles, and thus not appropriate any private gains for the service it provided. JTI was therefore seeking a legally sanctioned free ride, when it was entitled to compete to perform the role itself, and had in fact done so successfully in the retail segments where it chose to compete. Thus while JTI chose commercially to free ride on BATSA's captaincy, it sought to use competition law to neutralise BATSA's promotional efforts. The Tribunal noted that BATSA was not obliged to provide any free service to its smaller rivals.

Abuse of Dominance

The Commission alleged that BATSA's marketing practices were prohibited conduct in contravention of sections 8(d)(i) or 8(c) of the Act. It was alleged that BATSA's deviation from category management principles was equivalent to contravention of competition law. The alleged deviation included: seeking to dominate secondary displays at points of sale through payment of incentives (cash and free display units); allocating itself space based on aggregated national sales data; abusing its role as category captain by allocating premium / popular opposition brands with cheap brands (at the bottom left-hand corner of the display unit); and, failure to consult with other participants (rivals) in the category.

Exclusionary to anti-competitive effect

The Commission unsuccessfully argued that BATSA's conduct was exclusionary, and to the ultimate detriment of cigarette consumers through restriction of choice and the resultant obligation to pay higher prices.

- While the practice of selling preferential allocation of space and position was a form of limited exclusive, there was however no evidence of retailers assigning shelf space to BATSA on an exclusive basis.
- It was widely known by smokers that all cigarette brands were available at all retail outlets that sold cigarettes, and BATSA could not remove rivals' products from the display units.
- Cigarette purchasers did not browse the shelves, but requested attendants to find the desired brands.

- The agreements with retailers were of short duration (twelve to fifteen months), and thus the competitive arena for category captaincy was re-opened at short intervals.
- The retailers' display units' role in promotion of cigarettes was relatively inconsequential and therefore there was little, if any, foreclosure of promotional opportunities.
- In franchised stores, there was less compliance with head office agreements therefore smaller manufacturers could penetrate. Indeed, JTI had cherry-picked 10% of Spar stores, all of which were in urban areas, and 20% of Pick n Pay franchise outlets, notwithstanding BATSA-Spar and BATSA-Pick n Pay agreements. The moderate foreclosure was thus reduced by smaller rivals' proven ability to undermine BATSA's coverage.
- Promotional space in the organised garage forecourts was highly contested by the three manufacturers. This was evidence that the smaller rivals succeeded where they chose to compete for promotional opportunities.
- The decline in the market share of JTI's brand, Camel, could not have been a result of BATSA's agreements as it was Marlboro, another manufacturer's brand, that was eating into Camel's market share.
- The vast majority of cigarettes were not sold through vending machines or at the upmarket entertainment venues exclusively contracted by BATSA, but rather through entertainment venues in the historically black townships – and which were open to JTI to compete for promotional opportunities.

- The marketing of cigarettes was highly regulated in South Africa, and this had restricted promotional activities to retailers display units and points of sale, and entertainment venues. The Tribunal argued that it was the regulatory environment, rather than BATSA's conduct, that restricted JTI's promotional opportunities.
- The nature of the cigarette market was such that there was intense brand loyalty, which reduced the impact of merchandising and promotional activities.

For the above reasons, the Tribunal could not identify harm to consumers or find significant foreclosure arising from BATSA's promotional activities.

The Tribunal stated that aggressive pursuit or defence of market shares, even by dominant firms, is not necessarily anti-competitive. While dominant firms were uniquely subject to the Act's abuse of dominance provisions, such firms were entitled, and indeed expected, to compete as vigorously to increase or defend their market shares as their smaller rivals.

Efficiency justification

The restrictive regulatory environment had compelled BATSA to use new and innovative promotional methods, and this response was pro-competitive. Incentive payments to vending machine operators led to growth of this distribution mechanism, which was a pro-competitive gain.

BATSA, as category captain did a lot of work to ensure orderly displays of all cigarette categories, and also provided free display units to the benefit of itself, its' rivals and retailers. Indirectly, consumers benefit from the free benefits granted to retailers. BATSA's rivals also benefitted from the free service by having their cigarettes neatly displayed.

The Commission sought an order prohibiting BATSA from playing the role of category captain. It was however more efficient for a captain (manufacturer), as opposed to a retailer, to perform the role because it was difficult for retailers to understand the detailed aspects of thousands of categories.

Finding

The Tribunal found that it was not established that the conduct in question gave rise to anti-competitive effects either through direct consumer harm or significant foreclosure. In line with the test laid out in *CC v SAA*, the extent of foreclosure was not significant, and therefore there was no anti-competitive effect. There was also no showing of harm to competition, as there were available alternative promotional opportunities that JTI had ignored.

Competition law is concerned with ensuring that there is robust competition. Dominant firms are expected to continue to compete robustly as products or brands are not dominant forever. BATSA needs to be allowed to compete on its

other brands which have low market shares, such as Dunhill. Competition authorities cannot prevent it from doing so by forcing it to distribute its allocations of position and space between its various brands other than as it sees fit.

Case 4: The Competition Commission v Senwes Ltd 110/CR/Dec06 (“CC v Senwes”)

The Commission instituted a case against Senwes Ltd (“Senwes”), a vertically integrated firm, alleging that it had abused its dominant position in the grain storage market to the detriment of rival firms in the downstream market for the trading of physical grain.

Dominance

The Tribunal stated that while it is necessary to prove that a respondent is a dominant firm in a section 8 or 9 contravention, it is not necessary for the firm to be dominant in the market where effects of the abuse are felt. Senwes was found to be dominant in the regional (“Senwes area”) market for grain storage with a market share over 80%, although it was clearly not dominant in the downstream market for the trading of physical grain.

The Conduct

Senwes introduced differential tariffs for grain storage for farmers and traders. Farmers continued to enjoy a ceiling on their storage costs, which in essence meant that the cost of storage was capped at the cost for 100 days and storage for the remainder of the season was free. Traders were denied this capped storage benefit, and continued to pay the daily storage rate beyond the 100 days period (“post-cap period”). Additionally, when farmers applied for a silo certificate, a pre-requisite for trading grain on Safex (the commodities trading market of the

Johannesburg securities exchange) and for sale to a third-party trader, the farmer was treated as a “trader” and denied the capped storage benefit.

Senwes did not internally transfer storage costs to its internal trading division, nor did it charge it for the costs of a silo certificate.

Abuse of Dominance

It was clear in this case that abuse can occur in an adjacent market in which the respondent firm is not dominant, and thus a firm is not free to leverage its market power from one market to another with impunity.

Exclusionary to anti-competitive effect

The costs of storage affected traders’ profit margins to the extent that when traders did not get the capped storage tariff in the Senwes area, trading was not profitable. To illustrate, a trader who paid uncapped storage costs in the post-cap period had costs that were 3.3% more expensive than one who did not (such as Senwes’ trading division), and with net profit margins that seldom exceeded 1%, the transaction was not viable.

It was thus illustrated that Senwes had raised its rivals costs, with the effect that the traders would be foreclosed. It was not necessary for the foreclosure to be total, partial foreclosure was sufficient, as the vertically integrated dominant firm

could be content to restrict rivals' output and obtain a larger market share for itself in the downstream market.

The Tribunal explained the relevant conditions for the existence of a margin squeeze was that: the dominant firm supplied an input to downstream rivals; the input was essential for the rivals to compete; and, the input formed a substantial part of the rivals' fixed expenditure. It was then important to test whether the dominant firm's downstream operation could trade profitably on the upstream price charged to its rivals. An alternative test was whether the margin between the dominant firm's upstream price and the price that the downstream firm charges, would allow a reasonably efficient firm to obtain a normal profit.

From the evidence, Senwes was dominant in the upstream grain storage market, it operated in the grain trading market, storage was an essential input to traders in the physical grain trading market and Senwes' storage prices in the post-cap period rendered the activities of an equally efficient rival uncompetitive. Senwes' margin squeeze conduct therefore amounted to an exclusionary act that impeded or prevented rival traders from competing with its downstream trading division.

Third-party traders in the Senwes area were confined to trading within the first three months. Although it was more profitable to hold grain for longer periods, the uncapped storage tariff rendered the rival traders un-competitive. The result was that rival traders traded less in the post-cap period, and Senwes' trading division

reaped the benefits as evidenced by its increased trading volumes. Senwes' margin squeeze abuse therefore had an anti-competitive effect and substantially foreclosed the market to rivals in the post-cap period. Additionally, due to the inability of rival traders to competitively bid for purchase of farmers' grain and sale to grain processors, the abuse harmed consumer welfare in respect of prices paid to farmers and prices paid by processors.

Efficiency justification

Senwes failed to establish an efficiency or pro-competitive defence for its conduct. The Tribunal explained that without such a defence, a balancing between the anti-competitive effect and pro-competitive gain could not be conducted.

Finding

The Tribunal found that Senwes had contravened section 8(c) of the Act. The margin squeeze was an exclusionary abuse that had a substantial anti-competitive effect that foreclosed rival traders from the market in the post-cap period.

The Tribunal's finding was confirmed on appeal by the Competition Appeal Court ("CAC"). The CAC found that if Senwes' trading division incurred similar storage costs, it could not have profitably offered its trading prices. The Tribunal was thus justified in finding that Senwes conducted an exclusionary act that had the effect of impeding or preventing rival traders from competing with its trading division.

Case 5: Mandla-Matla Publishing (Pty) Ltd v Independent Newspapers (Pty) Ltd 48/CR/Jun04 (“*Mandla-Matla v Independent Newspapers*”)

Independent Newspapers (Pty) Ltd (“Independent Newspapers”) provided, *inter alia*, printing and distribution services for *Ilanga* newspaper, which was owned by Mandla-Matla Publishing (Pty) Ltd (“Mandla-Matla”). Upon expiry of the service agreement, Independent Newspapers refused to give Mandla-Matla access to its distribution network and distribution information. Mandla-Matla instituted a case against Independent Newspapers alleging that the refusal constituted an abuse of dominance.

Dominance

There was little clarity on the definition of the relevant markets, the newspaper publishing market and newspaper distribution market. The relevant geographical area appeared to be the Durban region of Kwa Zulu Natal, a province of South Africa. There was also no clear finding of Independent Newspaper’s dominance.

The Conduct

Upon expiry of the service contract between the two firms, Independent Newspapers was no longer contractually prevented from introducing a Zulu language newspaper, in competition with *Ilanga*. It introduced a new Zulu title, *Isolezwe*, and directed its independent distributors to cease distribution of *Ilanga*, failing which they would lose the right to distribute Independent Newspapers’ other titles. The independent distributors had developed a distribution network

throughout the historically black townships. Independent Newspapers also declined to give distributors' information to Mandla-Matla and its new service provider, Natal Witness Printing and Publishing Company (Pty) Ltd ("Natal Witness").

Natal Witness was a newspaper publisher based in Pietermaritzburg (a region of Kwa Zulu Natal). Independent Newspapers and Natal Witness had two competing newspaper titles, *Mercury* and *Witness*, respectively, and were also established distributors of newspapers and other printed material in their respective geographical areas.

Abuse of Dominance

It was alleged that Independent Newspapers had abused its dominance in the newspaper distribution market in order to protect and extend the market position of its new newspaper title *Isolezwe*, at the expense of *Ilanga*.

Exclusionary to anti-competitive effect

Mandla-Matla alleged that Independent Newspapers' conduct foreclosed it from the market. The Tribunal reiterated that as per their decision in *CC (Nationwide) v SAA*, sections 8(c) and (d) require that both elements of the exclusionary act and its alleged anti-competitive effect are proved. There was no evidence that Mandla-Matla had tried to gain access to the distribution network by offering distributors more attractive terms than Independent Newspapers. Furthermore, on the

evidence, sales of *Ilanga* started stabilising as early as the first month, Natal Witness having spent two months setting up a distribution network. The duration of the foreclosure was therefore minimal. The rapid establishment of the distribution network showed that there were very low barriers to entry, and that the relevant skills and assets required already existed in the market. There was no evidence that either Mandla-Matla or competition itself suffered from *Isolezwe*'s entry.

Efficiency justification

The fact that joint distribution was common in the newspaper distribution market was not, of itself, compatible with robust competition. Furthermore, the launch of a new title, *Isolezwe*, in competition with 100 year old *Ilanga* justified extra-ordinary measures, and Independent Newspapers was entitled to use its distribution network as its competitive advantage against *Ilanga*.

The establishment of 10-fold increase of printing capacity by Natal Witness and the expansion of the market for Zulu newspapers were pro-competitive outcomes of Independent Newspapers' conduct. Natal Witness' development of a parallel distribution network in Independent Newspapers' geographical network intensified rivalry in the distribution market. The Tribunal noted that Mandla-Matla's new contract with Natal Witness had significantly improved the competitive structure of three markets, namely, the market for newspaper printing, distribution and publishing.

Finding

The Tribunal dismissed the application on the ground that Mandla-Matla clearly failed to establish an anti-competitive effect.

Case 6: York Timbers Ltd v South African Forestry Company Ltd 15/IR/Feb01
(“York Timbers v SAFCOL”)

South African Forestry Company Ltd (“SAFCOL”) was responsible for the management and development of certain State forests. It sold saw logs from these forests and it also owned sawmills to which it supplied saw logs in competition with, *inter alia*, York Timbers Ltd (“York Timbers”). York Timbers instituted a case against SAFCOL alleging that a reduction in the guaranteed supply of saw logs constituted an abuse of dominance in contravention of section 8(d)(ii) or section 8(c) of the Act.

Dominance

The relevant market was defined as the quantum of saw logs available to non-integrated sawmills in Mpumalanga province. As SAFCOL’s share of this market clearly exceeded 45%, the Tribunal found that SAFCOL was dominant. The Tribunal stated that SAFCOL was deemed to be dominant in terms of section 7 of the Act, and it was therefore not relevant to show that it did not have market power.

The Tribunal however noted that the existence of long-term contracts do not constrain market power, as this would be exercised at the time of conclusion of the contract. It was further noted that no monopolist had absolute power to determine its price, as there was a price level at which it would not be able to dispose of its product.

The Conduct

SAFCOL and its predecessor (the Department of Water Affairs and Forestry) had historically (since the 1950s) entered into contracts with sawmills initially for ten years, which could be extended for successive five year periods subject to agreement. By contract, SAFCOL guaranteed sawmills specified volumes of saw logs per annum. Subsequently, SAFCOL revised the contracts and limited the tenure period to successive three year periods, and reserved a cancellation right subject to a three year notice period. Eventually, all SAFCOL sawmill customers, except York Timbers, accepted the new restricted contractual terms. As a result of York Timbers' persistent refusal to re-negotiate the commercial agreement, SAFCOL unilaterally reduced its guaranteed saw logs supply by two-thirds.

Abuse of Dominance

York Timbers alleged that SAFCOL was attempting to leverage its dominance in the upstream market for the supply of saw logs to the downstream sawmilling market. The Tribunal stated that for a vertically integrated firm, it was necessary to establish that the firm was drawing on its power in the market in which it was dominant and attempting to create or exercise market power in a related market.

The Tribunal stated that York Timbers needed to show that SAFCOL had refused to supply and that such refusal was in contravention of the Act. Although a reduction in supply could constitute a refusal to supply, the Tribunal found that there was no refusal to supply. SAFCOL had merely reduced the guaranteed

volume of logs. York Timbers was then able to compete for supply of logs with other sawmills at the current market price. Thus, if York Timbers was willing to pay the price that SAFCOL's other customers were willing to pay, it would obtain the logs it required.

Exclusionary to anti-competitive effect

As York Timbers could compete for saw logs on terms similar to those available to its competitors, it was not prevented from expanding in the market and SAFCOL's conduct was therefore not exclusionary.

The Tribunal also stated that York Timbers had failed to show the conduct was anti-competitive, through extension or creation of SAFCOL's market power in the downstream sawmilling market. The Tribunal noted that for such conduct to be anti-competitive, it must be shown to extend market power in a related or collateral market.

Efficiency justification

The anti-competitive effect was not established, and it was therefore not necessary for SAFCOL to show efficiency or other pro-competitive gains that outweighed the effect.

Finding

The Tribunal found that York Timbers had not established that SAFCOL had refused to supply scarce goods to a competitor in contravention of section 8(d)(ii) of the Act. York Timbers also failed to establish that the reduction in guaranteed supply constituted an exclusionary act in contravention of section 8(c). The Tribunal noted that this was a contractual dispute that was of no concern to competition law.

The Tribunal's finding was confirmed on appeal by the Competition Appeal Court.