February 2006 Rob Petersen SC

‘Prohibited price discrimination’ after the CAC decision in the Sasol / Nationwide Poles case

Lecture 1 (of 4)

Overview of the policy of the S.A. law on ‘prohibited price discrimination’: the elements of the prohibition, *onus* and defences

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1. It is widely thought, after the decision of the Competition Appeal Court (‘CAC’)[1] in favour of Sasol Oil[2] in the case brought by Nationwide Poles,[3] that it will be practically impossible in future to prosecute successfully cases of alleged prohibited price discrimination under the Competition Act. Apart from general educational purposes, my main object in volunteering to give these lectures is to combat that belief. In doing so, I propose to use the facts disclosed by the record in the case to illustrate key aspects of the subject of ‘prohibited price discrimination’ generally, and also put forward my own views based on some research of the issues, and my reading of the judgments of the Tribunal[4] and the Court, for you to consider and debate.

2. As you no doubt know, the case concerned the different prices charged by Sasol’s Carbo-Tar division to different customers, for a creosote product derived as a by-product from the production of

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[1] Case No. 49CACApr05; judgment 13 December 2005.

[2] Hereafter simply ‘Sasol’ — a wholly-owned subsidiary of Sasol Limited.

[3] Nationwide Poles CC, represented in the proceedings by its member, Mr Jim Foot.

[4] Case No. 72/CR/Dec03; decision and reasons 31 March 2005.

liquid fuels. The particular product is called 'Sak K'. 'Sak K' is described as 'A wax improved wood preservative for industrial use consisting of medium temperature creosote in an admixture with waxy oil.' Over a number of years 'Sak K' had been purchased and used by Nationwide Poles in producing treated pine building and fencing poles, primarily for use in vineyards.

3. The pricing policy applied by Sasol to this product, supplied to customers in tanker-loads, was no different from that applied by Sasol to its tanker-loads of creosote without the wax additive.

4. The decision of the CAC in favour of Sasol turned, in fact, on quite a narrow point. For what my view is worth, I happen to think that the Court was wrong on that point, for reasons which I will put forward mainly in the fourth lecture. That was very unfortunate for Nationwide Poles and Mr Foot, who had fought a tenacious struggle, representing himself with ability and courage in both forums. Nevertheless, there is much in the rest of the judgment of the CAC which gives grounds for comfort that section 9 of the Act has not been made a dead letter. And the point itself, on which the decision ultimately turned, need not greatly obstruct future cases, as I shall in due course try to show.

5. This was the first case of alleged prohibited price discrimination to be fully canvassed in proceedings before the Tribunal. This is an inherently difficult and controversial area of competition economics and law. It involves international comparative learning. The case was hard-fought in almost all its potential aspects on both sides. It thus provides a valuable object of proper study. But such a study is not an easy task. Economic and legal arguments were interwoven with the factual evidence throughout the proceedings. The record of the

proceedings is voluminous — the documentary bundles alone, including experts' opinions, exceed one thousand pages; the transcript of the evidence heard over five days runs to more than nine hundred pages; and detailed heads of argument covering many more issues than were addressed in the judgments were of course prepared, both in the Tribunal and for the CAC.

6. In making use of evidence in the case, I shall avoid areas of factual dispute and rely only on facts which were put forward by Sasol itself or which were common cause, taken together with facts which (while not admitted) seem beyond serious dispute.

Background to the Tribunal proceedings

7. This was, as you know, a private referral by the complainant in terms of section 51(1) of the Act, after the Commission, having investigated the complaint, had issued a notice of non-referral.[5] It seems to me that the Commission's evaluation of the matter was rather perfunctory and, as it played no further part in the matter, I shall not go into it. According to the concise statement of the complaint as formulated by Nationwide Poles,[6] Sasol was engaging in prohibited conduct in contravention of section 9 of the Act in that it —

> … is a dominant supplier, selling, in equivalent transactions, goods of like grade and quality to different purchasers and discriminating by way of price or discount allowed between those purchasers, Further, that this discrimination is likely to have the effect of substantially lessening or preventing competition.

This was the essence of the case.

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[5] Competition Commission file number 2003Apr458. Complaint submitted 30 April 2003; notice of non-referral 12 November 2003.

[6] Form CT1 (2), 3 December 2003.

8. It was common cause that, during the period covered by the complaint, Sasol applied to its bulk sales of 'Sak K' a price list which differentiated per tonne,[7] not according to the number of tonnes of the product *actually purchased* by the customer in the transaction concerned, but according to the number of tonnes of the product *previously* purchased by the same customer and projected forward by way of an annualised estimate. According to the evidence of Mr J. S. van Wyk of Sasol, this exercise was performed once every three months, taking each customer's previous three months' purchases into account. Depending upon the annualised figure resulting, the appropriate price band would be applied to the customer in respect of *all* its purchases during the following three months — whatever the actual volume of such purchases might be. I shall return to the significance of this particular pricing structure several times.

9. A table presented in Sasol's heads of argument to the CAC shows the price differentials applied to 'Sak K' during the periods 2002-2003 and 2003-2004 respectively, together with calculations showing the extent of the differential between bands:

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[7] The words 'ton' and 'tonne' are used interchangeably throughout the record to refer to the same metric quantity.

2002-2003				
Customer's historical volume in tonnes p.a.	**SAK K current price per tonne (excl VAT)**	**Additional amount per tonne relative to lowest price**	**Additional % relative to lowest price**	**% Discount relative to highest price**
>5500	R1 600,00			16,32%
3601-5500	R1 638,00	R38,00	2,38%	14,33%
2501-3600	R1 660,00	R60,00	3,75%	13,18%
1001-2500	R1 700,00	R100,00	6,25%	11,09%
451-1000	R1 780,00	R180,00	11,25%	6,90%
0-450	R1 912,00	R312,00	19,50%	
2003-2004				
Customer's historical volume in tonnes p.a.	**SAK K current price per tonne (excl VAT)**	**Additional amount per tonne relative to lowest price**	**Additional % relative to lowest price**	**% Discount relative to highest price**
>5500	R1 928,00			15,29%
3601-5500	R1 974,00	R46,00	2,39%	13,27%
2501-3600	R2 000,00	R72,00	3,73%	12,13%
1001-2500	R2 049,00	R121,00	6,28%	9,97%
451-1000	R2 127,00	R199,00	10,32%	6,55%
0-450	R2 276,00	R348,00	18,05%	

10. Similar differentials, on the same historical-volume basis, were applied by Sasol to bulk sales of creosote without the wax additive. You can see from the table that the smallest purchasers (in terms of historical volume) faced over a period of years a price some 18-20% higher than that faced by the largest. It seems clear, therefore, that <u>the extent of the difference</u> per tonne of creosote between the highest and lowest price applied <u>was substantial</u>, and that such difference was not episodic but was sustained over <u>a substantial period of time</u>.

Section 9 and its interpretation

11. You should all have section 9 of the Competition Act before you, so I shall run through its provisions very quickly. The section is divided into two parts. Sub-section (1) sets out the essential elements of the prohibition against price discrimination by a dominant firm.

Whoever prosecutes a complaint under section 9 bears the *onus* (burden) of proving on a balance of probabilities the existence of each of the following elements —

11.1 that the firm selling the relevant goods or services is 'dominant' in the relevant market in which those goods or services are sold;[8]

11.2 that the goods or services are 'of like grade and quality';[9]

11.3 that they are sold in 'equivalent transactions' to different purchasers;[10]

11.4 that the transactions involve 'discriminating' between those purchasers in terms of:[11]

11.4.1 the price charged for the goods or services;

11.4.2 any discount, allowance, rebate or credit given or allowed in relation to the supply of the goods or services;

11.4.3 the provision of services in respect of the goods or services; or

11.4.4 payment for services provided in respect of the goods or services; and

11.5 that the discrimination is 'likely to have the effect of substantially preventing or lessening competition'.[12]

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[8] See the preamble to section 9(1).

[9] See paragraph (*b*) of section 9(1).

[10] *Id.*

[11] See paragraph (*c*) of section 9(1).

[12] See paragraph (*a*) of section 9(1).

12. Sub-section (2) then provides for certain special defences. They are special defences in the sense that, even where all the elements in sub-section (1) have been proved, the respondent firm may avoid the conclusion that its discriminatory conduct is '<u>prohibited</u> price discrimination' by proving on a balance of probabilities —

    (a) that the differential treatment of the purchasers of the goods or services makes only 'reasonable allowance for differences in cost or likely cost' of the manufacture, distribution, sale, promotion or delivery resulting from the differing:

    - places to which;
    - methods by which; or
    - quantities in which

    the goods or services are supplied to different purchasers;[13] or

    (b) that the differential treatment of the purchasers of the goods or services is constituted by 'doing acts in good faith to meet a price or benefit' offered by a competitor;[14] or

    (c) that the differential treatment of the purchasers of the goods or services is in response to certain changing conditions affecting the market for the goods or services concerned, more particularly the perishing or obsolescence of goods, or the discontinuation or liquidation of the business.[15]

13. There is obviously a lot of material for interpretation and disputation in section 9. What was the legislature after in enacting this

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[13] See paragraph (*a*) of section 9(2).

[14] See paragraph (*b*) of section 9(2).

[15] See paragraph (*c*) of section 9(2).

prohibition? It is best to orient ourselves first by way of a general overview.

Comparative overview

14. Our Competition Act has not been the first to introduce a prohibition on ‘price discrimination’. In this instance as in many others, it draws heavily on the competition-law (or ‘antitrust’) legislation and experience of other jurisdictions, most notably the United States and what is now the European Union. The Courts have warned against simply transposing into the interpretation and application of our Competition Act conclusions reached there. They say our Act must be interpreted primarily with reference to its own language,[16] its preamble and stated purpose,[17] and in the light of South Africa’s particular economic and social circumstances. While, in interpreting and applying the Competition Act, appropriate foreign and international law may[18] (and very often ought) to be considered, it is nonetheless necessary, as Reyburn says, ‘to view the competition laws of other countries in their proper historical, social and institutional contexts’.[19] The same applies to competition economics and policy, which in this field come together with law. As was held by the CAC in the Mondi-Kohler merger case,[20]

> care must be taken before an uncritical borrowing of traditional anti-trust economic theories, as developed in the United States of America, encrust the process of interpretation of our Act. Unlike much comparative competition law, the Act specifies … [*as part of the overall purpose*] of

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[16] Cf *Standard Bank Investment Corporation Ltd v Competition Commission and others; Liberty Life Association of Africa Ltd v Competition Commission and others* 2000 (2) SA 797 (SCA) at 814F-815A.

[17] Section 2.

[18] Section 1(3).

[19] *Competition Law of South Africa* (Issue 5) page 2–4.

[20] *Mondi Ltd and Kohler Cores and Tubes (a division of Kohler Packaging Ltd) v Competition Tribunal* [2003] 1 CPLR 25 (CAC) at 35-36.

> the maintenance of competition, that small and medium size businesses have an equitable opportunity to participate in the economy and that there be promotion of a greater spread of ownership, in particular to increase the ownership stake of historically disadvantaged persons (section 2(*e*) and (*f*) of the Act).[21]

Jerome Wilson and I appeared as *amici curiae* at the request of the Court in that matter, and the judgment essentially adopted in this regard a submission which we had made. However, this local cautionary note should not be overplayed. It was the intention of the legislature in enacting the Competition Act to bring South Africa into the global mainstream of competition law and policy, not to keep it isolated in national particularism. As David Unterhalter puts it in the book of Brassey (*et al*) on *Competition Law*:[22]

> Our competition law is underdeveloped. There is a growing recognition that the convergence of competition laws is a virtue, and there is a strong common discourse that binds competition lawyers in the jurisdictions from which our competition law is drawn. The conceptual foundations of the substantive portions of our Act are to be found in the international mainstream. We should not allow the development of our competition law to be an eccentric local curiosity, responsive to special interests and purposes that bear no reasoned connection to the theoretical underpinnings of the concepts that we have adopted in our Act.

15. I would say, therefore, that where the <u>reasoning</u> underlying a particular legislative provision or decision of a foreign jurisdiction resonates also in our conditions, and is reconcilable with the evident purpose and wording of our legislation, it ought to be persuasive here. It is with this in mind that one ought to approach the interpretation and application of section 9 of the Competition Act.

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[21] Cf also *Federal-Mogul Aftermarket Southern Africa (Pty) Limited v Competition Commission* (decision of the CAC, Case Number 33/CAC/Sep03, 23 September 2004), pages 5-6.

[22] Page 181.

What is meant generally by the expression 'price discrimination?

16. In the third lecture, I shall be discussing the particular meaning of the word 'discriminating' intended by the legislature where it appears in section 9(1)(*c*). But first, in the context of a more general overview, we need to know what economists and competition lawyers mean generally by the expression 'price discrimination'. A crisp statement is provided by Herbert Hovenkamp:[23]

> Price discrimination occurs whenever a seller has two different rates of return on different sales of the same product.

Hal R. Varian gives a more detailed explanation in the *Handbook of Industrial Organization*:[24] He explains that different prices charged to different customers may not involve any real discrimination, because, for example, different costs (such as transport costs) may be involved; conversely, there may be underlying discrimination where the same final price is charged. He thus prefers Stigler's (1987) definition:

> … price discrimination is present when two or more similar goods are sold at prices that are in different ratios to marginal costs. … Of course, this definition still leaves open the precise meaning of 'similar', but the definition will be useful for our purposes. …[25]

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[23] *Federal Antitrust Policy: The Law of Competition and its Practice,* 2nd edition, page 179.

[24] Schmalensee and Willig, eds., pages 598-600.

[25] Varian adds:

'The traditional classification of the forms of price discrimination is due to Pigou (1920).

'*First-degree*, or *perfect* price discrimination involves the seller charging a different price for each unit of the good in such a way that the price charged for each unit is equal to the maximum willingness to pay for that unit.

'*Second-degree* price discrimination, or *nonlinear* pricing, occurs when prices differ depending on the number of units of the good bought, but not across consumers. That is, each consumer faces the same price schedule, but the schedule involves different prices for different amounts of the good purchased. Quantity discounts or premia are the obvious examples.

'*Third-degree* price discrimination means that different purchasers are charged different prices, but each purchaser pays a constant amount for each unit of the good bought. This is perhaps the most common form of price discrimination; examples are student discounts, or charging different prices on different

'Price discrimination' ***per se*** **is not prohibited**

17. Now, it is important to emphasise that the Competition Act does not aim to prohibit price differentiation or 'price discrimination' in general. As was rightly argued on Sasol's behalf, to do so would be absurd. One only has to think about this concretely. The necessity in general of allowing and indeed encouraging price differentiation — including 'price discrimination' which involves different relations between price and marginal cost — cannot be seriously disputed. It is essential to competition and consumer welfare. The ability of suppliers to maximise output and achieve economies of scale; the ability of individual customers to bargain for lower prices from suppliers; the ability of suppliers to meet or beat their rivals' prices to customers — all these depend vitally on the freedom of suppliers to change their prices flexibly and, in doing so, charge different prices to different customers in respect of comparable sales over various periods of time and in various places.

18. However, it does not follow from this that price discrimination is either wholly beneficial or always beneficial at all. If there is a single idea that you carry away from this lecture, let it be the distinction between *sporadic* price discrimination and *persistent* price discrimination. It is the most useful tool in the proper analysis of price discrimination cases.

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days of the week.'

All fixed classifications have their limits. At first glance, the complaint of Nationwide Poles against Sasol may seem to have involved price discrimination of the second kind: different prices for different quantities purchased — but as we have just seen, it was not quite as simple as that. It involved different prices based not on the quantities actually purchased by the different customers, but on quantities *previously* purchased by them — irrespective of the quantities purchased to which the prices were applied. Contrary to what was suggested to the CAC, therefore, it was not an ordinary discount for quantities purchased (cf the appellant's heads of argument, par 1.11). It does not fit comfortably within any of the three categories defined by Pigou. Nevertheless, price discrimination is what it is.

19. Some passages from the authoritative American work *Federal Antitrust Policy: The Law of Competition and its Practice*[26] by Professor Hovenkamp will serve to illustrate and explain both the beneficial and the potentially harmful features of price discrimination at a general level:

> [First:] Price discrimination would not occur in a perfectly competitive market in equilibrium. Any purchaser asked to pay a price above marginal cost would walk away from that seller and find someone willing to sell at the competitive price. In such a hypothetical market all sales would be made at marginal cost.[27]
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> In the real world markets are in constant flux, however. They are shocked regularly by wars, famines, fads, elections, and the weather. Further, no one has complete knowledge of all market conditions at any given time, and different buyers and sellers have different amounts and kinds of information. As a result, sporadic price discrimination is a daily occurrence in even the most competitive markets. One day a farmer may sell corn for $4.00 a bushel.[28] During the night news breaks about a particularly large harvest in a different state and several buyers decide to postpone their purchases. The first buyer who appears in the morning and the farmer himself may not know of the news, and they will complete a sale at $4.00. Later in the day, however, the second and third customers walk away. Eventually the farmer learns that the market price has dropped to $3.70. He sells to the next customer at that price. He has discriminated between two purchasers on the same day; however, this is an absolutely common occurrence in the most competitive of markets. …
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> Competitive markets change constantly not only through time, but also in space. Suppose that firm A sells in three cities. In one of them a competitor opens a new plant and the immediate result is a large supply in that city in relation to demand. The price in that city will drop first, and the price in the other two cities will drop some time later. Likewise, if there is a sudden surge of demand in one city the immediate result will be a price increase there, which will encourage more of the product to flow into that city until the balance between supply and demand is restored once again. Competitive markets *tend* towards an equilibrium in which all sales are made at marginal cost. In the process of arriving at that equilibrium, however, a certain amount of price discrimination is essential. The low price in Chicago and the high price in St. Louis causes goods to flow from Chicago to St. Louis until the balance is once again

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[26] See note 23 *supra.* In all quotations, emphasis in bold or underlined type has been added .

[27] [I shall leave aside discussion of this concept, and the problem of profit, or the relation between normal profit and ‘marginal cost’, in the hypothetical situation posed — RP.]

[28] [A bushel is a dry measure of 8 gallons — RP.]

restored. If the seller is forbidden from raising prices in response to increased demand in St. Louis, unless she also raises prices in Chicago where demand has not increased, the result will be shortages in one city and surpluses in the other.

The kind of price discrimination characteristic of competitive markets is usually termed *sporadic* because it varies daily and is often unpredictable. One day a particular buyer will be favored, the next day disfavored. By contrast, *persistent* price discrimination occurs when a seller with market power systematically divides customers into classes and obtains different rates of return from them.

The complete absence of sporadic price discrimination in a market is not a sign of healthy competition. Much more likely, the firms in the market are coordinating their prices. … *[S]poradic* price discrimination is generally consistent with competition on the merits and inconsistent with cartelization. Indeed our concern with collusion often causes us to favor markets where purchases are negotiated individually and privately, so that cartel members cannot verify the terms of sale. The sporadic price discrimination that results can upset the cartel or oligopoly.[29] …

Sporadic price discrimination is an everyday occurrence in competitive markets. **However, persistent price discrimination requires that a seller (or group of sellers) have market power.** Price discrimination is persistent when a seller or group of sellers establish a policy of obtaining a higher rate of return from some customers than from others. In a competitive market disfavored purchasers will simply seek out a different seller willing to sell to them at a competitive price.[30] …

All forms of **persistent** price discrimination transfer wealth away from consumers and towards sellers. **If antitrust policy is concerned with such wealth transfers, then price discrimination presents an antitrust problem.**

> [In this regard I recommend you read Sullivan and Grimes *The Law of Antitrust: An Integrated Handbook* (2000) pages 12-16. (— RP)] [31]

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[29] Pages 566-567. 'Oligopoly' is defined in *Webster's Third New International Dictionary* as 'a market situation in which each of a limited number of producers is strong enough to influence the market but not strong enough to disregard the reaction of his competitors… .'

[30] Page 567.

[31] Sullivan and Grimes *The Law of Antitrust: An Integrated Handbook* (2000) say on pages 12-16, dealing with the economic and social goals of antitrust policy: 'These goals generally fall into four categories: (1) consumer welfare goals, including the efficient allocation of existing resources and avoiding wealth transfers to participants with market power; (2) fostering innovation and technological progress; (3) protecting individual firms through fairness and equity goals; and (4) maintaining decentralized economic power.' Dealing with price discrimination, they say (pp 487-488): [E]very price discrimination will result in a transfer of wealth from the buyers that pay the higher price to the seller whose market power allows the imposition of the discriminatory price. … In real markets, a seller will impose price discrimination only when it increases the seller's profits. Hence, there will always be a wealth transfer loss if price discrimination does not increase output. **Preventing that wealth transfer**

> **The question is more complex** [*Hovenkamp continues*] **if economic efficiency is the exclusive goal of the federal antitrust laws.** Some commentators have argued that price discrimination should not be an antitrust concern because it does not produce losses in output as other monopolistic practices do.[32] **As noted earlier, however, only perfect price discrimination maintains output at the competitive level. Under imperfect price discrimination output is always lower [and perfect price discrimination never exists in the real world].**[33]
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> > [Richard Posner *Antitrust Law,* 2nd edition, pages 82-83, makes much the same point, adding: 'Many economists believe that [even] imperfect discrimination is more likely to expand than to reduce output, … **but there is not a firm basis for this belief**.' Posner is a former law professor and for many years has been a U.S. Court of Appeals judge. (— RP)] [34]
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> Further, [says Hovenkamp] price discrimination can generate substantial social losses, equivalent to the efficiency losses that can result from all forms of monopoly. First is the deadweight loss caused by a reduction in output. **Since all imperfect price discrimination results in output at less than the competitive level, and all real world price discrimination is imperfect, it necessarily follows that persistent price discrimination produces a certain amount of deadweight loss.** … [35]

Posner adds: [36]

> Still another inefficiency created by price discrimination even if perfect is distortion in the costs of the customers of the discriminating seller. They pay different prices for inputs that cost society the same to produce. They thus are confronted by false alternatives from the standpoint of minimizing overall social costs, and this may lead them to substitute inputs that cost society more to produce—just as in any case of single-price monopoly.'

Later in the same work Posner says: [37]

> '[P]rice discrimination impairs efficiency in the market in which the

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loss is a primary if not the preeminent goal of antitrust.'

[32] Hovenkamp cites as an example: R. Bork, *The Antitrust Paradox: A Policy at War With Itself* (1978 rev. ed. 1993) pages 394-398. Compare also Daniel Clough 'Law and Economics of Vertical Restraints in Australia', in [2001] *Melbourne University Law Review* 20.

[33] Page 568.

[34] Posner cites Jean Tirole, *The Theory of Industrial Organization* 152-158 (1988); Hal R. Varian, 'Price Discrimination,' in *Handbook of Industrial Organization*, vol 2, pages 597, 629-633; and Robert Wilson, *Nonlinear Pricing* (1993) pages 8-9.

[35] Page 569.

[36] *Op. cit.,* page 86.

[37] Page 203.

> purchasers from the discriminating seller sell by creating competitive cost disparities unrelated to differences in the relative efficiency of the competitors.'

Both Posner and Hovenkamp are, broadly speaking, adherents of the 'Chicago School'.

20. Despite his observations on the harm done by persistent price discrimination, Hovenkamp is firmly of the opinion that a prohibition on 'price discrimination' tends to do more harm than good.[38] He considers that the social costs of preventing price discrimination even by firms with market power, where there is no accompanying exclusionary conduct, would almost certainly outweigh any social benefits. Thus even where a market is oligopolistic, his view is that a policy of preventing price discrimination may actually serve to perpetuate supra-competitive prices. (He is speaking, of course, mainly with the United States in mind.) Posner, who (like Hovenkamp) is a critic of that country's Robinson-Patman Act, holds much the same view:

> It would be infeasible to draft a decree forbidding systematic price discrimination that did not constrain or inhibit legitimate pricing behavior as well. Such a decree would be a little Robinson-Patman Act.[39]

I shall deal later in more detail with the very wide ambit of the Robinson-Patman Act and decisions in terms of it.

21. In Australia, section 49 of the Trade Practices Act 1974, which contained a prohibition against price discrimination (like the Robinson-Patman Act, not confined to firms with market power),

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[38] *Id.,* pages 570-571. See also Hovenkamp 'The Robinson-Patman Act and Competition: Some Unfinished Business', 68 *Antitrust Law Journal* 125 (2000).

[39] *Op. cit.,* page 86.

was repealed in 1995.[40] New Zealand has not enacted any prohibition against price discrimination. Nevertheless, not only in the United States, but also in Canada and the European Union, variously worded legislative prohibitions against price discrimination persist. Our section 9 does not stand in isolation.

22. In the Nationwide Poles / Sasol case, the CAC made it clear that it is unimpressed by the general argument that prohibitions on price discrimination do more harm than good. It quoted,[41] with reference to the United States, the comment of the American Antitrust Institutes Working group on the Robinson-Patman Act (July 1, 2005):

> We do not believe it will be fruitful or constructive for the Commission to recommend repeal or radical revision of the Robinson Patman Act. Instead, we recommend that the Commission propose **three major reforms. These changes would bring the Act more in line with the other anti trust laws without abandoning its fundamental purpose.** Indeed, they would refocus secondary line price discrimination cases [*I shall deal later with what this means*] on their original objective — protecting small firms from price differentials that reflect a large firm's buying power rather then cost savings. More generally, they would put the Act on a sounder economic footing, differentiating more clearly between anticompetitive and pro competitive uses of the Act while preserving its ability to halt discrimination that poses a substantial and unjustified threat to small business or consumers.[42]

23. An expert report by G:enesis, submitted to the Tribunal on behalf of Sasol placed great stress on the idea that 'the economic literature' emphasises 'the pro-competitive impact' of price discrimination in input markets.[43] But as we have just seen, that would be a somewhat one-sided depiction of the relevant writings, even in the United

[40] By the Competition Policy Reform Act.

[41] Page 24.

[42] [My emphasis — RP.]

[43] Second G:enesis report, page 15 (Supplementary Bundle, page 71).

States. The report suggests — and here I would agree with them — several particular reasons why prohibiting price discrimination is likely to have certain anti-competitive effects:

- *Buyers' incentive to bargain is weaker.*[44] If, by law, upstream firms are not able to charge lower prices to firms with greater bargaining power, this will strengthen upstream firms' bargaining power vis-à-vis larger buyers. If the upstream firm offers price discounts to the larger buyer, prohibition will mean that it must offer the same price discount to all other firms. This decreases the incentive of all downstream firms to bargain (directly or indirectly), because all their competitors receive any price that they receive. In concentrated markets with high barriers to entry the main threats to upstream firms' market power is the bargaining power of larger buyers.[45]
- *Buyers may be more adept at sourcing product elsewhere.*[46] Downstream buyers that find an alternative source for their input or invest in a process that can more easily substitute away will give the upstream firm an incentive to lower the price it charges them. The lower price in effect rewards pro-competitive actions by downstream firms.
- *A fall in the effectiveness of distribution.* Differential pricing allows upstream firms to encourage firms that are more effective at selling. For instance suppliers can offer volume discounts to firms that are particularly effective at driving sales. Such discounts provide incentives for downstream firms to compete more aggressively to gain bigger discounts, thus increasing competition.[47]

24. As general postulates these may be unobjectionable — but in our situation they surely fall short of a case. I say this not merely because the South African legislature, in its wisdom, has decided to prohibit price discrimination in certain circumstances despite such points. More fundamentally, I think, the general argument that *any* prohibition on price discrimination will ultimately do more harm than good to consumers is seriously flawed. It is flawed insofar as it

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[44] G:enesis cites Trebilcock, Winter, Collins and Iacobucci (2002), *The Law and Economics of Canadian Competition Policy,* Chapter 5.

[45] G:enesis adds: 'Technological change is another major threat to market power.'

[46] G:enesis cites Trebilcock *et al* (*supra*), Chapter 5.

[47] G:enesis cites Wu, L (2004), 'Economics of Antitrust, new issues, questions, and insights', Nera Economic Consulting.

takes as its unspoken premise economic conditions in which firms with market power *stand to gain more by expanding output than by limiting it* —where, in other words, purchasing capacity all the way downstream to the ultimate consumer provides an adequate incentive for such suppliers to engage in vigorous price competition with each other despite a situation of oligopoly (or even duopoly) prevailing between them. This is an assumption which, while it may arguably have substance in the present-day United States — I shall not enter into that — is not generally tenable in South African conditions.

25. Similar considerations have been raised and dealt with in this country in the context of evaluating vertical mergers. They need to be borne in mind whenever the rationale behind the Competition Act has to be considered. In the *Mondi-Kohler* case already referred to, Jerome Wilson and I made in this regard the following observations in our written submissions as *amici curiae* to the CAC:[48]

> Every prevalent social attitude reflects a stage in historical and socio-economic development, and has its corresponding legal reasoning. In the United States, the advance of the ideas of the 'Chicago School' in regard to vertical mergers marked a move away from earlier policies which sought to protect small businesses against the greater efficiencies and other advantages achievable by the big players through vertical concentrations. Hence the attack on the *Brown Shoe* judgment [1962][49] as protecting competitors rather than competition. In that case the court had found that the tendency of manufacturers to become an increasingly important source of supply for their acquired retail outlets had as a necessary corollary the foreclosure of the independent manufacturers from markets otherwise open to them. The tendency of such vertical mergers to bring ever greater numbers of retail outlets within fewer and fewer hands was held *per se* to produce 'anti-competitive' effects on the horizontal plane, and was accordingly condemned. Such a standpoint faced towards the golden age of the small proprietor and small-scale entrepreneur. As a practical matter, it could not be sustained under U.S. and global competitive conditions as they were actually developing.

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[48] Submissions dated 22 September 2002.

[49] *Brown Shoe Co. Inc. v. United States* 370 U.S. 294.

> Conditions change law more than law changes conditions. The big corporations lean on the interests of 'consumers' for their justification — and they are often right.[50]

However (we went on to say), the retarded development of the South African economy, the relatively restricted and impoverished consumer market and the highly concentrated and distorted structure of ownership mean that what may be persuasive as a matter of economic logic in the United States does not necessarily carry similar weight here — despite the greatly increased pressures towards efficiency resulting from globalisation. Davis JP, giving the

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[50] Par 5 of the submissions. Compare what is said by Sullivan and Grimes *The Law of Antitrust: An Integrated Handbook* (2000), pages 15-16:

‘The populist goal of preventing the growth of big business motivated many supporters of the Sherman Act [1890] and still had some force during the activist period of antitrust enforcement that lasted into the 1960s. In *United States v. Aluminum Co. of America*, Judge Learned Hand wrote: “It is possible, because of its indirect social or moral effect, to prefer a system of small producers, each dependent for his success upon his own skill and character, to one in which the great mass of those engaged must accept the direction of a few.” [148 F.2d 416, 427 (2d Cir. 1945.] Picking up on this theme, Chief Justice Warren wrote in 1962: “[W]e cannot fail to recognize Congress’ desire to promote competition through the protection of viable, small, locally owned businesses. Congress appreciated that occasional higher costs and prices might result from the maintenance of fragmented industries and markets. It resolved these competing considerations in favor of decentralization. We must give effect to that decision.” [*Brown Shoe Co. v. United States* 370 U.S. 294, 344.]

‘As allocative efficiency became a more dominant goal of antitrust, the goal of maintaining a decentralized economy lost force. The internationalization of markets has reenforced this change. As major U.S. industries lost ground in competition with foreign rivals, it became clear that the efficiency of American firms should be a priority in crafting antitrust policy. A second consideration was the difficulty in formulating a workable test for pursuit of a decentralization goal: unless all moves toward concentration were to be condemned, courts were faced with an impossibly subjective balancing of how much lost efficiency should be tolerated in order to maintain dispersed economic power.

‘Nonetheless, the inherent power of the Jeffersonian ideal of dispersed economic power has not disappeared entirely from antitrust. For example, merger enforcement policy still is based on an incipiency standard: Section 7 of the Clayton Act forbids increases in concentration that “may” substantially reduce competition. [15 U.S.C.A. § 18.] Although recent iterations of federal merger guidelines have shifted to allow greater levels of concentration, a premise of these guidelines remains that trends toward concentration are to be halted in their incipiency—well before levels of monopoly power are reached. In the merger guidelines the federal enforcement agencies have found objective bases for determining how great a risk of reduction is sufficient by considering concentration ratios and entry barriers, and focusing on whether the risk of price fixing is noticeably increased by the structural change caused by the merger. The incipiency standard serves the goal of maintaining dispersed economic power and is also consistent with the consumer welfare goals of avoiding deadweight and wealth transfer injuries. The goal of maintaining dispersed economic power may still serve as a tiebreaker in much the same way as the goal of protecting an individual firm’s right to compete.’

See also John E. Kwoka, Jr. and Lawrence J. White, *The Antitrust Revolution: Economics, Competition, and Policy* (4th edition), pages 1-5.

judgment of the CAC in that case, essentially upheld this argument,[51] directly adopting our submission when he said:

> The idea that a monopolist may decrease prices when its costs are reduced depends on an assumption that the monopolist can preserve or increase profit by way of increasing the volume of sales at the lower price. **This practice might well be successful within the context of a vast continental market with a mass of affluent customers, but, in a less developed economy with a limited market afflicted by monopoly [or] oligopoly, this form of generalisation was less likely to hold.** …

It seems unlikely that the CAC will depart from this general approach in any matter where similar issues of economic rationality and overall policy come into play in the interpretation and application of the Competition Act.

26. Nevertheless, we need to bear in mind that a less developed country does not simply follow the path trodden by those that have gone before. On the one hand there can be protracted stagnation; on the other, an acceleration and combination or telescoping of stages, thanks in part to the internationalisation of experience as well as the qualitatively altered global environment in which the later development takes place.

27. The protection of small businesses against persistent price discrimination is necessary and progressive inasmuch as it facilitates the emergence and growth of vigorous competitors where effective competition has hitherto been lacking. Significantly, in the *Nationwide Poles* judgment, Davis JP quoted with approval[52] the following remarks of the chair of the Korean Competition Advisory Board (referred to in an article by Prof Eleanor Fox):

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[51] Page 33*d-h*.

[52] Page 27.

> In a developing economy where, incipiently, economic power is not fairly distributed, competition policy must play the dual role of raising the power, within reasonable bounds, of underprivileged economic agents to become viable participants in the process of competition on the one hand, and of establishing the rules of fair and free competition on the other. If these two objectives are not met, unfettered competition will simply help a handful of privileged big firms to monopolize domestic markets …[53]

28. However, it is not the object of our competition law to protect small businesses generally against ordinary competitive pressures, i.e., for their own sake, where no abuse of dominance by big players is involved, and where there is no merger tending to restrict competition. It is in that sense that the often-quoted expression that competition law *'protects competition, not competitors'* retains its validity, hard as it may be upon the weak.

29. The South African legislature has adopted a much more cautious, far less sweeping prohibition of 'price discrimination' than was enacted by the Robinson-Patman Act of 1936 in the United States.[54] Two

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[53] I have truncated the quotation — RP.

[54] The Robinson-Patman Act amended the Clayton Act of 1914. In connection with the Robinson-Patman Act, references to 'section 2(*a*)' are in fact references to section 2(*a*) of the Clayton Act as amended. So far as is relevant for comparative purposes, that section provides as follows:

'It shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly, to discriminate in price between different purchasers of commodities of like grade and quality, where either or any of the purchasers involved in such discrimination are in commerce, where such commodities are sold for use, consumption, or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, and where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them; Provided, That nothing herein contained shall prevent differentials which make only due allowance for differences in the cost of manufacture, sale, or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered … And provided further, That nothing herein contained shall prevent price changes from time to time where in response to changing conditions affecting the market for or the marketability of the goods concerned, such as but not limited to actual or imminent deterioration of perishable goods, obsolescence of seasonal goods, distress sales under court process, or sales in good faith in discontinuance of business in the goods concerned.'

Section 2(*b*) expressly places the burden of proving a cost justification or other defence upon the person charged, once there is *prima facie* proof of price discrimination. Thus, despite important differences in wording and some differences in precise effect, there are certain key parallels with our section 9.

differences in particular stand out. First, the Robinson-Patman Act does not limit its prohibition against price discrimination to dominant firms (or firms having market power): the prohibition applies across the board. Second, it requires only that the effect of the discrimination 'may be' substantially to harm competition. These aspects are largely responsible for the poor reputation it has earned.[55] In South Africa, in contrast, firms which are not 'dominant' in the relevant market are allowed to practice price discrimination to their hearts' content. Moreover, even a dominant firm may practice price discrimination unless it is 'likely' to have the effect of substantially preventing or lessening competition.

30. 'Dominance' or market power, as illustrated by the Sasol / Nationwide Poles case is the subject of my second lecture. The likelihood of a substantial prevention or lessening of competition, and the problem of proving it, is the subject of the fourth. I shall therefore leave these matters at this point and turn briefly to the question of defences which section 9 makes available to a respondent facing a 'prohibited price discrimination' complaint.

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[55] According to Hovenkamp, *op. cit.,* pages 572-573, the Robinson-Patman Act—

> '… has done an extraordinarily poor job of identifying those forms of price discrimination that most economists consider to be inefficient. At the same time, it has often been used to condemn efficient practices that were really evidence of healthy competition. The Act has been widely castigated by critics who see it as doing far more harm than good to the competitive process. The Department of Justice has not enforced the Act since 1977, and the Federal Trade Commission has greatly reduced its enforcement as well.
>
> '…[P]ersistent price discrimination cannot occur unless the seller has market power. However, the Robinson-Patman Act does not require a showing of the defendant's market power. This failure, plus the fact that the "cost justification" defense has been very narrowly construed, has yielded a large measure of over-deterrence. Many defendants condemned by the Act were not monopolists engaged in true price discrimination at all. Their differential prices were either nondiscriminatory or else part of the normal give-and-take of the competitive market process. Alternatively, they were efforts by oligopolists to compete by "cheating" on the oligopoly price. By condemning the resulting discrimination, the Robinson-Patman Act effectively supported the oligopoly.'

Defences provided for in section 9(2)

31. Where there is proof on a balance of probabilities that the requirements of section 9(1) of the Competition Act are satisfied, the respondent may avoid a finding that its conduct amounts to prohibited price discrimination by establishing — likewise by proof on a balance of probabilities — one or more of the defences provided for in section 9(2). In the Sasol / Nationwide Poles case, no such defence was mounted.

32. Section 9(2)(*a*) allows the respondent to establish that the differential treatment of its customers —

> makes only reasonable allowance for differences in cost or likely cost of manufacture, distribution, sale, promotion or delivery resulting from the differing places to which, methods by which, or quantities in which goods or services are supplied to different purchasers.

In other words, Nationwide Poles would not be entitled to the same price as another customer while purchasing a smaller volume than that other customer; all it is entitled to (so far as section 9(2)(*a*) is concerned) is that the higher price which it pays is reasonably related to the higher cost per tonne of producing (etc) that volume.

33. Relating cost to quantity is notoriously difficult, and is sometimes thought impossible — but the section requires only that the allowance made be 'reasonable': it does not require that it be precise. The intended test, I think, is an elastic one, and proof of *bona fide* and reasonable efforts to allocate costs and accordingly to align price

differences with cost differences should usually be enough to discharge the *onus*.[56]

34. It appeared from the record that, in fact, Sasol had not carried out any exercise designed to establish the cost of any unit of supply, or the differential costs entailed in supplying different quantities of those units. Mr van Wyk explained the business rationale behind the pricing structure specifically as a means of preferring big customers over small ones, because having the bigger instead of the smaller made it easier for Sasol to plan its production and tended to reduce risk. The pricing policy thus produced business benefits.[57] But, of course, every pricing policy (if it is rational) is designed to produce business benefits for the seller, and so would be a policy of prohibited price discrimination — except for the disadvantage of getting caught. One may accept that all the risk factors, and cost factors, were indeed as stated by Mr van Wyk. The problem remained that they had never been quantified as cost differences in relation to any quantity of creosote supplied, so as to allow the reasonableness of the relation between quantity and price to be proved as contemplated in section 9(2)(*a*).

35. The evidence of Sasol's own expert witness, the economist Mr Malherbe,[58] frankly showed that there was really no possibility of mounting a section 9(2)(*a*) defence. His investigations and interviews with management had established that the price

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[56] It may well be that over-punctilious foreign precedents will not be followed here (cf Hovenkamp, footnote 55 *supra*). U.S. comparative case law on the cost justification defence is usefully summed up by the American Bar Association in *Antitrust Law Developments (Fifth)* (2002) pages 486-491.

[57] Transcript 6 August 2004, pages 313-314.

[58] Transcript 6 August 2004, page 451.

differences were not based on cost differences. It was because Sasol could disregard the risk of losing small customers that it could differentiate against them in price. [59] This is not to say that greater or lesser risk may not in principle be translated into greater or lesser 'likely' costs. But it is no easy matter to do that. The evidence did not get anywhere near the point where a reasonable allocation of costs to particular quantities of supply could be made.[60]

36. Furthermore, one must remember that the price differences were based not on the actual quantities supplied to which the prices were applied, but to quantities previously supplied (quite possibly at other prices). Thus, two customers buying the same quantity could pay substantially different prices per tonne, and two customers buying substantially different quantities could pay the same price per tonne. One may fairly conclude, I think, that it is impossible to bring differential pricing structured in that way within the defence offered by section 9(2)(*a*).

37. Apart from cost justification, section 9(2) provides another defence which might potentially apply in the ordinary course of business even of dominant firms. Section 9(2)(*b*) says that differential treatment of purchasers is not prohibited price discrimination if it is constituted

> by doing acts in good faith to meet a price or benefit offered by a competitor.

This provides potentially a very important absolute defence to a complaint of price discrimination. On U.S. comparative authority

[59] Transcript 6 August 2004, page 452.

[60] Cf the Tribunal's reasons for decision, par 138-139.

which seems to make practical sense, this defence would apply equally to good-faith responses aimed at keeping old customers and to those aimed at obtaining new customers.[61] It has been held that the defence is not limited to customer-specific responses, provided it is a genuine, reasonable response to prevailing competitive circumstances.[62] However, it must be a good-faith response not just to general competition in the market-place but to the equally low price of a competitor — otherwise the defence would (as American judges put it) 'virtually obliterate' the prohibition on price discrimination.[63]

38. Sasol was unable to invoke a defence of that kind in the present case. The complaint related to Sasol's standard discount structure, not for example to the once-off 2003 'Christmas special' — and, in any event, no evidence was presented either of its competitor Suprachem's prices from time to time or of Sasol's good-faith belief (in the absence of knowledge) as to what those prices were.

39. The case therefore turned, not on any of the defences provided for in section 9(2), but on whether, in the final analysis, Mr Foot had succeeded (where the *onus* clearly lay on him) in proving on a balance of probabilities:

    39.1 that Sasol was dominant in the relevant market, or had market power as a seller of creosote;

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[61] *Falls City Industries, Inc. v. Vanco Beverage, Inc.* 460 U.S. 428 (1983).

[62] *Id.*

[63] *Hoover Color Corp. v. Bayer Corp.* 199 F.3d 160, 164 (4th Cir. 1999). See generally *'Meeting Competition' defence under § 2(b) of Clayton Act, as amended by Robinson-Patman Act (15 U.S.C.A. § 13(b))* by Amy P. Bunk, J.D., 164 A.L.R. Fed. 633; American Bar Association *Antitrust Law Developments (Fifth)* (2002) pages 481-487.

39.2 that it discriminated in price against purchasers such as Nationwide Poles in respect of ‘equivalent transactions’; and

39.3 that this discrimination was likely to substantially lessen or prevent competition.

As you know, it was on the last point specifically that Sasol emerged ultimately successful in its defence of the complaint.

February 2006 Rob Petersen SC

‘Prohibited price discrimination’ after the CAC decision in the Sasol / Nationwide Poles case

Lecture 2 (of 4)

‘Dominance’ or market power as illustrated by the evidence in the case

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1. The CAC did not find it necessary to deal with this aspect of the matter, as it felt able to decide the case in favour of the accused party (Sasol) on the basis of section 9(1)(*a*) alone. The Tribunal, for its part, had concluded that Sasol was ‘dominant’ in the market for bulk supplies of creosote, having more than 45% of the market so defined. This finding was the subject of vigorous challenge on appeal, the argument going into considerable detail, to do with market definition and the substitutability of another chemical compound (CCA) for creosote, as well as other complex aspects requiring a thorough evaluation of the evidence that would take more than the time available to me merely to set out. I propose to approach the matter rather from the angle of normal analytical tests for ‘market power’, using aspects of the evidence regarding substitutability to illustrate the subject.

Market power and ‘dominance’

2. It is important to emphasise that being dominant in a market, or having market power, is not an offence. Competitors legitimately aim to defeat all rivals. Once a firm becomes dominant, however,

once it gains market power, it is required to conform to standards of conduct designed to prevent that power from being abused.

3. Section 9 of the Competition Act prohibits price discrimination only 'by a dominant firm, as the seller of goods or services'. Thus, section 9 does not concern itself directly with the ability of powerful buyers to extract lower prices from their suppliers than are made available to competing buyers. Where, for example, a large supermarket chain uses its market power to obtain prices from a captive supplier that are far lower than the prices made available by that supplier to small neighbourhood grocery stores or *spazas*, the supermarket chain could not be pursued by a complaint under section 9.[1] Whether a supplier to the chain could be so pursued would depend *inter alia* upon whether it is to be characterised as 'a dominant firm' in terms of the Competition Act.

4. Section 7 of the Act, as you know, provides that a firm is dominant in a market if—

   4.1 it has at least 45% of that market; or

   4.2 it has at least 35%, but less than 45% of that market, unless it can show that it does not have 'market power'; or

   4.3 it has less than 35% of that market, but has 'market power'.

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[1] There is a report prepared in 1981 by the UK Monopolies and Mergers Commission 'on the general effect on the public interest of the practice of charging some retailers lower prices than others or providing special benefits to some retailers where the difference cannot be attributed to savings in the supplier's costs'. The need for the report arose out of growing concern at that time in Britain over the increasing dominance of the great supermarket chains, and the declining viability of the corner grocer. In the course of some 256 pages of factual analysis and discussion, the Commission came to the conclusion that the result of this price discrimination was likely to be lower average prices to consumers, and declined to recommend legislation to prohibit it. The South African legislature may well have had similar considerations in mind when confining section 9 of the Competition Act to price discrimination by dominant sellers.

'Market power' is defined in section 1 of the Act as the power of a firm to control prices, or to exclude competition, or 'to behave to an appreciable extent independently of its competitors, customers or suppliers'.

5. Ordinarily, the analysis of whether a firm is dominant or not begins with a definition of the relevant market[2] — the latter being established by reference to a particular product or combination of products,[3] and by reference to the geographical area or areas within which buyers of those products are realistically confined and within which suppliers therefore compete for those customers.[4] By defining the relevant market, one can proceed to determine the firm's market share.[5] However, determining market share is only one route to establishing 'dominance'.

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[2] See generally *Antitrust Law Developments (Fifth)* by the American Bar Association (2002) — an exceptionally incisive and useful digest of authorities — pages 525-532.

[3] In *Massmart Holdings / Jumbo Cash and Carry (Pty) Ltd* [2001-2002] CPLR 193 (CT) (Case No. 47/LM/Aug01) par 8, the Tribunal said: 'The relevant product market comprises all of those products and/or services, which are regarded as interchangeable or substitutable by the consumer, by reason of the products' or services' characteristics, their prices and their intended use.'

[4] 'The geographic market is conventionally understood to refer to that geographic area to which consumers can practically turn for alternative sources of product and in which the antitrust defendant faces competition.' *JD Group Ltd / Ellerine Holdings Ltd* [1999-2000] CPLR 53 (CT) at 67*d-e* (Case No. 78/LM/Jul00).

[5] The need to define the relevant product and geographical market depends on the particular statutory context and the precise inquiry which the statute enjoins. Thus where so-called '*per se*' violations are alleged, involving neither proof of dominance nor an evaluation of anti- or pro-competitive effects, defining the relevant product and geographical market will ordinarily not be necessary. On the other hand, in *JD Group Limited and another in re: Competition Tribunal v JD Group Limited and another* [2004] 1 CPLR 31 (CAC) (Case No. 28/CAC/May03), at 36*i*-37*d*, the CAC criticised the failure of the Competition Tribunal, when evaluating a merger and the need for conditions to be attached to approval thereof, to provide a clear finding on the definition of the relevant market:

'This problem of market definition is not only common to South Africa. In *France v The Commission* (case no. 68–94, C–34/35, a judgment of the European Court of Justice given on 31 March 1998) the Court states: "A proper definition of the relevant market is a necessary precondition for any assessment of the effect of concentration on competition". Similarly, in a case which has been cited often by this Court and the Tribunal, *Brown Shoe Company v United States* (1962) 370 US 294, the court held: "Thus as we have previously noted: ' determination of the relevant market is a necessary predicate to a finding of a violation of the Clayton Act because the threatened monopoly must be one, which will substantially lessen competition within the area of effective competition. "Substantially" can be determined only in

6. The practical effect of section 7, with its somewhat arbitrary categorisations, is to alter the incidence of the burden of proof and the scope for rebuttal, depending on the market share which the firm concerned is proved to have. Because a firm having at least 45% of a market is irrebuttably presumed to be 'dominant' in that market, no mention of 'market power' in that connection is made. There can, however, be little doubt that, even in the absence of a definite finding as to a firm's market share, if it is shown in fact to have the power to behave to an appreciable extent independently of (say) its customers — if it is shown in other words to have captive customers — it will be held to be 'dominant' for the purposes (*inter alia*) of section 9.

7. Richard Whish *Competition Law* (5th edition) says:[6]

> The most important issue in competition assessment is whether a firm or firms have **market power**. … [M]arket definition provides a framework within which to carry out this assessment: market definition is not an end in itself. Indeed, there may be cases in which it is very difficult to separate market definition from the identification of market power itself: in some cases the two issues **may overlap**.

In fact the UK Competition Commission's merger reference guidelines which are cited by Whish go further:

> In practice the analysis of these two issues [the relevant market and market power] **will overlap significantly**, with many of the factors

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terms of the market affected'." See also *Lantec Inc v Novell* 2001 (146) F.Supp 2d 1140.'

However, in my view, this general observation by the CAC is a little too sweeping and in a case under section 9 of the Competition Act needs to be qualified. As I shall discuss later in more detail, whereas a substantial *lessening* (or likely lessening) of competition would be impossible to establish without a proper definition of the relevant market and a full evaluation of competition or likely competition within it, it is possible to establish the likelihood of a substantial *prevention* (in the sense of the *hindering* or *impeding*) of competition, at least in the secondary line, without the same exercise being required. Although any likely prevention of competition does come into consideration in merger evaluations (along with the likely lessening of competition), anti-competitive effects at every level along the offsetting effects of pro-competitive gains always have to be weighed in the balance. This makes unavoidable a definition of the market within which to identify and evaluate those effects. Section 9 of the Competition Act — in contrast with section 12A as well as sections 4(1)(*a*), 5(1) and 8(*c*) and (*d*) — makes no mention of offsetting or counter-weighing pro-competitive effects.

[6] Page 43.

> affecting market definition being relevant to the assessment of competition and vice versa. For instance, in contemplating the extent of supply-side substitution for the purposes of identifying the relevant market, it is likely that the potential for entry and expansion, a key issue in the assessment of competition, will also be considered. Therefore, market definition and competition assessment should not be viewed as two distinct, chronological stages – rather **they should be viewed as two overlapping analyses**.' [7]

Bishop and Walker *The Economics of EC Competition Law* (1999) say similarly:[8]

> … [T]he definition of the relevant market is **merely a tool for aiding the competitive assessment** by identifying those substitute products or services **which provide an effective constraint** on the competitive behaviour of the products or services being offered in the market by the parties under investigation.[9]

It must follow that, where the issue is simply *whether* market power exists, the 'mere tool' of market definition should not be treated as invariably indispensable.

8. Unfortunately, the Competition Tribunal has not always been entirely consistent on this point — there is not time now to read out all the references and quotations.[10] It is enough for present purposes for me to quote and agree with what the Tribunal said in *Natal Wholesale Chemists (Pty) Ltd v Astra Pharmaceutical Distributors (Pty) Ltd*:[11]

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[7] *Merger References: Competition Commission Guidelines* (June 2003, CC2), par 1.25.

[8] Page 47.

[9] See also Sullivan and Grimes *The Law of Antitrust: An Integrated Handbook*, page 91. Compare also *Patensie Sitrus Beherend Bpk v Competition Commission* [2003] 2 CPLR 247 (CAC) (Case No. 16/CAC/Apr02) at 257*c*.

[10] Compare *SAR (Pty) Ltd v SAD Holdings Ltd (1)* [1999-2000] CPLR 256 (CT) (Case No. 04/IR/Oct1999) page 261*e; DW Integrators CC v SAS Institute (Pty) Ltd* [1999-2000] CPLR 191 (CT) (Case No14/IR/Nov99) par 23; *Cancun Trading and others v Seven-Eleven Corporation* [1999-2000] CPLR 173 (CT) (Case No. 18/IR/Dec99) par 31; *Nationwide Airlines (Pty) Ltd v SAA (Pty) Ltd* [1999-2000] CPLR 230 (CT) (Case No. 92/IR/Oct00), at 234*h*; *Bidvest Group Ltd / Paragon Business Communications Ltd* [2001-2002] CPLR 119 (CT) (Case No. 56/LM/Oct01) page 128*h-I*; *Nuco Chrome (Pty) Ltd v Xstrata SA (Pty) Ltd and another* [2004] 2 CPLR 341 (CT (Case No. 31/IR/Apr04) at 352*b-e.*

[11] [2001-2002] CPLR 363 (CT) (Case No. 98/IR/Dec00), pages 376-377.

> We concur with the complainant that **the purpose of defining a relevant market is to identify the exercise of market power** [as] defined in the Act … and that market definition is only a tool for estimating market power, not a scientific test. … **If the exercise of market power, as defined, is identified** — if, for example, the firm is able to raise appreciably the price of its product without occasioning a significant reduction in demand — **then a market relevant for the purposes of the enquiry will have been identified**.

9. The practice of price discrimination may itself indicate the exercise of market power.[12] As the passage from Hovenkamp quoted in my first lecture made clear, *sporadic* price discrimination by sellers is a normal and positive feature of competitive markets; it would thus not be indicative of market power. Moreover, even in a market dominated by powerful firms, sporadic price discrimination would rarely if ever lead to competitive harm. On the other hand, *persistent* price discrimination may generally be expected to have some harmful effects, through both output and 'wealth transfer' losses. The crucial point is that *persistent* price discrimination can only exist where the disfavoured customers are unable freely to move their custom to other suppliers or to substitute other products at a better price — where, in other words, the firm or firms practising such discrimination have market power.[13] To quote Hovenkamp:

> If the favored purchaser is paying a competitive price (marginal cost), the disfavored purchaser must be paying a price higher than marginal cost, and giving the seller monopoly profits. For this reason, **the ability**

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[12] In the words of Sullivan and Grimes *The Law of Antitrust: An Integrated Handbook*, page 787: 'In economic terms, true discrimination occurs only through the exercise of market power.' This is true at least of persistent price discrimination. See *id.,* page 69.

[13] See also page 179 of the same work: 'Persistent price discrimination is inconsistent with competition: customers asked to pay the discriminatorily high price will seek out a different seller, and in a competitive market there will always be a seller willing to make the sale at marginal cost. The existence of persistent price discrimination is therefore evidence that the market is not performing competitively.' Cf Posner *op. cit.,* page 80: 'Persistent price discrimination can be evidence of monopoly because it is inconsistent with a competitive market; it implies that some consumers are paying more than the cost of serving them, a situation that would disappear with competition, at least perfect competition.' (American antitrust writers commonly refer to 'monopoly' or 'a monopolist' as a kind of shorthand when they have in mind any situation of appreciable market power.)

> **to price discriminate is evidence that the seller has a certain amount of market power**.[14]
>
> Although the absence of price discrimination does not show absence of market power, **the presence of persistent price discrimination is pretty good evidence that a seller has market power in the high priced markets**.[15]

When we hear it argued that price discrimination does not itself indicate market power, the advocate concerned is forgetting to draw the vital distinction between sporadic and persistent price discrimination. The very ability of a firm to sustain significant price discrimination provides evidence of captive customers bound to pay the higher prices, and accordingly evidence of market power.[16]

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[14] *Federal Antitrust Policy*, *supra*, page 566.

[15] *Id.,* page 136.

[16] The same logic explains why a realistic possibility of 'arbitrage'— reselling by favoured buyers to disfavoured buyers at a significantly lower price than the latter could obtain from the supplier — would tend to undermine and ultimately prevent persistent price discrimination by the supplier. (See Hovenkamp *Federal Antitrust Policy* (*supra*), page 568.) The same result would follow where, realistically, buyers can readily combine to obtain more favourable bulk prices from the supplier, and divide up the quantities so purchased among themselves. Of course, apart from obvious practical difficulties attending such combinations by competitors, there will always be some additional cost to them in doing this. However, the persistence of price discrimination itself shows that these hypothetical escape routes are in fact not realistically available to disfavoured buyers. In my view, it would be wrong to suggest that the 'possibility' of arbitrage or buyers' combinations means that there is no 'discrimination' in fact. That argument proceeds from an incorrect starting-point. Our law does not oblige purchasers to attempt to find another supplier or engage in buying combinations in order to counter price discrimination by a dominant firm: they can simply look to section 9 of the Competition Act for their remedy. Section 9(1)(*b*) speaks of the *sale* to different purchasers. There is nothing to suggest that this criterion does not apply or is altered if different purchasers *could* combine to form one purchaser. In this connection, citing Canadian authorities such as Trebilcock et al, *The Law and Economics of Canadian Competition Policy* does not assist. Paragraph 50(1)(*a*) of the Canadian Competition Act defines prohibited price discrimination by a comparison with what is '*available*' to competitors. Our Act is not open to that construction: section 9(1) compares the terms of actual '*sale*'. Accordingly, the possibility of arbitrage or buyers' combinations does not affect whether or not prohibited discrimination has occurred. However, cf the fourth lecture, regarding the possibility of arbitrage or collective buying as potentially rebutting the likelihood of substantial anti-competitive effects.

On the facts of the Nationwide Poles / Sasol case, there would seem to have been a number of practical difficulties attending on arbitrage or collective buying of bulk creosote loads, as Mr van Wyk explained (Transcript 6 August 2004, pages 362-363 and 372-375). Since apparently intermediaries are not permitted in this field, an entity registered with the Department of Agriculture as a treatment plant would have had to buy the creosote (substantially in excess of its own needs), after having satisfied Sasol of its credit-worthiness or being in a position to pay cash, and would then effectively have had to on-sell or on-deliver to other registered treatment plants. It would seem clear, therefore, that no defence to the charge of prohibited price discrimination lay along that track.

10. It seems to me that Sasol's differential pricing structure as set out in the table referred to in the first lecture itself provided evidence of market power. The price differences were on the face of them substantial, and they had clearly been sustained over a considerable period of time.[17] They satisfy the ordinary definition of 'price discrimination' — that is to say, the prices of the various units sold have no constant ratio to the marginal cost of supply. It is possible to draw this conclusion without any investigation of actual costs in relation to quantity supplied, for two very simple reasons.

11. First, each price band included significant differences in quantity, so that, for example, customers A and B would qualify for the same price per tonne even though A had purchased a quantity annualised as 1 001 tonnes while B had purchased a quantity annualised as 2 500 tonnes. Second, and more important, the price bands were based on *historical* volumes purchased by each customer, not on the volumes purchased to which the prices were applied.[18] It was thus inherent in the pricing structure that customer C and customer D might end up paying substantially *different* prices for the *same* volume purchased at a particular time merely because they had purchased different volumes previously. Nor was there any aggregation of current and historical volumes, and corresponding adjustment (by way of rebate, for example), to achieve ultimately a volume-related unit price applicable on a standard basis to each customer.[19] Both in any particular supply and in the aggregate of

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[17] This is apparent from the tables themselves. Moreover, it appears that Sasol's pricing structure along these lines had been in operation for about ten years. (See telefaxed letter from Sasol's attorneys to Nationwide Poles, 6 May 2004, par 2.5: Tribunal bundle page 573.)

[18] This was covered in the first lecture.

[19] See Sasol's main heads of argument dated 30 August 2004, par 3.7 and 3.8.

supplies to each customer, the actual ratio of price to marginal cost remained arbitrary.

12. For these reasons, I think, *persistent* price discrimination — and with that, *market power* — was indicated by the persistence of Sasol's pricing structure itself.

13. Nothing was to be gained in this case by invoking the following theoretical qualification made by Hovenkamp in *Federal Antitrust Policy* (*supra,* page 136, note 15):

> Price discrimination may sometimes be evidence that the market contains one or more powerful, monopsony buyers, rather than a monopoly seller. A monopsonist may be able to reduce its demand for a product and buy at a lower price. A seller who deals with the monopsonist as well as other buyers may be price discriminating **even though it has no market power**.

However, the fact that Sasol did not negotiate its creosote prices customer-by-customer, but systematically applied to all alike a pricing structure as described, shows plainly that customer monopsony was not the true basis of the discrimination. The real power has been on the supplier's side.

14. Then we have the crucially important, undisputed evidence of the *increases* in Sasol's prices of bulk creosote (including 'Sak K') prior to and during the period covered by the Nationwide Poles complaint.

15. The background to the price increases was the following. Originally, the crude tar stream from which creosote and other tar derivative products have been manufactured by Sasol, came only from coal-based gasifiers at its Sasolburg plant. The Sasolburg production facilities, established some fifty years ago, were designed to produce fuels from the gas stream but not from the crude tar stream coming from the gasifiers. Thus the entire crude tar stream had to be utilised

as inputs in the production of creosote and other (non-fuel) tar derivative products. More recently, in contrast, crude tar has been produced in much greater quantities at Sasol's Secunda plant, and this tar is able to be used there to produce fuels. If it is to be used to produce creosote, it must be transported to Sasolburg for processing.[20] As the matter was stated in Sasol's main heads of argument to the Tribunal —

> The Gasification Plant [at Sasolburg], which produced the mixture of crude tars and oils, used as raw materials in the Tar Workup Plant, has closed. The Tar Workup Plant will continue to operate, but will make use of tar and oil 'imported' from Secunda. Accordingly, while creosote was previously produced at relatively small marginal cost, the requirement that the Tar Business Unit now source its feedstock from Secunda, where petrol and diesel are alternative propositions, **has resulted in a massive increase in the effective marginal cost of creosote**. The increase is in the order of 300%.[21]

16. Now wait a minute! This way of putting the matter, if not more closely examined, seems to me to obliterate any real distinction between cost and profit, or simply relocates profit discretionally from one point to another within an integrated enterprise. In reality, of course, the increase referred to involved <u>not an absolute increase in actual production costs, but an increase based on the recognition for the first time of the so-called 'opportunity cost' of not using the tar and oil from Secunda to produce fuels</u>.[22] Since, however, fuels are

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[20] See the evidence of Mr van Wyk, Transcript 6 August 2004, pages 304 *et seq*. See also the summary of the technical evidence in Sasol's main heads of argument to the Tribunal, pars 2.7-2.12.

[21] Par 12.5.

[22] See the Tribunal's reasons for decision, par 63. Mr van Wyk referred to it as the 'alternative value of the Secunda product for the tar': Transcript 6 August 2004, page 305. On page 306 he is recorded as saying: '[W]e purchase the product, the raw tar from a different business unit within Sasol. So we don't have ownership. We buy it. And their alternative was round about R300,00 to R350,00 a ton, their alternative, what they could do with it. If we process it, we can add value and sell it into the market at a different price. So that was our purchase price.' It is not clear that these different business units are indeed separate *personae*, involving a true purchase and change of ownership. Nevertheless, it is possible to analyse the matter adequately from the point of view of competition law without going into that.

still priced in South Africa, not primarily with reference to the cost entailed in their production,[23] but with reference to 'import price parity', there is something artificial in regarding the substantially increased price of creosote as being the *result* of increased 'marginal cost'.[24] It appears rather to have been the result of profit-maximising decisions predicated on import price parity for liquid fuels. Where goods can be marked up in the domestic market to import parity at a price way above production cost, this itself indicates a lack of domestic competition in the supply of that market, and manifests the existence of market power. In *Tongaat Hulett Group / Transvaal Suiker Bpk*,[25] the Tribunal correctly noted that

> the ability of domestic producers to price up to import parity thereby taking full advantage of the tariff is symptomatic of their *monopoly power in a domestic market rather than their lack of power in an international market*.[26]

It seems to me that the ability of Sasol to increase creosote prices substantially in sustained increments on the basis of factoring in the so-called 'opportunity cost' of not switching the tar inputs to the production of liquid fuels, itself points (during the period concerned) to a power to behave to an appreciable extent independently of its creosote customers. The indications are that this was a firm with market power effectively in more than one market.

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[23] Mr van Wyk's evidence (Transcript 6 August 2004, page 327) that '[t]he total tar business is making a loss at this point in time because of the input cost which is too high' has to be understood in this context. The 'input cost' figure is to a considerable extent notional — and so would be the 'loss'. If there were an actual loss on a sustained basis, the question would be why production of creosote continues at all. See Transcript 6 August 2004, page 347, lines 16-17.

[24] Cf also the evidence of Mr Malherbe, Transcript 6 August 2004, page 484: 'What's at play here is the fact that what you see reflected in this company's results during these years, is the benefit that it has from an idiosyncratic supply advantage, which arises from its other activities.'

[25] [1999-2000] CPLR 127 (CT) (Case No.83/LM/Jul00) at 138*d-e*.

[26] The same approach would apply here even though creosote itself is not priced directly on an import parity basis.

17. But let us accept for the sake of argument that the increase in Sasol's 'marginal cost' of producing creosote was absolutely real. The increase was said to have been effective from June 2004.[27] Yet the substantial increases in Sasol's list prices for creosote began, *in anticipation of this change, three years earlier*. Sasol's argument to the Tribunal included this:

> [Sasol's] series of price increases, over the last three years, were designed to compensate for the impact of this supply (cost) shock. With both cost and price increases now fully manifest, [Sasol's] profit margin has reduced during the current financial year to less than a tenth of its previous level.[28]

Stripped of the polish of advocacy, what this really signified was that Sasol was able to raise its creosote prices (and concomitant profits) substantially well in advance of the increase in marginal cost. According to Sasol's argument in the Tribunal,[29] the real cumulative price increase for its creosote from 2001 to 2003 was 29% — and this during a period when the real price of CCA[30] (a potential substitute for much of creosote usage) was evidently decreasing.[31]

18. Mr van Wyk frankly described how, in anticipation of the change in the (opportunity) cost of feedstock, Sasol had openly explained the situation to its creosote customers:[32]

> So the alternatives, we put them all on the table. We did our own calculations as well. And we asked the industry would they prefer us keeping the price on the normal PPI increases and so on and then after four years you give them a 500% or whatever increase. Or do you want

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[27] Sasol's main heads of argument to the Tribunal, par 12.5.

[28] Par 12.5.

[29] Par 12.11.4 and 12.13.

[30] Copper chrome arsenate. Timber treated with CCA is green, whereas timber treated with creosote is dark brown or black.

[31] See Transcript 6 August 2004, page 438.

[32] Transcript 6 August 2004, pages 324-325.

> us gradually increasing it to a point where we believe we can start doing normal business again. And that happened in the past three years. And what they told us is they prefer us phasing it in, because it won't give them a total shock, because on their contracts [with their customers] as well they won't be able to negotiate their contracts on a big increase. They can maybe incorporate it in a phased manner.

Admirable as this transparent conduct may have been, the description of it — and of the customers' response — surely manifests a situation in which customers were to a significant degree prisoners of a supplier with market power. The situation was essentially this: *'You'll have to take your price medicine. You can take it in one big spoonful or in several smaller ones — the choice is up to you.'* [33]

19. One could hardly ask, I think, for clearer evidence that Sasol's prices for creosote were in fact not effectively constrained by pressure of competition, whether from CCA or from creosote supplied by Suprachem.[34] During the period relevant to the complaint, Sasol's only competitor[35] in the bulk supply of creosote was Suprachem (Pty) Ltd — a wholly-owned subsidiary of Iscor Ltd (subsequently Ispat Iscor Ltd and now Mittal Steel South Africa Ltd). Mr Malherbe conceded under cross-examination that if Sasol actually saw CCA as a competitor it would have been able to reduce its creosote prices to meet that competition[36] — yet there is no indication that it ever did so. Mr van Wyk was able to refer to only one instance when Sasol departed from its standard price list in order to meet creosote price

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[33] Under cross-examination, Mr van Wyk acknowledged that it did not make economic sense for customers to pay price increases in advance of the increased costs to Sasol being incurred, yet 'that was their preference'. (Transcript 22 November 2004, pages 83-85.)

[34] This competitor is variously referred to in the record as 'Suprachem', 'Iscor' and 'ICC'.

[35] See Transcript 6 August 2004, page 332.

[36] Transcript 6 August 2004, page 486.

competition from Suprachem — namely the instance of the so-called 'Christmas Special' of 2003.[37] This is an example of the exception proving the rule. The fact that Sasol was otherwise prepared to lose creosote customers rather than lower prices or forego price increases is surely precisely a manifestation of independence from its customers at that time. It is against this background of clear signs of market power that one ought really to weigh the facts concerning the extent to which CCA is substitutable for creosote,[38] and the extent to which Sasol lost custom to CCA-producers and to Suprachem following the increases in its creosote prices.[39]

20. Very sensibly, in order to avoid a finding that its share of the relevant market for purposes of the complaint exceeded the levels at which a presumption of 'dominance' would apply in terms of section 7 of the Competition Act, Sasol contended that the <u>relevant market</u> for determining its dominance or otherwise for purposes of the 'price discrimination' complaint included both creosote and CCA.[40]

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[37] See Transcript 6 August 2004, page 387.

[38] As Sasol's supplementary heads of argument to the Tribunal recognised (par 2.13), 'substitution is a question of degree.' See also Transcript 23 November 2004, page 285.

[39] Sasol's heads of argument to the Tribunal stated (par 16.18): 'The evidence, in this case, is clear: from the very moment that [Sasol] announced its price increases, (the price of its creosote increased from R1459 to R1666, an increase of 14.2% in May 2001 for the 2001/2002 period), [Sasol] began losing market share, not only to [Suprachem] but also to the CCA manufacturers.' Suprachem increased its sales of creosote by some 13% between 2001 and 2003, while Sasol's declined by 28% (see Sasol's supplementary heads of argument to the Tribunal, par 2.12). This obviously indicates a loss of creosote customers to Suprachem. The fact that the absolute fall in Sasol's creosote sales over this period (58 tonnes) was much greater than Suprachem's gain (21 tonnes) can only be explained by a shift of some creosote customers to CCA — given that the overall market for wood treatment products was expanding, and that only Sasol and Suprachem produced creosote at that time. Mr Currie of SAWPA confirmed (Transcript 5 August 2004, page 247) that people have been moving to CCA as a result of increases in the price of creosote.

[40] If creosote alone is considered, Sasol was conceded to have had 56% of the market in 2003 and 42% in 2004. (See Transcript 4 August 2004, page 93.) If, however, both creosote and CCA are taken together, Sasol's share was in all probably less than 35%. In the latter event, in terms of section 7 of the Competition Act, 'dominance' would have to be established purely by reference to 'market power'. The fact that Sasol did not cotton on to the 'substitutability' of CCA as a possible argument in its favour at the

21. It is clear from the evidence that, for most purposes, CCA is substitutable for creosote in the treatment of timber.[41] Hence it is not surprising that, where timber treated with creosote competes in a downstream market with timber treated with CCA, the prices of the two kinds of treated timber are the same.[42] But such price equivalence is irrelevant when it comes to kinds of treated timber where, either functionally or for other reasons, treatment with CCA is <u>not</u> acceptable as a substitute for treatment with creosote. Consequently, to the extent that customers of Sasol have depended on Sasol for supplies in order to serve such a distinct segment of the market for treated timber, it is obvious that Sasol's market power can in no way have been mitigated by potential substitution of another product.

22. In regard to market segments or 'submarkets', the CAC has adopted the methodology advanced as follows by Warren C.J. in *Brown Shoe v. United States*:[43]

> The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it. However, within this broad market, well-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes. The boundaries of such a submarket may be determined by examining such practical indicia as industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors.

See *Patensie Sitrus Beherend Bpk v Competition Commission and*

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outset of the proceedings (I would not call it a 'glaring inconsistency in Sasol's evidence and argument': cf Tribunal's reasons, footnote 20) can hardly affect the correctness or otherwise of the contention.

[41] SABS standards generally hold them equally suitable for preserving timber from attack by fungi and insects, in almost all applications.

[42] See the first G:enesis report, par 32 (Tribunal Bundle, page 125).

[43] 370 U.S. 294 (1962) at 325.

others.[44]

23. It seems clear that, in at least one very substantial segment of the market for treated timber, CCA is not an acceptable substitute for creosote. It appeared to be common cause that wooden poles used for carrying Telkom and Eskom lines are all treated with creosote,[45] and that that CCA-treated poles are not generally considered suitable for this purpose because they do not adequately withstand veld fires.[46] In contrast with creosote-treated poles, they suffer from an 'afterglow' effect. The same applies to fencing poles generally where the risk of veld fires is significant.[47] To the extent that Sasol supplied creosote to customers producing for this market segment,[48] it could not be regarded as supplying a product for which CCA was a substitute capable of freeing the customers concerned from what would otherwise be Sasol's market power.

24. Persistent price discrimination, in relation to bulk creosote supplies generally, could substantially impede firms in competing in the segment of the treated-timber market which involves the supply of treated telephone and electrical transmission poles (as well as other

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[44] [2003] 2 CPLR 247 (CAC) (Case No. 16/CAC/Apr02) at 256*e-g*.

[45] Sasol's senior counsel aptly described Telkom and Eskom as 'very, very sizeable customers' — i.e. in the downstream market for treated timber. (Transcript 4 August 2004, page 102.)

[46] See e.g. Transcript 4 August 2004, page 102; Transcript 5 August 2004, page 208. This must be qualified to some extent by the *possibility* of the use of CCA-treated poles where there is no serious risk of veld-fires: Transcript 22 November 2004, pages 6-7. This, however, does not alter the essential point.

[47] See evidence of Mr Currie, Transcript 5 August 2004, page 207.

[48] See Transcript 22 November 2004, page 137:

> ADV UNTERHALTER: Were you aware of the fact that certain customers had a greater need for creosote than others, in other words that part of their need for creosote was linked to what their customers in turn demanded? So in other words, not all customers were in the same position [as Woodline, which had reduced its creosote purchases by two-thirds, while switching to CCA].
>
> MR VAN WYK: That's true. Not all customers, depending in which market you are playing, for example, transmission poles, smaller poles. There are different drivers to what their needs are.

fencing poles where substitution of CCA for creosote is limited). I would think, therefore, that this is <u>a market segment capable of being treated as a distinct relevant market</u> for purposes of establishing 'dominance' as contemplated by section 9, read with section 7, of the Act. It does not matter that the complainant itself had not previously competed in that market segment; the evidence was that it was a potential competitor in that segment.[49] In any case, for a 'price discrimination' complaint to succeed, it is not necessary that the complainant should itself have been disadvantaged or be capable of being disadvantaged by the conduct complained of:[50] the question is simply whether the pricing behaviour identified by the complaint is prohibited by the Act.[51] The same considerations must, I think, apply when examining whether the firm so behaving has market power or a market share amounting to 'dominance'.

25. The fact that there is a <u>statistical</u> category of 'other poles' — i.e. other than transmission poles — provides no reason to define the downstream market relevant to the complaint as the market for 'other poles'. The purpose in attempting to do so was obviously to facilitate the suggestion that, in the relevant market, CCA is freely substitutable for creosote.[52] But this suggestion seems to me to have been inherently unsound. If it is conceptually correct, as I think it is, to identify a particular segment of the market for treated timber as

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[49] See par 34 of the Tribunal's reason's for decision. Mr Foot's uncontested evidence as to why Nationwide Poles does not (yet) produce creosote-treated telephone poles is that he has been unable to secure supplies of poles (Transcript 4 August 2004, pages 111-112). If this constraint were to be overcome, price discrimination by a dominant creosote supplier could impede Nationwide Poles's expansion in the market in that regard.

[50] The matter would be different in this regard were interim relief claimed: see section 49C(2)(*b*)(ii) of the Competition Act as amended.

[51] Cf *Patensie Sitrus Beherend Bpk v Competition Commission and others* [2003] 2 CPLR 247 (CAC) (Case No. 16/CAC/Apr02) at *262d-e*.

[52] See e.g. Transcript 5 August 2004, page 146.

being distinct on the basis that creosote alone is suitable (as in the case of transmission poles), then there ought to be included therein for purposes of identifying the relevant market that part of the so-called 'other poles' market in which, likewise, creosote alone is suitable or is reasonably to be preferred.

26. It was contended by Sasol that the entire market for treated poles other than transmission poles was one in which both CCA and creosote could be used.[53] However, the evidence of the well-informed and impartial witness, Mr Currie, confirmed that there is not a simple overlap between the markets for creosote-treated and for CCA-treated timber.[54] Nationwide Poles, for its part, accepted that 'there are many producers of poles that are choosing CCA in greater quantities over creosote'.[55] It likewise did not dispute that sales of CCA-treated poles had been increasing at the expense of sales of creosote-treated poles, which have been declining.[56] But none of this demonstrates substitutability of CCA for creosote <u>in general</u>. As to switching to CCA-treatment, Nationwide Poles appeared to accept that the costs of doing so would not be prohibitive (for it);[57] its own reasons for not switching were to do with its assessment of likely resistance to CCA in the market which it aims to serve. Thus Mr Foot conceded that it would be rational to shift to using CCA because of the substantially higher price of creosote, except for the increasing and anticipated unacceptability of CCA-treated poles in the particular downstream markets which

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[53] Transcript 6 August 2004, page 439.

[54] Transcript 5 August 2004, pages 226-230 and 152.

[55] Transcript 4 August 2004, page 105.

[56] *Id.,* pages 105-108.

[57] Transcript 4 August 2004, page 119. However, see further below.

Nationwide Poles serves.[58] It was freely acknowledged by Sasol's senior counsel that the questions around the acceptability of CCA-treated timber in agricultural applications (including viticulture) are '<u>very much in flux</u>'.[59] That seems the very least that could have been conceded on this point.[60] Yet, was this not enough to show that, even in the so-called 'other poles' market, CCA was <u>not</u> generally or sufficiently substitutable for creosote to make a market definition including both products appropriate?

27. At least one further factor bears materially on this part of the analysis. The market downstream from Sasol included producers using <u>both</u> CCA and creosote for treating timber, and others like Nationwide Poles, as well as likely new entrants on the smallest scale, who were using or would use <u>only</u> creosote, either because of choice or because of the substantially lower capital costs of establishing the necessary treatment facilities. Timber-treaters using an open bath process are confined to using creosote. The minimum

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[58] Pars 3.28-3.31 of Nationwide Poles's heads of argument in the Tribunal.

[59] Transcript 5 August 2004, pages 148-149.

[60] See the evidence of Mr Currie, Transcript 5 August 2004, pages 250-252 and pages 262-267, and that of Mr Stears, *id.,* pages 282-295. The question, of course, is not whether there is adequate scientific foundation for the concerns about CCA, but whether the concerns are such as could reasonably be expected to affect the future readiness of consumers to accept CCA in substitution for creosote in particular applications, such as in poles for vineyards. See pages 58-59 of the G:enesis Report, containing as an annexure an assurance issued by SAWPA in August 2001 as to the safety of CCA. The very production of this assurance from the industry manifests concern over present or future consumer resistance. It would be difficult to disagree with par 39 of the Tribunal's reasons, and dismiss commercial calculations in this regard in assessing whether or to what extent creosote-treatment plants would have been inhibited from undertaking a switch to CCA when faced with the above-mentioned increases in the price of creosote — or indeed would be inhibited from switching if faced in future with small but significant non-transitory price increases. The evidence, in particular of Mr Stears (Sasol's witness), on pages 285-286 and 298 of the Transcript, would seem to settle the question in favour of a distinct market for creosote during the period covered by the complaint, for purposes of the inquiry into dominance. When one adds to this the unsuitability of CCA for treating telephone and electricity transmission poles, such a conclusion is greatly reinforced. The future prospect of new substitutes for CCA, which may themselves prove to be adequate substitutes for creosote, is irrelevant to the question of whether and to what extent creosote customers of Sasol could freely switch to using a substitute product during the period relevant to the complaint. (Cf par 1.1.15 of Sasol's supplementary notice of appeal.)

capital investment needed for a vacuum-pressure process, which can be used for either CCA- or creosote-treatment, is evidently at least ten times as much.[61] This must surely tend to affect the relative elasticity or inelasticity of demand on the part of different categories of Sasol's customers, according to their size. In the case of the smallest customers, demand for creosote would tend to be less elastic while the adverse price discrimination would tend to be the most severe.

28. In *Antitrust Law Developments (Fifth)* by the American Bar Association (2002), the following passage shows the potential significance of price discrimination when it comes to determining the relevant market:

> In certain situations, price discrimination may provide a basis for concluding that sales of a single product to a particular group of customers constitutes **a relevant product market separate from sales of the same product to other customers**. More particularly, if a seller or group of sellers can earn substantially different returns from different classes of customers based on their relative demand elasticities for the products of the sellers, **the relatively inelastic class of customers may constitute a relevant market**.[62]

[61] See first G:enesis report, par 40.3 (Tribunal Bundle page 127). The report adds, in par 43, that 'a producer who because of technology choice cannot readily switch, such as [Nationwide Poles], would be at a disadvantage.' (*Id.*) Obviously so would small new entrants without significant capital.

[62] Page 550. This is elaborated in footnote 105 as follows: 'See, e.g., *United States v. Grinnell Corp*., 384 U.S. 563 (1966) (finding a relevant price discrimination product market for class of inelastic buyers); *United States v. Rockford Mem'l Corp*., 898 F.2d 1278 (7th Cir.) (Posner, J.) (explaining that each category of customers identified with a specific hospital service (i.e., a specific medical indication) could represent a separate relevant product market if a hypothetical monopolist could discriminate in price (or other terms of competition) between such categories based on identified demand elasticities), cert. denied, 498 U.S. 920 (1990); *R.R. Donnelley & Sons Co*., 120 F.T.C. 36, 153 (1995) (under the standards set forth in § 1.11 of the 1992 Merger Guidelines, the FTC will define a relevant market for a group of buyers for which a hypothetical monopolist could profitably impose a "small but significant and nontransitory" increase in price); *Owens-Illinois, Inc*., 115 F.T.C. 179, 295-96 (1992) (same); *Midcon Corp*., 112 F.T.C. 93 (1989). In R.R. Donnelley, the FTC concluded that a profitable discriminatory price increase would be possible, and therefore sufficient to define a relevant market, if three conditions were satisfied: (1) the hypothetical monopolist can identify gravure customers with sufficiently inelastic demand for gravure printing (i.e., those who will not switch to offset printing in response to a five percent price increase); (2) the hypothetical monopolist can selectively and profitably increase prices to those gravure customers; and (3) arbitrage of gravure printing (resale by favored elastic customers to targeted inelastic customers) would not be sufficient to undermine the price increase. 120 F.T.C. at 158. After

29. Hovenkamp quotes U.S. antitrust guidelines to show how price discrimination enters into the determination of relevant markets for purposes of merger evaluation:[63]

> '[W]here a hypothetical monopolist likely would discriminate in prices charged to different groups of buyers … the Agency[64] may delineate **different relevant markets corresponding to each buyer group**. Competition for sales to each such group may be affected differently by a particular merger and markets are delineated by evaluating the demand response of each such buyer group. …'
>
> In the context of product markets, the Guidelines then explain as follows:
>
> 'A different analysis applies where price discrimination would be profitable for a hypothetical monopolist. **Existing buyers sometimes will differ significantly in their likelihood of switching to other products in response to a "small but significant and nontransitory" price increase**. **If a hypothetical monopolist can identify and price differently to those buyers ("targeted buyers") who would not defeat the targeted price increase by substituting to other products in response to a "small but significant and nontransitory" price increase for the relevant product, and if other buyers likely would not purchase the relevant product and resell to targeted buyers**, then a hypothetical monopolist would profitably impose a discriminatory price increase on sales to targeted buyers. **This is true regardless of whether a general increase in price would cause such significant substitution that the price increase would not be profitable**. The Agency will consider additional relevant product markets consisting of a particular use or uses by groups of buyers of the product for which a hypothetical monopolist would profitably and separately impose at least a "small but significant and nontransitory" increase in price.'

30. One has to consider the general relevance of this approach to the case. It is true that Sasol's differential pricing structure was not targeted at individual customers — but it was by Sasol's own admission targeted at customers grouped by size (for which historical volumes purchased acted as the measure). Bigger

evaluating these factors, the FTC concluded that because a significant and nontransitory increase in gravure prices for high-volume printing would likely expand use of offset printing, "high volume publication gravure printing" did not constitute a relevant market. *Id.* at 176.'

[63] *Federal Antitrust Policy, supra,* pages 130-131.

[64] I.e., the Antitrust Division of the Justice Department or the F.T.C., depending on which is analyzing the merger in question.

customers were targeted for lower prices; the converse of this must be that smaller customers were in effect been targeted for higher prices. To the extent that the price discrimination against the latter has been persistent — and it clearly has persisted for a long time — it would seem to demonstrate inelasticity of demand on the part of those adversely affected.

31. Inasmuch, moreover, as prices were raised in real terms by some 29% in advance of increases in input costs, and yet Sasol was able to retain significant numbers of customers — including smaller customers affected by the adverse price discrimination — the evidence of Sasol's market power at that time, in relation to the supply of creosote to them, becomes (so it seems to me) overwhelming.

32. The so-called 'SSNIP test' was first employed by the U.S. Department of Justice and the Federal Trade Commission when analysing horizontal mergers, but it has since gained wider recognition and application wherever a relevant product market has to be defined. Its utility is acknowledged *inter alia* by the CAC in South Africa. See *Patensie Sitrus Beherend Bpk v Competition Commission and others*.[65] 'SSNIP' , as you know, stands for *'small but significant non-transitory increase in price'*. In establishing whether product A should be regarded as being in a market of its own, or whether it shares a wider market with product B, the question is asked: in the event that a hypothetical monopolist supplying product A were to raise the price of the product by 5–10 per cent, would customers switch to product B. The application of

[65] [2003] 2 CPLR 247 (CAC) (Case No. 16/CAC/Apr02) at 256*i*-257*i*.

the SSNIP test is complicated by the fact that one does not know whether the initial price of product A is at a competitive level or not. As the Tribunal pointed out in par 51 of its reasons in the Nationwide Poles / Sasol case,

> An increase from a supra-competitive price level may well give rise to a sharp decline in demand for the product in question and a concomitant increase in the demand for an alternative without suggesting that at *competitive* price levels the two products are substitutes. This is the well-documented operation of the 'cellophane fallacy'.

In *York Timbers Ltd v SA Forestry Company Ltd (1)*[66] the Tribunal said,

> No monopolist has absolute freedom to determine its price. There is a level of price at which even a monopolist will not be able to dispose of its product.

Thus the fact of customers switching from product A to product B does not necessarily prove that A and B, properly considered, belong to the same relevant market. On the other hand, however, if a significant number of customers do not switch from product A to product B when faced with a 'SSNIP', it is safe to conclude that for them the two products are not substitutes. The 'SSNIP test' is really a rough measure of market power used to arrive at a delineation of the relevant product market. As Sullivan and Grimes note,[67] the appropriate 'SSNIP' percentage will vary with circumstances. Nevertheless, by any reckoning, real increases of 29% over three years — and prior to the cost increases said to warrant the price increases — would surely meet the test. In the Nationwide Poles case, therefore, you might conclude that Sasol had at the relevant times market power in respect of creosote, at least in respect of a

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[66] [2001-2002] CPLR 408 (CT) (Case No. 15/IR/Feb01), par 79.

[67] *The Law of Antitrust: An Integrated Handbook,* pages 581-582.

portion of its creosote customers, and that this confirms that the market for creosote was indeed the relevant market for ascertaining the relevant market shares.

33. Against this background, the evidence of the degree to which CCA is substitutable for creosote in large parts of the market for timber-treatment products would (I think) do little or nothing to disturb the picture of market power in that part of the market more narrowly defined.

34. When one assembles and analyses all the interlocking indicators of market power in this way, one can also better place in perspective the ability or inability of Sasol's creosote customers to escape captivity by obtaining their supplies from Suprachem. It seems evident that, instead of <u>one</u> dominant firm, there were at the material times <u>two</u> dominant firms in the bulk creosote market:[68] Sasol and Suprachem.

35. It was suggested by Nationwide Poles that, at least during the period covered by the complaint,[69] the possibility of Sasol's customers reliably obtaining alternative bulk supplies of creosote was limited

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[68] I should note here that, in viewing a creosote market as the relevant market, I base ourselves on the facts and reasoning above. I would place no weight whatsoever on references by Mr van Wyk and in Sasol's documents to the 'creosote market' or the 'market for creosote'. The Tribunal was (I think) mistaken in seeking to draw conclusions adverse to Sasol from the latter. Creosote is what Sasol supplies; it does not supply CCA. It is entirely natural for practical business people to refer in this way to the market for the product which their firm supplies. It says nothing about whether or to what extent they regard another product as a competitor, and whether or to what extent it is a competitor in fact.

I should also note for the sake of completeness that, in my view, there was potentially a case to be made out for treating 'Sak K' as a distinct relevant market — Sasol having in that case a 'share' of 100%. However, Nationwide Poles did not sustain its contentions in this regard. Mr Foot of Nationwide Poles said that he had not turned to Suprachem for creosote supplies because he wanted 'Sak K', and Suprachem had no wax-additive creosote product. (Transcript 4 August 2004, page 53.) But he had not investigated whether Nationwide Poles could itself add wax to Suprachem's creosote — i.e. at reasonable cost. (Page 55.) Thus no 'SSNIP test' was possible on the evidence, in relation to 'Sak K'.

[69] The picture may have altered subsequently as a result of the entry of a company called 'FSS' into creosote production and supply. (See Transcript 22 November 2004, page 13.)

because of capacity constraints on the part of Suprachem.[70] This, however, is doubtful. Towards the end of the proceedings there was 'evidence' introduced by way of a print-out from the Ispat Iscor (now Mittal) website showing that its tar plant

> has a capacity of 200 000 tonnes per annum. Iscor Coke and Chemicals distils more than 140 000 metric tonnes of coal tar-based products annually.[71]

From this information, Mr van Wyk calculated that Iscor/ Suprachem's *potential* to produce creosote would be about 40 000 tonnes p.a. — a quantity in excess of total domestic demand for creosote. There seems no reason to think that, during the period covered by the complaint, Iscor/Suprachem would have been unable to increase creosote output had it been commercially advantageous to do so. Creosote output has surely involved — and will continue to involve — a profit-maximising choice in the allocation of its tar inputs as between creosote and various other tar-based products historically produced and supplied (road-binding pitch, paint, etc).

36. The question is why — during a period of several years when Sasol was steeply and systematically raising its real creosote prices in advance of real increases in costs — Suprachem did not simply capture the entire creosote market. There is no clear evidence in the record regarding Suprachem's creosote prices. There is little to suggest, however, that its prices were significantly lower than those of Sasol's for any extended period of time. It seems clear that, when Sasol began to raise prices, it did lose a significant volume of business to Suprachem. But the arrow did not remain pointing in

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[70] This was not challenged in the second G:enesis report (page 35, Supplementary Bundle, page 91).

[71] Referred to in Transcript 22 November 2004, pages 9-10.

only one direction. The evidence of Mr van Wyk was that smaller customers have often 'moved between' Sasol and Suprachem in purchasing creosote.[72] He likewise testified that, while Suprachem gained some bigger customers from Sasol, Sasol in turn won some bigger customers from Suprachem.[73] This is incompatible with a picture of vigorous and sustained price competition on the part of Suprachem, taking full advantage of Sasol's price increases. It strongly suggested, rather, that Suprachem generally shadowed Sasol's creosote prices — perhaps after a delay and at least in relation to customers unable or unwilling to switch to CCA. The fact that Suprachem on one occasion posed a significant threat by dropping prices substantially tends to confirm that the general pattern of its competition with Sasol was otherwise.

37. No-one has suggested price-collusion between Sasol and Suprachem. Moreover, collusion is not the inevitable consequence of duopoly. But it is unsurprising, where there is an enduring duopoly of supply in a relatively small market, to find the division of the market attended by relatively stable customer relations on each side, particularly with big customers. In such conditions a customer lost today is not easily won back tomorrow, at least not without risk of substantial cost (or loss of profit). All-out war for customers, while never ruled out, is a high-risk undertaking for both duopolists. While they may not collude, there are ordinarily advantages for both in keeping their struggle a low-intensity one. Common sense suggests

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[72] Transcript 6 August 2004, page 317. Cf also what was put to Mr Foot, Transcript 4 August 2004, page 96.

[73] Transcript 6 August 2004, pages 333-334. Cf also what was put to Mr Foot, Transcript 4 August 2004, pages 86-89. There was evidence (acknowledged in Sasol's heads of argument in the CAC, par 8.14, that Suprachem's average creosote prices in 2003 were above those of Sasol.

— and game theory has sought to prove — that the firms in a non-colluding duopoly can both extract maximum sustainable profit by moderating their price competition with each other around a supra-competitive price level which is nevertheless below an outright monopoly price. If they were to compete more vigorously, one or the other might make initial gains but they would both end up with lower profits as a result of driving prices down. On the other hand, were one to push its prices up too high, the temptation for the other not to follow but to compete would intensify. Where the ultimate potential advantages for a duopolist in all-out competition with its rival are restricted by the small scale of the downstream markets, the tendency to moderate their competition between themselves around a cautiously supra-competitive level would be all the more pronounced.

38. The point, therefore, is not that there has been no competition between Sasol and Suprachem, at least for the bigger creosote customers. Nevertheless, taking account of all the circumstances which have been described, the overwhelming probability is that the competition between them has taken place at prices which are supra-competitive so that the 'alternative' offered by Suprachem has not been sufficient to eliminate Sasol's appreciable independence from its customers, and thus its own market power.[74]

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[74] In *Distillers Corporation (SA) Ltd and Stellenbosch Farmers' Winery Group Ltd* (Case No. 08/LM/Feb02, reasons for decision dated 19 March 2003, par 136) the Tribunal observed:

'…[T]he "cellophane fallacy effect" should be borne in mind when using demand elasticities to determine market power or the extent of the relevant market, as any profit-maximising firm with a degree of market power will set prices at a level where demand for its product is elastic (otherwise it would raise prices further). … As Bishop & Walker [*Economics of E.C. Competition Law: Concepts, Application and Measurement*, Sweet and Maxwell, 1999] remark:

"The mere fact that at the monopoly price, a monopolised product faces demand substitutes does not mean that the firm producing the product has no market power." It is therefore generally argued that in

39. It would appear from the evidence of Mr van Wyk — although he said that this occurred before his time — that prior to the pricing policy reflected in the volume-price lists in issue in the case, Sasol negotiated prices with customers.[75] Once the price lists were introduced, however, negotiation with customers ceased and even if Suprachem offered a better price Sasol would not meet it (the exception being the 2003 'Christmas Special'). It was (as he put it) 'a choice for the customer'.[76]

40. Thus the suggestion[77] that the inflexibility of Sasol's price structure could equally well indicate, not a situation where it enjoys market power, but a highly competitive market where suppliers have no room to deviate from their listed prices, was (I would say) an abstraction wholly removed from the realities of the period in question. The history of Sasol's price-raising without reference to the creosote prices of its competitor (or indeed the price of CCA) and well in advance even of the increase in the so-called 'opportunity cost' to it of tar; the evident arbitrariness of the price bands; the acknowledged lack of any cost quantification to support the volume-related price differences — all these at least are indicative of a situation in which there was an absence of the kind of competitive

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non-merger inquiries observed own-price elasticities may understate the degree of market power.'
[Richard Whish *Competition Law* (5th edition, pages 30-31) explains the 'cellophane fallacy' as follows: 'A monopolist may already be charging a monopoly price: if it were to raise its price further, its customers may cease to buy from it at all. In this situation, the monopolist's "own price elasticity" — the extent to which customers switch from its products in response to a price rise — is high. If an SSNIP test is applied in these circumstances between the monopolised product and another one, this might suggest a high degree of substitutability, since consumers are already at the point where they will cease to buy from the monopolist; the test therefore would exaggerate the breadth of the market. This error was committed by the US Supreme Court in *United States v EI du Pont de Nemour and Co* [351 U.S. 377 (1956)] in a case concerning packaging materials, including cellophane, since when it has been known as the "Cellophane Fallacy".' See also Unterhalter in Brassey (*et al*) *Competition Law* pages 185-186.]

[75] Transcript 6 August 2004, page 427.

[76] *Id*.

[77] By Mr Malherbe, Transcript 6 August 2004, page 440.

pressure on Sasol which a competitive market would imply. The inflexibility of the price structure — the absence of a willingness to bargain or negotiate — is, therefore, quite obviously an additional indicator of market power.

41. The absence of supply contracts between Sasol and its creosote customers is, one would think, a further manifestation of its market power during the period in question. The suggestion by Mr van Wyk that the absence of contracts was essentially for the benefit of the customer's freedom of choice strains credulity. It has been for the benefit of Sasol,[78] and Sasol could only benefit from the absence of a contract insofar as the customer could not readily — or would have no sufficient incentive to — switch. The Chairperson of the Tribunal observed:[79]

> [C]ommodity markets are difficult, because there are very few contracts and I've never met a commodity market that didn't like a long-term contract if they could get it. Even the platinum producers enter into long-term contracts because it offers security. I find it very puzzling, particularly given the premium that Sasol seems to place on security of off-take that they don't want long-term contracts.

The puzzle would largely disappear if it is remembered that Sasol was moving to a position where it could utilise its tar stream to make fuels. If Sasol could get security of uptake of creosote <u>without limiting by contract its ability to switch the tar inputs to fuel production</u>, the foregoing of long-term contracts — indeed, a refusal to enter into them — would make business sense.

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[78] See Mr van Wyk's evidence, Transcript 6 August 2004, page 396 lines 2- 3 ('… if we look on our side as well'); Mr Malherbe's evidence page 465 lines 11-13 ('…long-term contracts … will probably cost you significantly deeper discounts than the one that customers are used to').

[79] Transcript 6 August 2004, page 466.

42. These are all factors which would have warranted consideration if the CAC had thought it necessary to go into the issue of 'dominance' or market power, rather than take a short cut to a decision on another aspect of the case. In my own view, a proper consideration of the evidence pointing to market power would also have brought better into focus the question on which the outcome of the appeal may ultimately have turned: namely whether Nationwide Poles had failed to show the likelihood of anti-competitive effects in Sasol's price discrimination because it had not excluded by specific evidence the possibility of disadvantaged customers escaping such effects by simply going to Suprachem instead.

February 2006 Rob Petersen SC

‘Prohibited price discrimination’ after the CAC decision in the Sasol / Nationwide Poles case

Lecture 3 (of 4)

‘Discrimination’ and equivalence of transactions

‘Discriminating’ between purchasers — section 9(1)(*c*)

1. Section 9(1)(*c*) of the Competition Act stipulates that an action by a dominant firm is prohibited price discrimination only if it involves *‘discriminating’* between purchasers in terms of price etc. In its reasons for decision in the Nationwide Poles case, the Tribunal dealt with this aspect rather summarily, whereas the CAC found it unnecessary to deal with it at all. The Tribunal said: [1]

> It is common cause that the discrimination in question relates to the price differential engendered by differential discounts based on past sales volumes. Different prices are charged to small and large customers, by dint of the volume of their purchases from Sasol. This is sufficient to bring Sasol's conduct within the ambit of Section 9(1)(*c*).

Sasol contended essentially that the word ‘discriminating’ in this context suggests that the legislature intended to prohibit only individualised or targeted discounts. As I have indicated, I think there was targeting — although group targeting and not individual targeting. Be that as it may, I think that such a narrow construction of the word ‘discriminating’ was not intended by the legislature, and

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[1] Par 137.

to give it that meaning would simply frustrate the broader object of section 9.

2. This issue has been considered by the U.S. Supreme Court in the context of the Robinson-Patman Act. In *F.T.C. v Anheuser-Busch Inc.* 363 U.S. 536 (1960), a national brewer had lowered its prices in the St. Louis, Missouri, market without making similar price reductions in other (geographical) markets. The Court of Appeals had dismissed the price discrimination suit brought by the Federal Trade Commission, holding that the statutory threshold element of 'discrimination' had not been established. The basis of its view was that each customer in the same geographical market paid the same price, and they did not compete with customers in other markets paying a different price. However, the Supreme Court did not like the implications of this. The case before the Supreme Court was limited to a preliminary legal issue, and did not concern evidence of actual anti-competitive effects. But the Supreme Court thought the interpretation placed on the expression 'discriminate' by the Court of Appeals would operate to defeat that part of the section which aimed to protect competition in what is called the 'primary-line'. [2]

3. 'Primary-line' effects of price discrimination are those effects felt at the level of the supplier and its own competitors; 'secondary-line' effects are those felt at the level of the purchasers in whose favour or against whom the discrimination directly operates, and on the competition between them.[3]

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[2] Page 546.

[3] 'Tertiary-line' effects further downstream are also potentially of relevance in price discrimination cases,

4. If beer was supplied at different prices in different markets it might not affect the customers in those different markets in their competition with each other, but it could potentially affect the competition between the different suppliers to those markets, i.e. in the 'primary line'.

5. Anheuser-Busch did not resist this reasoning, but still argued that —

> at least there must be 'proof that the lower price is below cost or unreasonably low for the purpose or design to eliminate competition and thereby obtain a monopoly.'

They argued that this would be consistent with the scheme of the section, which was not aimed at preventing price differences as such but only price differences which were anti-competitive. The alternative would be to impose rigid price uniformity upon the business world, contrary to sound economics and the policy of the antitrust laws. In rejecting that argument in connection with the construction to be placed on the word 'discriminate', the Supreme Court said:

> **The trouble with respondent's arguments is** not that they are necessarily irrelevant in a s 2(*a*) proceeding, **but that they are misdirected when the issue under consideration is solely whether there has been a price discrimination.** We are convinced that, whatever may be said with respect to the rest of ss 2(*a*) and 2(*b*) — and we say nothing here — there are **no overtones of business buccaneering in the** s 2(*a*) **phrase 'discriminate in price**.' Rather, **a price discrimination within the meaning of that provision is merely a price difference**.
>
> *[After citing several precedents in secondary-line cases which all assumed, like the commentators, that in order to establish 'discrimination' the FTC need only prove that a seller had charged one purchaser a higher price for like goods than he had charged one or more of the purchaser's competitors, the Court went on:]*
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> These assumptions, we now conclude, were firmly rooted in the structure of the statute, for **it is only by equating price discrimination with**

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although very rarely so.

> **price differentiation that s 2(*a*) can be administered as Congress intended**. As we read that provision, it proscribes price differences, subject to certain defined defenses, where the effect of the differences 'may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit' of the price differential, 'or with customers of either of them.' See *Federal Trade Comm. v. Morton Salt Co*., 334 U.S. 37, 45-47, 68 S.Ct. 822, 827-828, 92 L.Ed. 1196. **In other words, the statute itself spells out the conditions which make a price difference illegal or legal, and we would derange this integrated statutory scheme were we to read other conditions into the law by means of the nondirective phrase, 'discriminate in price.'** Not only would such action be contrary to what we conceive to be the meaning of the statute, but, perhaps because of this, it would be thoroughly undesirable. As one commentator has succinctly put it, '**Inevitably every legal controversy over any price difference would shift from the detailed governing provisions — "injury," cost justification, "meeting competition," etc. — over into the "discrimination" concept for *ad hoc* resolution** divorced from specifically pertinent statutory text.' Rowe, *Price Differentials and Product Differentiation: The Issues Under the Robinson-Patman Act*, 66 Yale L.J. 1, 38.[4]
>
> …
>
> What we have said makes it quite evident, we believe, that **our decision does not raise the specter of a flat prohibition of price differentials**, inasmuch as price differences constitute but one element of a s 2(*a*) violation. In fact, as we have indicated, respondent has vigorously contested this very case on the entirely separate grounds of insufficient injury to competition and good faith lowering of price to meet competition.[5]

Now, although the legislative history and object of section 9 of our Competition Act is not identical with that of the Robinson-Patman Act in the United States, the interpretive reasoning in the above passage nonetheless seems persuasive and applicable here.

6. As discussed previously, the <u>economic</u> definition of 'price discrimination' implies a difference between the two transactions in the relationship between the price charged and the marginal cost of

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[4] Pages 547-551.

[5] Page 553.

supply. From that angle there may be price discrimination without a price differential, and a price differential without price discrimination. But the legislature recognised that proof of the relationship between price and cost in the two transactions would, in the ordinary course, be extremely difficult if not impossible for a complainant or the Competition Commission to establish. It would ordinarily be something peculiarly within the knowledge of the seller, or peculiarly within the latter's ability to provide. Hence the legislature laid down in section 9(2) that the seller will escape the conclusion that its conduct involving differential treatment of purchasers constitutes prohibited price discrimination if **it** establishes that such differential treatment makes no more than reasonable allowance for differences in cost or likely cost. The other special defences provided for in section 9(2) similarly involve factual matters integral to the seller's business operations and which the seller (the respondent) alone could reasonably be expected to prove.

7. While paragraph (*c*) of section 9(1) uses the expression *'discriminating between ... purchasers'*, section 9(2) uses the expression *'differential treatment of purchasers'* when referring to back to that very same paragraph (*c*) in section 9(1). This strongly indicates that *'discriminating'* in the context of section 9(1)(*c*) was intended to mean no more than *differentiating*.[6]

8. To give any other meaning to the word 'discriminating' in section 9(1)(*c*) would affect the incidence of the *onus* of proof regarding (*inter alia*) the cost of the different supplies, and would serve to

[6] Moreover, the structure of section 9(1), with *'discriminating'* in paragraph (*c*) following paragraph (*b*), suggests that 'discriminating' there simply refers to differential treatment of purchasers in terms of price etc. — *where the goods or services are of like grade and quality and are sold in equivalent transactions.*

defeat the obvious intention of the legislature in that regard. Such a construction is clearly to be avoided.[7] In order to satisfy the requirement of section 9(1)(*c*), the Commission or complainant needs to show nothing more than differentiation of the kind indicated. It does not bear any *onus* of proving 'discrimination' in the *economic* sense, namely that the price difference does not correspond to differences in marginal cost of the different supplies. It does not bear the *onus* of disproving either the 'reasonable allowance for differences in cost' defence or any of the other defences made available to the respondent by section 9(2).

9. Of course, one consequence of this interpretation is that without a price (etc) difference, the seller would not be 'discriminating' between purchasers as contemplated in section 9(1)(*c*) — irrespective of any difference in the marginal cost of supply. The same has been held to be the law in the United States.

10. Summing up the case law, the American Bar Association *Antitrust Law Developments (Fifth)* (2002) says:[8]

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[7] Cf Cross *Statutory Interpretation* (3rd edition by Bell and Engle) page 49, regarding statutory interpretation in England: 'If the judge considers that the application of the words in their grammatical meaning and ordinary sense would produce a result which is contrary to the purpose of the statute, he may apply them in any secondary meaning which they are capable of bearing.' And on page 167: 'If, of two meanings which might reasonably be attributed to the legislature, one would and the other would not lead to a result which is contrary to the purpose of the statute, the latter meaning is to be preferred.' The approach of the Roman and Roman-Dutch law has been the same: *verba ita sunt intellegenda ut magis veleat quam pereat*. Steyn *Die Uitleg van Wette* (5th edition) says on page 120, after citing Donellus: ' 'n Uitleg dus, wat minder van pas of minder dienstig is by die saak wat die wetgewer ten uitvoer wil bring moet, as die bepaling onduidelik of dubbelsinning is, agtergestel word by een wat beter sou inpas by wat verrig moet word en die doel van die wetgewer dus beter sou dien. Volgens Forster moet, by welke bepaling ook [d.w.s die vermoede dat die wetgewer geen kragtelose of doellose bepaling wil maak nie], die uitleg plaasvind ooreenkomstig die doel waarvoor die bepaling gemaak is en die woorde geuiter is. Hieruit volg verder dat ons by twee moontlike interpretasies waarvan die een aanleiding kan gee tot ontduiking van die wet, en die ander nie, daardie uitleg verkies moet word wat ontduiking sou vermy; want 'n wet word deur ontduiking geheel en al of gedeeltelik kragteloos.' See also Devenish *Statutory Interpretation,* pages 207-210, and authorities there cited.

[8] Page 463.

> **Actual net prices** — after all discounts, rebates, surcharges, and other factors that affect price — **are compared to determine, as a factual matter, whether there was a price difference**. … To be actionable, there must be an actual price difference.' In the 2002 Annual Review of this topic, the ABA adds (page 101) that to be actionable, the price difference must be more than *de minimis* and must have occurred in contemporaneous sales. Sales may be sufficiently contemporaneous, however, even though they be made several months apart.

11. Now, to return to Sasol's argument, there seems to me to be nothing in the purpose or wording of section 9 of the Competition Act (any more than in the Robinson-Patman Act) which would justify confining its application to individualised or specially targeted discounts and rebates.

12. For comparative purposes, one should also note that, in Europe, the scope of Article 82 [formerly 86] (2)(*c*) of the Treaty is by no means confined in its application to individualised or targeted discounts or rebates. The selective prosecution of such instances under the provision should not be confused with the intended legal meaning of the provision itself, properly construed. Article 82(2)(*c*) generally prohibits abuse of a dominant position by 'applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage.'[9]

13. Dealing with quantity discounts in *Portuguese Republic v Commission*,[10] the European Court of Justice said generally that —

> [a]n undertaking occupying a dominant position is entitled to offer its customers quantity discounts linked solely to the volume of purchases made from it (see *inter alia* Case 322/81 *Michelin v Commission* [1983] ECR 3461, paragraph 71). However, **the rules for calculating such discounts must not result in the application of dissimilar conditions**

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[9] See generally Whish *Competition Law* (5th edition) pages 716-724.

[10] [2001] ECR I-2613.

> **to equivalent transactions with other trading parties** within the meaning of subparagraph (c) of the second paragraph of Article 86 of the Treaty.' (Par 50.) Thus 'where, as a result of the thresholds of the various discount bands, and the levels of discount offered, discounts (or additional discounts) are enjoyed by only some trading parties, giving them an advantage **which is not justified by the volume of business they bring or by any economies of scale they allow the supplier to make compared with their competitors**, a system of quantity discounts leads to the application of dissimilar conditions to equivalent transactions. In the absence of any objective justification, having a high threshold in the system which can only be met by a few particularly large partners of the undertaking occupying a dominant position, **or the absence of linear progression in the increase of the quantity discounts**, may constitute evidence of such **discriminatory treatment**.' (Pars 52-53.)

14. There is thus clearly no requirement of targeting. However, because of the wording of Article 82, which does not have a structure comparable to our section 9 — it has no equivalent of section 9(2) and the special defences — the issues of economies of scale, cost savings etc, and the appropriateness of any discount in the light of that, <u>have to enter into the meaning of 'discrimination' itself</u>. Invoking European cases may thus lead to confusion when interpreting the expression 'discriminating' in our section 9(1)(*c*); it is the American cases which are rather in point.

'Equivalent transactions' — section 9(1)(*b*)

15. Section 9(1)(*b*) of the Competition Act provides that an action by a dominant firm, as the seller of goods or services, is prohibited price discrimination (only) if —

> it relates to the sale, in equivalent transactions, of goods or services of like grade and quality to different purchasers; …

16. The Tribunal remarked that the Robinson-Patman Act (while it refers to different purchasers of commodities of 'like grade and quality')

does not require 'equivalence' in the transactions before price discrimination as between them is prohibited.

> It appears that the requirement of 'equivalence' was introduced into the [South African] legislation during the Parliamentary process — sub-section 9(1)(*b*) was not in the original Bill. Clearly the legislature sought to limit the ambit of price discrimination by introducing another limiting feature to price discrimination, one not found in the United States legislation.[11]

However, this observation by the Tribunal needs qualification. Ulrich Springer, writing in the *European Competition Law Review*,[12] has pointed out that —

> …the Robinson-Patman Act, … prohibits discrimination between different purchasers of commodities of 'like grade and quality' where competitive injury results. The European **equivalent** … provides that an abuse of a dominant position may consist of 'applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage'.
>
> **Analysis shows that in both jurisdictions the fundamental structure of the approach to the requirement of comparability is identical: first, the products sold to different customers must be comparable, and secondly, the transactions as a whole must also be reasonably analogous.**[13]

I think the same clearly applies to section 9(1)(*b*) of our Act. Our section has the merit, perhaps, of distinguishing expressly between the comparability of the goods or services as regards their 'grade and quality', and the comparability of the 'transactions' as such. <u>It is not a case of an additional requirement, when the substance of the different statutes is compared</u>.

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[11] Par 127.

[12] 'Borden and United Brands Revisited: A Comparison of the Elements of Price Discrimination under E.C. and U.S. Antitrust Law', E.C.L.R. 1997, 18(1), 42-53. (Cited in Sasol's heads of argument in the appeal.)

[13] Pages 42-43.

17. In Europe, the general requirement of 'equivalent transactions' is read and applied so as to include comparability of the goods or services.[14] In the United States, for its part, the Supreme Court held in *F.T.C. v Borden Co.*[15] that the Robinson-Patman Act prohibits 'unequal treatment of different customers in **comparable transactions**'.[16] The requirement of comparable transactions — even where not expressly stated — is rationally inherent in the prohibition of price discrimination itself.

18. What, then, does 'equivalent transactions' mean in section 9 of the Competition Act? The Tribunal in the Nationwide Poles / Sasol case drew from the *Concise Oxford Dictionary* two alternative meanings of the word 'equivalent':[17]

> '1. equal in value, amount, function, meaning etc. 2. (**equivalent to**) having the same or similar effect.'

Having regard to the context within which the word appears, and preferring the second of these two meanings, the Tribunal concluded that —

> … transactions are equivalent if they have the same or similar **economic effect**.[18]

It went on to say:

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[14] See e.g. *United Brands Co and United Brands Continental BV v Commission* [1978] ECR 207, par 204. It was enough that the bananas were 'of almost the same quality'. Cf also *HOV SVZ/MCN* [1994] O.J. L104/34. In the U.S. the test is whether the commodities concerned offer 'substantially identical performance'. (See Sullivan and Harrison *Understanding Antitrust and Its Economic Implications*, page 416.) Under both U.S. and E.U. law, 'in cases where the identity of the products or services in question is not clear at first sight, … sufficient product substitutability from a consumer perspective will be used as the test … for product comparability.' (Springer, *op. cit.*, page 43.)

[15] 383 U.S. 637 (1966).

[16] At 643. The Tribunal's observation regarding the Robinson-Patman Act is thus based on a superficial reading, and is wrong.

[17] See pars 129-131.

[18] Par 131.

> Thus transactions may be functionally equal — one business class seat or one telephone call between Cape Town and Johannesburg may be functionally equal to another business class seat or telephone call — but they may not be equivalent (a call or a flight made in a peak time as opposed to one made during a non-peak period) in the sense that **their economic effect is different** and hence the legislature, recognising this, chose not to bring 'non-equivalent' transactions under the rubric of prohibited price discrimination despite the fact that in other respects they may be regarded as equal.[19]

One can roughly discern what the Tribunal is getting at here, although the reasoning and expression chosen are open to criticism. If the legislature had wanted to refer simply to transactions having the same or similar *'economic effect'* it could readily have used that expression itself. The Tribunal here substitutes a phrase of its own, which is less flexible and comprehensive — yet by no means clearer[20] — than the legislature's choice of the general word 'equivalent' linked to the word 'transactions'.

19. One must agree, I think, with the Tribunal that the legislature could not have intended to include a requirement in section 9(1)(*b*) that the transactions in question be equal in value or amount. Section 9(2) specifically provides for the seller to be able to justify an otherwise prohibited differentiation in (e.g.) price on the basis of reasonable allowance for differences in the cost or likely cost of the differing quantities supplied to the different purchasers. This would have been entirely unnecessary if transactions involving different quantities

[19] Par 132.

[20] It has been suggested to me that the Tribunal may have had in mind that non-'equivalence' of transactions could be indicated simply by different elasticities of demand applying to the different transactions. I am not at all sure that that is what the Tribunal meant. If so, care needs to be taken with a generalisation of that kind, for, otherwise, the very thing that keeps the disfavoured customers captive to price discrimination could provide the basis for excusing it. That cannot have been intended by the legislature.

(and thus also different values) were never to be regarded as 'equivalent'.

20. On the other hand, however, it is would not follow that differences in the sheer scale of transactions can never be so enormous as to take them out of the ambit of 'equivalence'. This is one of the difficulties involved in interpreting and applying the section. When interpreting a statutory provision, the task is to ascertain what the legislature intended in using the words which it chose to use. This is not the same as simply ascertaining the meaning of the words used — for when words are considered in the light of their context and the purpose of the enactment, it often emerges that the meaning which the words were intended to convey is narrower — or wider — than the words themselves might at first literally suggest. As it happens, even in the truncated definitions of the *Concise Oxford Dictionary* the general idea of *similarity*, as opposed to actual *equality*, is brought in. It seems to me sound to say that similarity, in the sense of practical comparability, is the key. When defining 'equivalence', *Webster's Third New International Dictionary* speaks of '*EQUATABILITY*'. 'Equivalent' includes *'like in significance or import.'* The Afrikaans text of section 9 speaks of *'gelyksoortige transaksies'*[21] — analogous transactions; in other words transactions similar in attributes making them capable of being compared.[22] The

[21] The *Verklarende Handwoordeboek van die Afrikaanse Taal* renders *"gelyksoortig'* as *'van dieselfde soort; soortgelyk; homogeen'*. The relevant meaning of *'homogeen'* for our purposes would be: *'Waarby die samestelling en fisiese toestand in elke punt dieselfde is; waarby dieselfde eienskappe, toestande en voorwaardes deurgans aanwesig is.*

[22] There is no conflict between the English (signed) and Afrikaans texts in this regard, and it is therefore appropriate to use the Afrikaans text to resolve any ambiguity in the use by the legislature of the English word 'equivalent': see *The Law of South Africa* First reissue, vol 25(1), *sv "Statute Law and Interpretation"* by Du Plessis, par 342 (esp pages 372-373); *Du Plessis and others v De Klerk and another* 1996 (3) SA 850 (CC) per Kentridge AJ at par [44].

object of section 9 is essentially to prohibit differentiation in the prices charged by a dominant firm to its customers, where it could realistically be expected to charge either the same price to all or prices making only reasonable allowance for differences in the actual or likely cost of the supply,

> … resulting from the differing places to which, methods by which, or quantities in which, [the] goods or services are supplied to different purchasers.

21. The burden of proving reasonable allowance for cost differences is specifically placed on the supplier (seller). I would say that ‘equivalent transactions’ means sales sufficiently alike in their essential features and content so as to be capable of realistic comparison when it comes to price (and indeed the other elements of comparison specified in section 9(1)(*c*)) — bearing in mind the special defences which the respondent may establish in terms of section 9(2). The requirement in terms of section 9(1)(*b*), that the Commission or complainant prove the ‘equivalence’ of the transactions, must not be construed in a way that would defeat the object of legislature in placing on the respondent the burden of proof where cost and other justifications for the differentiation between purchasers are concerned.

22. I would further suggest that differences between the customers involved in the compared transactions are irrelevant unless those differences enter into and affect the transactions qualitatively. For purposes of section 9 of the Competition Act, the equivalence — or lack of it — must be found in the transactions themselves. A

transaction (in this context) is *'a piece of business; a deal'*.[23]

23. In Europe it has been accepted, for example, that equivalence was absent where price differentials were applied to different categories of customers reflecting reasonable and objective differences in the '<u>commercial factors</u>' of the transactions concerned.[24] Thus in *AKZO Chemie BV v Commission* [25] the European Court of Justice held:

> It should next be pointed out that there was no abusive policy of discrimination between the individual mills in the Allied group and the 'large independents', **as these two categories of customers are not comparable**. On the one hand, **the central purchasing agency of the Allied group** (30% of the purchases of benzoyl peroxide) **has always enjoyed (whoever the supplier was) more advantageous prices** than those granted to the 'large independents', which buy only small quantities (together they account for 10% of the purchases of benzoyl peroxide). On the other hand, a mill in the Allied group can always obtain supplies of additives through its central purchasing agency. Consequently, an offer to an individual mill has no real chance of succeeding unless it is at the level of the price quoted to the purchasing agency. It cannot normally be expected that an individual mill will agree to pay to its suppliers a price higher than that which it can obtain through the purchasing agency.
>
> The complaint regarding selective nature of the quotations made to individual mills in the Allied group is therefore unfounded.[26]

24. In *Eurofix-Bauco v Hilti* (a decision of the Commission of the EEC which was confirmed on appeal),[27] Hilti AG — a firm dominant in the market for nail guns and related consumables — faced the complaint *inter alia* that it had applied reduced discounts to customers who purchased nails for its nail guns from a rival supplier. Upholding the complaint, the Commission found that —

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[23] *Shorter Oxford English Dictionary* (5th edition). *Webster's Third New International Dictionary*: 'a business deal'.

[24] See Springer *op. cit.,* page 46.

[25] [1991] ECR I-3359.

[26] Par 120-121. Like much European competition jurisprudence, which tends to be somewhat *ad hoc*, this passage is unfortunately rather lacking in the clarity of its underlying principles.

[27] [1988] OJ L65/19.

> [t]he reduction of discounts was not linked primarily to any objective criteria such as quantity but was based substantially on the fact that the customer was purchasing competitors' nails.[28]

It found that certain conditions applied by Hilti were 'discriminatory in that other customers of Hilti buying similar or equivalent quantities did not benefit from these special conditions.'[29] The implication, therefore, was that if only quantity-linked discounts had been applied, or if special conditions had been applied only to those buying different quantities, there would not have been the application of dissimilar conditions to 'equivalent transactions'.[30]

25. However, one must be careful when applying such reasoning to South African cases. As I have already pointed out, Article 82 of the European Treaty contains no equivalent of our section 9(2) — i.e. the special defences. Thus, for example, objective cost justifications for price differentials in relation to different quantities supplied have to be examined in Europe within the framework of the test for 'equivalent transactions'. South Africa's legislature, when it enacted section 9 including 9(2), could not have intended that merely quantitative differences would take the transactions out of 'equivalence', unless such differences were so great as to affect the essential comparability of the transactions themselves.

26. I would agree with the submission of Sasol's counsel that, in evaluating two or more transactions in order to determine whether they are 'equivalent' or not, a court (and likewise the Tribunal) would have to have regard to matters of substance rather than form,

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[28] Par 33.

[29] Par 80.

[30] See Springer, *op. cit.,* page 47.

and to all the circumstances, weighing factors which point towards an essential equivalence from those which point against it. In this regard differences or similarities in 'economic effect' (the Tribunal's phrase) — whatever that may mean — could be relevant. It is impossible to give a fixed or dogmatic content to the expression 'equivalent transactions'. The test of 'equivalence' and its outcome will depend heavily on the facts of each case. As Bellamy & Child point out in *European Community Law of Competition*:[31]

> In broad terms, price discrimination consists of not treating like cases alike (or giving the same treatment to cases that are different).

(So far as the latter aspect is concerned, however, one should note again that without 'differentiation' there is no 'discriminating' as contemplated in section 9(1)(*c*) of our Competition Act.)

27. It would be too dogmatic to rule out in principle that differences in quantity, if they are sufficiently large to result in an essential **qualitative** difference in the transactions themselves, may have as a consequence that the sales concerned are not capable of being regarded sensibly as 'equivalent transactions'. In other words, theoretically, a point could be reached where, on account of quantitative differences, the transactions being compared have such different commercial or other attributes that it no longer makes any sense to treat them as *'equivalent'* or *'gelyksoortig'*. However, having regard to the intention of the legislature in placing the *onus* on the respondent to prove a justification of price differentiation based on any allowance made for cost differences where different quantities are supplied, I would suggest that the quantitative

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[31] 5th edition, page 728.

differences in the supplies would have to be very considerable indeed before they could ever be held to affect the equivalence of the transactions in the sense intended by section 9(1)(*b*).

28. Be that as it may, there would seem to be little doubt that Sasol's pricing structure for bulk creosote did involve discriminating in price between essentially 'equivalent transactions'.

    28.1 *First*, Sasol itself treated transactions for the bulk supply of creosote as essentially equivalent by including them all in a single price list,[32] applicable to all customers without distinction.[33]

    28.2 *Second*, the transactions or deals which are relevant for purposes of section 9 are transactions of sale. In each instance in this case, the actual sale was evidently concluded by the customer taking delivery from Sasol of a tanker load (usually *via* a tanker transport service provider).[34] The price payable by the customer was arrived at by weighing the creosote load,[35] and issuing an invoice reflecting the number of tonnes of creosote contained in the load multiplied by the price per

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[32] According to information provided by Sasol management, the prices on the price list are factory-gate bulk prices (excluding VAT). See par 19.1 of the first G:enesis report (Tribunal Bundle page 123). See also Sasol's 1 April 2004 'Pricing policy for products supplied at Sasol Carbo-Tar (Tar Division)' (Exhibit 5, Tribunal Bundle page 723), where (apart from volume-related differences) the simple distinction is made for pricing purposes between bulk supplies of tar products and those supplied in drums. (Par 1.1.)

[33] See e.g. par 10.3 of the answering affidavit of Mr van Wyk, Tribunal Bundle page 32.

[34] See further below. Mr van Wyk, in par 20.1 of his answering affidavit (Tribunal Bundle page 40), when dealing with paragraph 16 of the referral affidavit of Mr Foot (Tribunal Bundle page 8), did not deny that each truck load of creosote is separately invoiced and that each load so invoiced is 'an independent and identifiable transaction'. This was stated with reference to Nationwide Poles, but there was no suggestion that the transactional position was otherwise where other customers were concerned. See also Transcript 6 August 2004, page 368.

[35] See Transcript 6 August 2004, page 369.

tonne applicable to the customer at that time.[36] Each invoice thus manifested a definite transaction, pertaining to a single tanker-load of creosote.[37]

28.3 *Third*, this mode of effecting the transactions of sale was directly connected with two other essential facts. One is that the price applicable to the particular customer in respect of the particular load was determined by the quantity of creosote purchased by that customer during a previous period, and was not affected by any difference in the number of the tonnes or loads purchased to which the price was actually applied. The other is that the customers did not purchase their loads in terms of contracts binding Sasol to supply. All this serves to support the conclusion that the relevant transaction in each case was the purchase of a load.

29. There is European precedent which suggests that, in appropriate circumstances, transactions with 'contractual' customers may not be equivalent to transactions with 'non-contractual' customers. In the *Benzien en Petroleum Handelsmaatschappij* case,[38] a supplier was held not to have abused its dominant position through differential treatment of customers when, faced with an international oil supply crisis, it reduced its own supplies to 'non-contractual' or occasional

[36] See Transcript 6 August 2004, page 370. It appears from the sample invoices included in the record (Tribunal Bundle pages 195-196 and 203) that a truck-load of creosote is approximately 30 tonnes, with the price applied and calculated per tonne.

[37] The aggregate amount owing by the customer at the end of a month will obviously depend on the aggregate of debits arising from the invoices, together with any credits that might have arisen. See Transcript 6 August 2004, page 371. Mr van Wyk stated that the amount owed by the customer at the end of the month appears in the statement 'where all the credits and debits and deliveries and so on has been summarised.' (*Id.*) A statement is conventionally an aggregation and summary of particular transactions, and the debits and credits relating to them.

[38] *Benzien en Petroleum Handelsmaatschappij BV v Commission* 1978 ECR 1513, par 29-32.

customers to a greater extent than to those with which it had contracts. A similar idea is echoed in par 134 of the Tribunal's reasons for decision.

30. To repeat the point: The argument that sales to bigger customers are not the 'equivalent' of sales to smaller customers is one which has to be approached with great reserve if the object of section 9 of the Competition Act is not to be defeated. There would be some merit in this argument if, on the facts of a case, a large purchase had been made by way of a large order placed significantly in advance of delivery,[39] with acceptance of the order rendering it legally binding as a contract of sale on supplier and purchaser alike. When contrasted with occasional purchases on a small scale, it could be said that there is a qualitative difference in the transactions so that they cannot properly be compared and treated as 'equivalent' for the purposes of section 9. But would it be sound to draw such a conclusion from the evidence in the Nationwide Poles / Sasol case?

31. In respect at least of its bigger customers, Sasol seems to have planned its creosote output with the help of so-called 'orders' faxed or telephoned through at the beginning of the month. But a careful analysis of the evidence[40] (there is not time to go through it in this lecture) shows that no binding deals — no transactions — occurred on the basis of orders. The transaction was concluded, tanker by tanker, only at the time the tanker was loaded and weighed. Sasol was not in favour of binding itself in advance.

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[39] It is true, as the European Court of Justice observed in the *Benzien en Petroleum* case (*supra*) that 'the plans of any undertakings are based on reasonable forecasts.' (Par 30.)

[40] See esp. the evidence of Mr van Wyk: Transcript 6 August 2004, pages 315-317, 361, 369-371 and 381.

32. And here again we also have to bear in mind the fact, inherent in Sasol’s pricing structure, that two customers ordering the identical quantity of creosote in a single month might pay significantly different prices. The fact that discounts were based, not on the volume purchased in the transaction (or combination of transactions) to which the price was applied, but on historical volumes purchased, seems to me to undermine radically any argument to the effect that the price differences related to transactions which were not ‘equivalent’.

33. It is perhaps appropriate to mention here also the ingenious argument that the different risk for Sasol in having larger rather than smaller customers should lead to the conclusion that transactions with customers in the one category were not the ‘equivalent’ of transactions with customers in the other. There are several problems with such an approach.

    33.1 *First*, it tends to equate the characteristics of the customer too simply with the characteristics of the transaction. The section requires the ‘equivalence’ — the comparability — in the transactions themselves.

    33.2 *Second*, if risk is reducible to cost or likely cost, and if there is a different risk in the different transactions, then section 9(2) leaves open a line of defence whereby the supplier could prove that the price differences applied make only reasonable allowance for the differences in cost or likely cost of the quantities supplied. Allowance for different levels of risk enters naturally into the scheme of section 9 there. To require the complainant to negative such differences when proving the ‘equivalence’ of the transactions would entirely undermine the

scheme of *onus* and proof set out in the section. It should be rejected, I think, for similar reasons to those given by the U.S. Supreme Court in *Anheuser-Busch*.

February 2006 Rob Petersen SC

‘Prohibited price discrimination’ after the CAC decision in the Sasol / Nationwide Poles case

Lecture 4 (of 4)

Proof of the likelihood of a substantial prevention or lessening of competition

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1. Section 9(1)(*a*) of the Competition Act provides that an action by a dominant firm, as the seller of goods or services, is prohibited price discrimination (only) if —

> it is likely to have the effect of substantially preventing or lessening competition.

If a complainant (or the Commission) in a complaint referral fails to prove this element on a balance of probabilities (assisted, by the way, where appropriate by the inquisitorial powers of the Tribunal [1]), the respondent would rightly be entitled to a decision dismissing the complaint that prohibited conduct has occurred.[2]

2. In the Nationwide Poles case, the Tribunal held[3] that section 9(1)(*a*)

> invites a Complainant to establish a competition relevance to his complaint … when the legislature asks is it ‘likely’ it is asking us to situate the complaint as one **relevant to competition**. When it asks is it ‘substantial’ it invites us **to distinguish the trivial effect from the weightier**.

This was disapproved by the CAC, and in my view rightly so. However, more concretely, the Tribunal seemed to take the view that

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[1] See section 52(2) of the Competition Act.

[2] See sections 27(1) and 31(4) of the Competition Act.

[3] Par 103.

all that a complainant need establish in this regard is that it is a competitor (as opposed to an end consumer)[4] and that the product purchased constitutes a substantial input cost in its business.[5] I would suggest this needs some important qualifications, but there is nevertheless something sound in this idea that should not simply be dismissed; one should not throw the baby out with the bathwater. I will come back to this aspect.

3. Now, first of all, it is clear that actual harm to competition, to consumer welfare or indeed to any competitor, need not be proved. On the other hand, if there is actual harm, that will help to prove the likelihood of harm; and if there has been no harm, the Tribunal or Court will naturally have to ask itself, why not?

4. Sasol's counsel argued that the words *'is likely to have the effect of substantially preventing or lessening competition'* bear the same meaning as they do in other sections of the Competition Act. They argued that the approach taken by the Tribunal (the approach argued by Mr Foot) in giving a special meaning to this expression where it appears in section 9 was wrong — and the CAC essentially agreed with them. With respect, I also agree that Sasol (so far at least) was right. Nevertheless, it does not follow that Nationwide Poles should have lost its case.

5. The reasoning of the Tribunal in regard to section 9(1)(*a*) is contained in paragraphs 91 – 111 of its reasons for decision. I don't have time to read the argument out. You ought to read it for yourselves if you have not already done so. It is very convoluted and

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[4] Par 104. This case concerns, of course, secondary-line effects.

[5] Par 105.

(to my mind) unconvincing, in its effort to escape the ordinary meaning of the words which the legislature chose to use, in favour of a perceived 'purpose' behind section 9.

6. Now, of course the purpose of an enactment is plainly a vital part of ascertaining the true meaning of the words which the legislature has used, especially where these are ambiguous when read in their pure linguistic context. Indeed, in extreme cases, where it is plain that the legislature cannot have meant what the words seem to say, one may be justified in relying on the evident purpose of the enactment to substitute, in effect, other words [6] — but that is not the situation here.

7. We are not permitted to speculate about 'purpose'. If in general the search for so-called 'purpose' is separated unduly from the meaning of the words chosen by the legislature, then what happens? What happens is that your view — or my view — of the law becomes as good as the view of the next person; discretion by the decision-maker is substituted for certainty. The rule of law is ousted in this way. The tribunal (whichever it happens to be) then usurps the role of the legislature. The rule becomes, in the words of Lord Seldon in the 17th century, as variable as 'the length of the Chancellor's foot'.

8. Mr Foot's argument, in effect endorsed by the Tribunal, was in my view clearly wrong. Mr Foot argued [7] for an automatic *onus* on the respondent of proving reasonableness once price discrimination in an imperfect market is shown to exist. But the Act prohibits price discrimination only in imperfect markets (indeed, only where a firm

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[6] *Du Plessis v Joubert* 1968 (1) SA 585 (A) at 594 *in fine* – 595B and the cases there cited, including *Venter v Rex*, 1907 T.S. 910 at 913 - 915, 921, 924.

[7] See e.g. referral affidavit pars 31 and 33; par 10 of the complainant's heads of argument in the Tribunal.

has market power), and nonetheless requires the Commission or complainant to prove a substantial adverse effect on competition before the dominant firm has to show the reasonableness of the price discrimination concerned.

9. The Tribunal's idea that 'the legislature could not have intended the complainant to establish the anticompetitive effect of price discrimination' on account of the legislature's concern with the prospects for small businesses [8] has always seemed to me unsound and wholly insufficient to overturn the ordinary rules and presumptions (or reasonable suppositions) of interpretation. Among these are that, if it can be prevented, no word used by the legislature should be regarded as superfluous;[9] and that the same words in the same enactment should be taken to have been intended to bear the same meaning.[10] The Tribunal in effect rewrote the statute in pursuit of the preferred outcome in the case. The CAC disapproved of that approach, and no number of disappointed articles in the financial press can change the fact that, in this respect at least, the CAC was surely right.

10. Nevertheless, I am going to submit to you that Mr Foot was not precluded from winning his case by the plain, ordinary meaning of section 9(1)(*a*). What seems to me to have happened is that the Tribunal overlooked a very important part of the ordinary meaning

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[8] Par 99.

[9] See e.g. *Attorney-General, Transvaal v Additional Magistrate* 1924 AD 421 at 436; *Wellworths Bazaars Ltd v Chandler's Ltd and another* 1947 (2) SA 37 (A) at 43; *CIR v Golden Dumps (Pty) Ltd* 1993 (4) SA 110 (A) at 116F-117B; Steyn *Die Uitleg van Wette* (5th ed) pages 17-19.

[10] See e.g. *Minister of the Interior v Machadodorp Investments (Pty) Ltd and another* 1957 (2) SA 395 (A) at 404D-E; *Durban City Council v Shell and BP Southern Africa Petroleum Refineries (Pty) Ltd* 1971 (4) SA 446 (A) at 457A-B. Cf also *Sullivan v. Stroop,* 496 U.S. 478, 484 (1990).

of those words — *'substantially preventing or lessening competition'* — and that the CAC likewise did not properly keep that part of the ordinary meaning in focus.

11. Competition lawyers and economists are in the habit of speaking of a 'substantial prevention or lessening of competition' as if it is a single idea — we even call it 'SLC' for short. We tend to forget that it contains several ideas. 'Lessening' is not the same idea as 'preventing'. Yet the Tribunal addressed the whole matter under the heading: ***'Section 9(1)(a) - A substantial lessening of competition'***.

12. I say again, *'lessening'* is not the same as *'preventing'*. To prove 'lessening' of competition you must make a full market analysis.[11] To prove 'prevention' of competition, that is not necessarily so.[12] The ordinary dictionary meaning of to *'prevent'* is not only to 'stop' but also to 'hinder or impede',[13] … to hinder the progress [of something] ... to hold or keep back (one about to act)'.[14] Thus what stands in the way of a firm expanding competitively within a market is likely to hinder or impede, and thus prevent, competition in that market. Compare the definition of **'exclusionary act'** in section 1(1) of the Competition Act: 'an act that impedes or prevents a firm entering

[11] What would be 'full' (or adequate) in a market analysis will depend on the market concerned, and thus cannot be judged in isolation from the facts of the particular case.

[12] It may well remain necessary in primary-line cases (where, by definition, any anti-competitive effect would be indirect). In merger analysis under section 12A, both direct and indirect effects have to be evaluated widely, and thus, as is specifically directed by the section, market analysis will remain necessary in relation to likely 'prevention' as well as likely 'lessening' of competition. As was noted in footnote 5 to the second lecture, merger evaluation also requires the evaluation of pro-competitive effects, where substantial likely anti-competitive effects are found.

[13] *Black's Law Dictionary* (7th edition); *Shorter Oxford English Dictionary* (5th edition). Though there may be particular legislative (or indeed contractual) contexts in which 'preventing' means nothing less than stopping (see *Stroud's Judicial Dictionary of Words and Phrases*, 6th edition), there seems no reason to think that our Competition Act is one of them.

[14] *Webster's Third New International Dictionary.*

into, or expanding within, a market.'

13. In my view, in the context of the expression 'substantially preventing or lessening competition', the word *'preventing'* includes hindering or impeding competitive expansion. Whatever hinders or impedes firms — and this obviously applies particularly to small firms — in expanding on a competitive basis within a market, plainly *'prevents'* competition on the part of those firms. Nationwide Poles did not have to prove the likelihood of a substantial lessening of competition. All it had to prove (I think) was the likelihood of a substantial prevention of competition, in the sense that Sasol's differential pricing placed in its way, or in the way of other small firms, a substantial hindrance or impediment to their competitive efforts.

14. This approach is not unique to the South African legislation, as appears most clearly when one looks below the surface of statutes and interprets the unspoken as well as the spoken text of the judgments in other jurisdictions.

15. In Europe, the test provided by Article 82(2)(*c*) of the Treaty[15] is whether the application of dissimilar conditions to equivalent transactions places those discriminated against *'at a competitive disadvantage'*.[16] That is all. So easily is this test taken to have been satisfied where material discrimination exists that, as Richard Whish tells us — [17]

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[15] Formerly Article 86(2)(*c*).

[16] See the CAC judgment, page 24.

[17] *Competition Law* (5th ed) page 721. In Canada, 'no lessening of competition as such needs to be shown in order for a violation to have occurred…' (Elliott, *Competition Act and Commentary* (2004 edition) page 48; see paragraph 50(1)(*a*) of the Canadian Competition Act.

> … it is noticeable that in some cases little attention has been given to this issue. In *Corsica Ferries* [*Italia Srl v Corpoazione dei Piloti de Porto di Genoa* [1994] ECR I-1783] the ECJ said that Article 82(2)(*c*) applied to 'dissimilar conditions to equivalent transactions with trading partners', without mentioning the requirement of competitive disadvantage at all. … [etc].

While, in my view, the Tribunal's interpretive reasoning was mistaken, it is not difficult to see where it was coming from in relation to section 9(1)(*a*).

16. The Robinson-Patman Act in the United States distinguishes in reality between the concepts of 'preventing' and 'lessening' of competition. It prohibits price discrimination where the effect of such discrimination may be —

> substantially to **lessen competition** or tend to create a monopoly … **or** to injure, destroy or **prevent competition** with any person who either grants or knowingly receives the benefit of such discrimination, or **with the customers of either of them**.[18]

Lessening competition through price discrimination is thus contextually linked with its potential effect on the structure of and degree of concentration in the relevant market; preventing competition is contextually linked with the potential effect of the discrimination on competition with the giver or receiver of the benefit or with their respective customers.[19] In practice, this has led in the U.S. to two distinct streams of judicial interpretation and law-making, depending upon whether the injury is alleged to occur in the secondary or the primary line. In the secondary line the discrimination operates directly upon the respective competitive positions of favoured and disfavoured purchasers, whereas it can

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[18] Section 2(a) of the Clayton Act, as amended by the Robinson-Patman Act.

[19] There is not the same contextual separation in section 9(1)(*a*) of our Competition Act.

operate only indirectly on competition in the primary line. So far as the latter is concerned, the relevant test of harm to competition is now generally taken to be the same as in cases of predatory pricing.[20] (Predatory pricing, as you know, generally involves an attempt by a dominant firm to put rivals out of business, or else to discipline them not to undercut its usual prices, by temporarily driving prices down below cost.)

17. The two leading American cases exemplify these differences. *F.T.C. v. Morton Salt Co*. 334 U.S. 37 (1948) essentially concerned the possible prevention (hindering) by discriminatory pricing of competition between customers of the supplier — i.e., an anti-competitive effect in the secondary line. On the other hand, *Brooke Group Ltd. v. Brown & Williamson Tobacco Corporation* 509 U.S. 209 (1993) essentially concerned the possible lessening of competition by (*inter alia*) discriminatory pricing tending to create monopoly at the level of the supplier — i.e. an alleged anti-competitive effect in the primary line. For reasons of time, I must confine myself to the secondary-line issues.[21]

Secondary-line harm: price discrimination *'likely to have the effect of substantially preventing … competition'*

18. Mr Foot relied on the *Morton Salt* case, and I think he was quite right to have done so. Sasol, on the other hand, argued in the Tribunal that *Brooke Group* should be applied instead, requiring in

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[20] See *Antitrust Law Developments (Fifth)* by the American Bar Association (2002) pages 474-477. Cf also the decision of the High Court of Australia in *Boral Besser Masonry Limited (now Boral Masonry Ltd) v Australian Competition and Cons* [2003] HCA 5 (7 February 2003).

[21] Nationwide Poles initially contended that there were also primary-line anti-competitive effects, but this line of attack was ultimately abandoned.

effect a full market analysis before there could be a finding of competitive harm. I think this was clearly wrong, and I notice that Sasol’s counsel somewhat changed their tack in the appeal. It is very important, at least for future price discrimination cases, to appreciate that the CAC endorsed the general approach in *Morton Salt*. My criticism of the judgment of the Court is that, in doing so, it neglected the main feature of the *Morton Salt* decision — a feature that was common to both the majority and minority judgments in the Supreme Court — regarding the manner of arriving at sufficient proof of likely prevention of competition.

19. In the *Morton Salt* case the F.T.C. had found, after a hearing, that the respondent company, which manufactured and sold table salt in interstate commerce, had discriminated in price between different purchasers of like grades and qualities, and concluded that such discrimination was in violation of section 2 of the Clayton Act, as amended by the Robinson-Patman Act. The company had won its appeal against the F.T.C. in the Court of Appeals,[22] but the Supreme Court reversed this decision and upheld the F.T.C.’s order, with some variations not relevant here.

20. The facts were that the company sold its Blue Label table salt to customers, who included wholesalers and large retail chain-stores, according to a standard quantity discount system available alike to all. The prices per case ranged, in four bands, from $1.60 down to $1.35.[23]

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[22] 7th Circuit.

[23] There were four price bands: $1.60, $1.50, $1.40 and $1.35. The price of $1.50 applied to ‘carload purchases’ and $1.40 applied to ‘5,000-case purchases in any consecutive 12 months’.

Quantity	**Price per case**
Less-than-carload purchases	$1.60
Carload purchases	$1.50
5,000-case purchases in any consecutive 12 months	$1.40
50,000-case-purchases in any consecutive 12 months	$1.35

21. Only five companies had ever bought sufficient quantities to obtain the $1.35 per case price. They could buy in such quantities because they operated large chains of retail stores in various parts of the country. As a result of the lower price, they had been able to sell Blue Label salt at retail cheaper than wholesale purchasers could reasonably sell the same brand of salt to independently operated retail stores, many of whom competed with the local outlets of the five chain stores.

22. The Supreme Court took the view[24] — and this was the view of the whole bench — that the legislative history of the Robinson-Patman Act made it abundantly clear that Congress considered it to be an evil that a large buyer could secure a competitive advantage over a small buyer solely because of the large buyer's quantity purchasing ability.

> The Robinson-Patman Act was passed to deprive a large buyer of such advantages except to the extent that a lower price could be justified by reason of a seller's diminished costs due to quantity manufacture, delivery or sale, or by reason of the seller's good faith effort to meet a competitor's equally low price.[25]

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[24] Justice Black delivered the opinion of the Court. Justices Jackson and Frankfurter agreed with this part of the opinion, but dissented in respect of another part, which I shall deal with further below.

[25] Page 43. The Supreme Court held further that the language of the section, and the legislative history behind it, showed that 'discrimination' in price meant no more than the charging of a higher price to one purchaser than to another, where the commodities purchased were of like grade and quality and where the effect of such difference 'may be to injure, destroy, or prevent competition with any person who either

With the vital differences that in our case the prohibition applies only where the seller has a dominant position in the relevant market, I think that the South African legislature had a fundamentally similar object in section 9 of our Competition Act (so far as secondary-line effects are concerned). This seems also to be the view of the CAC.

23. It was noted by the U.S. Supreme Court in *Morton Salt* that actual harm to competition did not have to be shown. The object of the prohibition was to stop such discrimination in its incipiency. The F.T.C. had found what, in the view of the Court,

> **would appear to be obvious**, that the **competitive opportunities** of certain merchants were injured **when they had to pay** respondent **substantially more** for their goods **than their competitors had to pay**. The findings are adequate.[26]

You may notice that there is nothing in this statement that would justify limiting it to cases where the disadvantaged merchants are foreclosed, i.e. have to exit or are likely to exit the market.[27] In the U.S., it has never been held to be so limited.

24. In *Morton Salt* there was no difference between the majority and minority judgments on this crucial point. The difference was on a very specific, separate question. The majority held that a mere 'reasonable possibility' of substantial harm to competition was

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grants or knowingly receives the benefit of such discrimination, or with customers of either of them….' The Court cited *Moss v. Federal Trade Comm*., 2nd Cir., 148 F.2d 378, 379, which had held that proof of a price differential in itself constituted 'discrimination in price,' where the competitive injury in question was between sellers, and referred also to *Federal Trade Comm. v. Cement Institute et al*., 333 U.S. 683. See also *Brooke Group Ltd v. Brown & Wilkinson Inc.* 509 U.S. 209, 220: '….we have reiterated that " 'a price discrimination within the meaning of [this] provision is merely a price difference,' " *Texaco Inc. v. Hasbrouck,* 496 U.S. 543, 558 … (1990) (quoting *FTC v. Anheuser-Busch, Inc.,* 363 U.S. 536, 549 … (1960).' See also *Falls City Industries, Inc. v. Vanco Beverage, Inc.,* 460 U.S. 428, 444 (1983).

[26] Page 46.

[27] Contrast page 37 of the judgment of Davis JP in the CAC. (Selikowitz JA and Mhlantla AJA concurred.)

enough. The minority preferred 'reasonable probability' as the standard. That was all. They were agreed on the outcome of the case; they differed only on a part of the reasoning. The majority's view depended on the express word 'may' in the statute under interpretation: the prohibition occurs where the effect of the discrimination '<u>may be</u> substantially to lessen competition … or prevent competition'.

25. Somewhat mysteriously, the CAC held — *obiter* (I would point out) — that while the word 'likely' in our section 9(1)(*a*) involves a probabilistic inquiry,[28] <u>a mere reasonable possibility would suffice</u>.[29] This is very difficult to follow. A likely effect means a probable effect, not a possible effect. It makes no sense to speak of a reasonable possibility of a probability. A thing is either likely or it is not; either probable or not. This confusion may be expected to be cleared up in later cases. It would still be safest to say (when analysing a price discrimination case in South Africa for purposes of prosecution) that the <u>probability</u> — *'likelihood'* — of competition being substantially prevented or lessened has to be shown, despite the *obiter dictum* of the CAC, that a mere 'reasonable possibility' is enough. After all, as we know from *Ansac-Botash*,[30] beyond the CAC there is potentially Bloemfontein.

26. But now let me turn to the really important issue. It had been argued by the *Morton Salt* company that the evidence was inadequate to support the Commission's findings of potential injury to competition,

[28] Page 28.

[29] Page 37.

[30] *American Natural Soda Ash Corporation and another v Competition Commission and others* 2005 (6) SA 158 (SCA).

but the Supreme Court disagreed. The majority held as follows:

> That respondent's quantity discounts did result in price differentials between competing purchasers **sufficient in amount to influence their resale price of salt** was shown by evidence. **This showing in itself is adequate to support the Commission's appropriate findings that the effect of such price discriminations 'may be substantially** to lessen competition … and **to injure**, destroy **and prevent competition**.'[31]
>
> … The Commission here **went much further** in receiving evidence **than the statute requires**. It heard testimony from many witnesses in various parts of the country to show that they had suffered actual financial losses on account of respondent's discriminatory prices. Experts were offered to prove the tendency of injury from such prices. The evidence covers about two thousand pages, largely devoted to this single issue — injury to competition. **It would greatly handicap effective enforcement of the Act to require testimony to show that which we believe to be self-evident, namely, that there is a 'reasonable possibility' that competition may be adversely affected by a practice under which manufacturers and producers sell their goods to some customers <u>substantially cheaper than they sell like goods to the competitors of these customers</u>. This showing in itself is sufficient to justify our conclusion that the Commission's findings of injury to competition were adequately supported by evidence.**[32]

27. You will notice again that there was absolutely nothing to suggest the need to prove likely foreclosure, or that the *Morton Salt* approach applied only where the price difference was so great as to threaten that. In interpreting Morton Salt in that way, in sailing onto those rocks, the CAC (I believe) was too much attracted by the siren song of eloquent advocacy.

28. Note also the minority opinion in *Morton Salt.* Justice Jackson said:[33]

> The Robinson-Patman Act itself, insofar as it relates to quantity discounts, seems to me, on its face and in light of its history, to strive for two results, both of which should be kept in mind when interpreting it.
>
> On the one hand, it recognizes that the quantity discount may be utilized

[31] Page 47.

[32] Pages 50-51.

[33] Pages 58-59.

> arbitrarily and without justification in savings effected by quantity sales, to give **a discriminatory advantage** to large buyers over small ones. **This evil it would prohibit**.
>
> On the other hand, it recognizes that a business practice so old and general is not without some basis in reason, that much that we call our standard of living is due to the wide availability of low-priced goods made possible by mass production and quantity distribution, and hence that whatever economies result from quantity transactions may, and indeed should, be passed down the line to the consumer. …

By reducing the test from a reasonable *probability* to a mere reasonable *possibility* of harm to competition, the majority was in danger of obliterating the difference between what the Act would foster and what it would condemn. After analysing the facts, he continued:[34]

> **I agree that these facts warrant a *prima facie* inference of discrimination and sustain a finding of discrimination unless the Company, which best knows why and how these discounts are arrived at and which possesses all the data as to costs, comes forward with a justification.** …
>
> **Even applying the stricter test of probability, I think the inference of adverse effect on competition is warranted by the facts as to the quota discounts. It is not merely probable but I think it is almost inevitable that the further ten-cent or fifteen-cent per case differential** in net price of salt between the large number of small merchants and the small number of very large merchants, **accelerates the trend** of the former towards extinction and of the latter towards monopoly.

'Accelerates the trend' — which is there anyway for small businesses to disappear. There was plainly no necessity of proving likely foreclosure, likely exit from the market, as a direct consequence of the price difference.

29. Moreover — and this crucial point seems not to have been mentioned by any advocate and was entirely overlooked by the CAC — Justice Jackson characterised the majority's approach to proof, as

[34] Page 60.

well as the minority's (i.e. his own) approach, as accepting evidence of the extent of the price discrimination as being in itself adequate to create a *prima facie* case of competitive harm. In the majority and minority judgments alike, the principles enunciated in no way depended on the inability of the disfavoured retailers to earn any margin on table salt. The point was simply that there was a substantial relative disadvantage to them on the basis of the differential prices charged. This alone was held sufficient to establish *prima facie* that competition between competitors at that level could — and probably would — be harmed. Proof that disfavoured firms have exited or cannot survive as a result of the price discrimination would be entirely unnecessary.

30. Survival in the market-place is a necessary element in competition, but competition means much more than mere survival. It means an ability, where all else is equal, to expand market share on the basis of greater efficiency, enterprise, innovation and hard work. The point therefore is the handicap which disfavoured firms would be likely to face in expanding, all else being equal. That handicap may not lead to an actual 'lessening' of competition; but it quite obviously leads to a 'prevention' of competition, in the sense of impeding competitive expansion.

31. Indeed, the effect of price discrimination in impeding the possibility for disfavoured firms to expand within a market will be all the greater where competition in that market is already keen. The U.S. decisions have not overlooked this.

32. The approach of the U.S. courts is summed up as follows in the American Bar Association's *Antitrust Law Developments (Fifth)* (2002):[35]

> Injury to competition can be proved through direct evidence of lost sales or profits caused by the discrimination.[36] **The more common approach is to prove the requisite competitive injury by inference.** In *FTC v. Morton Salt*.[37] the Supreme Court held that the existence of a substantial price difference over a substantial period of time involving a product for resale, where competition among resellers is 'keen,' creates an inference of injury to competition.[38] Cases inferring competitive injury from price discrimination frequently involve entrenched discriminatory pricing between highly competitive customers operating with low profit margins.[39] **No inference of injury to competition is permitted when the discrimination is not substantial.**[40]
>
> A number of courts have held that injury to a single competitor may be

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[35] Pages 478-479.

[36] [ABA:] See, e.g., *Falls City Indus*., 460 U.S. at 434-35; *DeLong Equip. Co*., 990 F.2d at 1202; *Alan's of Atlanta, Inc. v. Minolta Corp*., 903 F.2d 1414, 1418 (11th Cir. 1990); *J.F. Feeser, Inc. v. Serv-A-Portion, Inc.*, 909 F.2d 1524, 1539 (3d Cir. 1990), cert. denied, 499 U.S. 921 (1991); *Eagle Windows of N. Ill., Inc. v. Eagle Window & Door, Inc.,* No. 89 C 662, 1992 U.S. Dist. LEXIS 1254 (N.D. Ill. Feb. 7, 1992).

[37] *Supra.*

[38] [ABA:] *Id*. at 50-51. The Supreme Court reaffirmed the *Morton Salt* rule in *Falls City Indus*., 460 U.S. at 436. The FTC adopted the inference in *Beatrice Foods Co*., 76 F.T.C. 719 (1969), aff'd sub nom. *Kroger Co. v. FTC*, 438 F.2d 1372, 1379 (6th Cir.), cert. denied, 404 U.S. 871 (1971).

[39] [ABA:] See, e.g., *Stelwagon*, 63 F.3d at 1273 (favored customers were charged prices that were 5 to 25% lower than prices paid by plaintiff); *J.F. Feeser*, 909 F.2d at 1539 ('customer loyalty is compromised at two cents a case'); *Hasbrouck v. Texaco, Inc*., 842 F.2d 1034, 1041 (9th Cir. 1987) (price differences over many years of 2.5 to 5.75% substantial in gasoline retailing), aff'd, 496 U.S. 543 (1990); *Rose Confections, Inc. v. Ambrosia Chocolate Co.*, 816 F.2d 381, 387-89 (6th Cir. 1987) (absorption of $300,000 in freight over two and one-fourth years); *United Biscuit Co. of Am. v. FTC*, 350 F.2d 615 (7th Cir. 1965) (grocery stores typically operate on very low margin), cert. denied, 383 U.S. 926 (1966).

[40] [ABA:] See, e.g., *Chrysler Credit Corp. v. J. Truett Payne Co*., 670 F.2d 575, 581 (5th Cir. 1982) (less than $11 per car), cert. denied, 459 U.S. 908 (1983); *S & W Constr. & Materials Co. v. Dravo Basic Materials Co*., 813 F. Supp. 1214, 1222 (S.D. Miss. 1992) (4% advantage involving five transactions over a nine-month period did not support inference of injury), aff'd without op., 1 F.3d 1238 (5th Cir. 1993); *Mays v. Massey-Ferguson, Inc*., 1990-1 Trade Cas. (CCH) ¶ 69,028, 1990 U.S. Dist. LEXIS 10245 (S.D. Ga. 1990) (single sale not substantial); *Dairy King, Inc. v. Kraft, Inc*., 645 F. Supp. 126, 130 (D. Md. 1986) (two-week introductory offer); *Olympia Co. v. Celotex Corp*., 597 F. Supp. 285, 297 (E.D. La. 1984) (discounts of $150 to $235 when plaintiff's expert conceded that $1,000 discount would be de minimis), aff'd on other grounds, 771 F.2d 888 (5th Cir. 1985), cert. denied, 493 U.S. 818 (1989); *Uniroyal, Inc. v. Hoff & Thames, Inc*., 511 F. Supp. 1060, 1068-69 (S.D. Miss. 1980) (less than $200 de minimis); *Petroleum for Contractors, Inc. v. Mobil Oil Corp*., 493 F. Supp. 320, 326 (S.D.N.Y. 1980) ($1,413 on sales of $3 million de minimis); *Fred Bonner Corp.*, 57 F.T.C. 771 (1960) (3% price difference on one toy not substantial when standard mark-up was 41%). But see *Chroma Lighting v. GTE Prods. Corp*., 111 F.3d 653 (9th Cir.), cert. denied, 522 U.S. 943 (1997) (2.38% price difference could be actionable under the circumstances presented).

sufficient to establish competitive injury in a secondary line injury case.[41] Although some decisions have reached a contrary conclusion,[42] they are still in the minority.

Even where a substantial price difference exists, the *Morton Salt* inference may be rebutted. The Supreme Court stated in *Falls City Industries v. Vanco Beverage, Inc.*[43] that 'this inference may be overcome by evidence breaking the causal connection between a price differential and lost sales or profits.'[44] In *Boise Cascade Corp. v. FTC*,[45] the D.C. Circuit reasoned that 'the inference can also be overcome by evidence showing an absence of competitive injury within the meaning of Robinson-Patman'[46] and held that proof that disfavored customers have prospered may rebut the inference.[47] **A number of courts, however, have declined to follow the D.C. Circuit's approach.**[48]

33. In the 2000 case of *McCormick & Co., Inc.* (Docket No. C-3939), F.T.C. Chairman Robert Pitofsky and two concurring Commissioners said the following which illustrates that agency's approach:[49]

Under the Supreme Court's controlling decision in *F.T.C. v. Morton Salt Co.*, injury to competition at the retailer (i.e., 'secondary') level **can be inferred where substantial and durable price discrimination exists**

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[41] [ABA:] See, e.g., *George Haug Co. v. Rolls Royce Motor Cars, Inc.*, 148 F.3d 136, 143-44 (2d Cir. 1998); *Chroma Lighting*, 111 F.3d at 657; *J.F. Feeser*, 909 F.2d at 1535; *Alan's of Atlanta*, 903 F.2d at 1418; see also *Coastal Fuels of Puerto Rico, Inc. v. Caribbean Petroleum Corp.*, 79 F.3d 182, 189 (1st Cir.), cert. denied, 519 U.S. 927 (1996); *Hasbrouck*, 842 F.2d at 1040 ('injury to competitors may be probative of harm to competition'); *Allied Sales & Serv. Co. v. Global Indus. Techs., Inc.,* 2000-2 Trade Cas. (CCH) ¶ 72,953, 2000 U.S. Dist. LEXIS 7774 (S.D. Ala. 2000).

[42] [ABA:] See *Richard Short Oil Co. v. Texaco, Inc.*, 799 F.2d 415, 420 (8th Cir. 1986); *Motive Parts Warehouse v. Facet Enters.*, 774 F.2d 380, 393-95 (10th Cir. 1985); *Bob Nicholson Appliance, Inc. v. Maytag Co.*, 883 F. Supp. 321, 326 (S.D. Ind. 1994) (evidence that plaintiff paid higher price than competitor did not prove injury to competition); *RSI Wholesale v. Rollex Corp.*, No. 1:92-CV-603, 1993 U.S. Dist. LEXIS 15839, at 5 (W.D. Mich. Oct. 15, 1993) ('Injury to a specific competitor, without more, ... is not enough to show that price discrimination may substantially lessen competition.'); *Oreman Sales, Inc. v. Matsushita Elec. Corp. of Am.*, 768 F. Supp. 1174, 1185 (E.D. La. 1991) ('one competitor's mere inability to compete is not actionable *per se*' under Robinson-Patman Act).

[43] 460 U.S. 428 (1983).

[44] At 435.

[45] 837 F.2d 1127 (D.C. Cir. 1988).

[46] *Id*. at 1144.

[47] [ABA:] *Id.* at 1135. On remand, the FTC held that there must be evidence connecting disfavored customers' overall growth and their performance in the relevant product market. 113 F.T.C. 956 (1990).

[48] [ABA:] *Chroma Lighting*, 111 F.3d at 658 (rejecting argument that the *Morton Salt* inference can be rebutted by proving an absence of injury to competition); *Coastal Fuels*, 79 F.3d 193-94; *Allied Sales & Serv. Co.,* 2000-2 Trade Cas. (CCH) ¶ 72,953 at 88,122-23, 2000 U.S. Dist. LEXIS 7774 (suggesting, but not deciding, that the Eleventh Circuit would follow *Chroma Lighting* and reject *Boise Cascade*).

[49] The statement is included in the record as part of Nationwide Poles's Supplementary Information.

> **between competing purchasers who operate in a market with low profit margins and keen competition.**
>
> … The fact remains that favored chain store buyers received from a dominant seller **substantially better discounts** than disfavored buyers, **and they were injured**, **and competition at the secondary line was injured, as a result**.
>
> … The Commission was **influenced in the decision to enforce the Robinson-Patman Act here because McCormick is a dominant seller.** Our [dissenting] colleagues' conclusion that market dominance by the discriminating seller should be irrelevant to secondary-line price discrimination flies in the face of commentary by leading scholars such as Herbert Hovenkamp suggesting that the dominance of the seller is exactly the factor that should be examined in the exercise of prosecutorial discretion.[50]
>
> … [T]here will be circumstances in which the *Morton Salt* presumption is appropriate and dispositive. There may be other market settings in which it makes sense for the Commission, **as a matter of prosecutorial discretion**, or the Commission and Courts, in the process of considering whether there has been a violation, to look past the *Morton Salt* factors to a broader range of market conditions to determine whether there has been real injury to competition. Taking those additional factors into account, the majority concluded that there was injury not just to the disfavored buyers, but to secondary-line competition generally.

34. Turning then to our conditions: A supplier firm with <u>market power</u> (i.e. whose customers are effectively captives) engages in <u>persistent price discrimination</u> against its smaller customers, unjustified by differences in the unit cost of the various quantities supplied. The <u>degree and duration</u> of the price discrimination are <u>both substantial</u>. This should be enough to create a *prima facie* case of a likely effect of substantially impeding competition in the customers' market (i.e. in the secondary line), in the sense at least that firms subject to the adverse substantial discrimination are likely to be substantially handicapped in <u>expanding competitively</u> within that market (all else being equal). This requires no 'speculation', as the CAC seems to

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[50] Pitofsky *et al* say: '*See, e.g.,* Herbert Hovenkamp, *Market Power and Secondary-Line Differential Pricing,* 71 Geo. L.J. 1157, 1170 (1983) ("Systematic, long-term price discrimination can be achieved only by a seller with market power. If the seller does not have market power, purchasers asked to pay the higher price will purchase from another seller willing to sell at a more competitive price.")'

have thought; it follows obviously from the degree and duration of the discrimination itself — as the whole bench of the U.S. Supreme Court in *Morton Salt* was able to recognise, and as I think would be recognised by almost everyone on the Clapham omnibus.

A *'prima facie'* case

35. A *prima facie* case becomes a sufficient case (proof on a balance of probabilities) in the absence of an answer. *Prima facie* proof is proof which, if not effectively rebutted or qualified by the respondent, may at the end of the case justifiably be considered by the trier of fact and fact-based issues as having hardened into conclusive proof.[51] The burden is on every litigant to adduce evidence to answer (i.e. rebut) a *prima facie* case (or defence) put up by the opponent. This is a different matter from, and applies regardless of, the legal incidence of the ultimate *onus* of proof on any issue.[52] Thus the ultimate burden of proof is not changed: it remains on the complainant or the Commission to prove all the elements of the prohibition on a balance of probabilities. I agree with the point made by Sasol that the burden of proof cannot alter just because the one seeking to discharge it is poorly resourced. But in order to establish proof on a balance of

[51] See *Salmons v Jacoby* 1939 AD 588 at 593; *SM Goldstein & Co (Pty) Ltd v Cathkin Park Hotel (Pty) Ltd and another* 2000 (4) SA 1019 (SCA) at 1023J, 1025E-G; *S v Boesak* 2000 (3) SA 381 (SCA) at 396D-H; *South African Veterinary Council and another v Veterinary Defence Association* 2003 (4) SA 546 (SCA) at 556A-B. Where inferences from facts are relied on to form a *prima facie* case, the inferences must at least be ones which may reasonably be drawn from the facts. In *Laugh It Off Promotions CC v South African Breweries International (Finance) B.V. t/a Sabmark International and another* 2005 (8) BCLR 743 (CC), the Constitutional Court has observed that 'ordinarily probability is a matter of inference to be made from facts consistent with the inference.' (Case CCT 42/04, as yet unreported, par [54].) Absent facts consistent with the inference, the inference cannot properly be drawn, and a probability of material detriment cannot be founded on conjecture alone. (Cf *id.*, par [59].) To harden into conclusive findings those inferences must, in the end, be the more natural or acceptable from several conceivable ones: *Hülse-Reutter and others v Gödde* 2001 (4) SA 1336 (SCA) at 1344C-F.

[52] See *Neethling v Du Preez and others; Neethling v The Weekly Mail and others* 1994 (1) SA 708 (A) at 761B-762G. Cf also *Sjelbreds Rederi A/S and others v Hartless (Pty) Ltd* 1982 (2) SA 710 (A) at 733F-G.

probabilities, one may rely ultimately on *prima facie* proof which, at the end of the case, has not been rebutted by the defence. This is a perfectly ordinary feature of litigation.[53]

36. I am not talking here of the defence having to prove pro-competitive effects to offset the harmful ones: I doubt that section 9 would permit that. I am talking simply of rebuttal of the *prima facie* proof of likely prevention, hindering, impeding competition. For example, realistic prospects of collective buying or arbitrage at insubstantial extra cost would in principle defeat a complaint of price discrimination because the likelihood of competition being substantially prevented (hindered or impeded) could in such a case not be proved. However, for reasons evident from the record (but which would take too long now to set out),[54] I do not think that a defence along those lines was ever realistic in the Nationwide Poles case.

'Substantial'

37. When does a likelihood of harm become 'substantial'? 'Substantial' is a comparative or relative concept, depending upon the context in which the word is used as well as broader considerations of the legislature's purpose in using it. I would agree with Sasol's counsel that, contrary to what the Tribunal held, 'substantial' must mean something more than non-trivial — if by trivial is meant so minor as

[53] See e.g. *Smith's Trustee v Smith* 1927 AD 482 at 487: 'As was pointed out by INNES, C.J. in *Ohlssons Cape Breweries* 1909 TS 98 in most cases the *onus* is not shifted; it remains upon the plaintiff, but the question always is whether at any stage there is sufficient evidence before the Court to entitle the plaintiff to judgment in the absence of sufficient evidence to the contrary on the part of the defendant.'

[54] See 2nd lecture, footnote 16.

to be irrelevant.[55] Merely trivial price differentiation would, on the principle *de minimis non curat lex*, not amount to discriminating in price in any intelligible sense and could not at all be the object of the prohibition. No words are needed in a statutory provision to express that; it is implicit everywhere. Due weight must thus be given to the legislature's express use of the word 'substantial' in the context of section 9(1)(*a*). 'Substantial' ordinarily means material or considerable in amount and duration.[56] 'Considerable' means large enough to be worthy of consideration, of some importance; and 'material' means 'of serious importance'.[57] A substantial effect is consequently an effect sufficiently weighty to be taken seriously.[58]

38. Sasol's price differentials which formed the subject of the complaint were of an order that has routinely been held sufficient to establish secondary-line injury in terms of the Robinson-Patman Act in the United States.[59] Over a sustained period, customers least favoured paid prices for bulk creosote some 18% to 20% higher than those most favoured. Calculations by Mr Malherbe on Sasol's behalf showed that the net effect was to raise the relative costs of firms in the position of Nationwide Poles — and thus constrict their relative

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[55] Cf the Tribunal's reasons for decision, pars 103, 109 and 188.

[56] See e.g. *The Chambers Dictionary* (1998). *Webster's Third New International Dictionary* gives for 'substantial': 'something of moment : an important or material matter, thing, or part.'

[57] *Id.*

[58] It is unnecessary to consider (and the Tribunal did not discuss) Nationwide Poles's allegations of individual and relatively minor instances of 'discrimination' by Sasol unrelated to the price list. Even if proved, these would be legally irrelevant. Only discrimination which is substantial in extent — and this would ordinarily though not invariably include a substantial duration — could suffice to prove a *likelihood* that it will have the effect of substantially preventing or lessening competition. Moreover, in regard to discrimination in the cost of transportation, there is no evidence that Nationwide Poles could not switch to alternative transport services. (See in this regard Mr Unterhalter's cross-examination of Mr Foot, Transcript 4 August 2004, pages 74-77.)

[59] See footnote 40 above. See also the review of the case law in *Discount as a cause of secondary-line competitive injury under § 2(a) of Clayton Act, as amended by Robinson-Patman Price Discrimination Act (15 U.S.C.A. § 13(a))* 172 A.L.R. Fed. 267, by Ann K. Wooster, J.D.

margins — by some 3.6% to 3.8%.[60] This seems to me a conservative estimate, but in any event it should be quite enough to count as ‘substantial’. Mr Foot was surely right in arguing also that the longer the price discrimination persists, the greater is the cumulative handicap.

39. Mr Foot gave uncontested evidence that price discrimination impeded competition by Nationwide Poles because it reduced the working capital available for expansion.[61]

> We are paying more. It affects our cost structures. By affecting our cost structures, by definition it prevents me from … it doesn’t prevent me from competing. [Here Mr Foot uses ‘prevent’ in the sense of actually stopping.] **It lessens my ability to compete and to grow, because my working capital gets taken away from me and it sits in somebody else’s pocket**.

Surely this was *prima facie* evidence of a likely substantial hindering of competition, assuming that the price discrimination were to persist (and one must assume that where discrimination is systematic). The fact that Nationwide Poles was able to increase its turnover substantially after Mr Foot bought the business and injected working capital does not in any way indicate that the impediment to competition which price discrimination inherently creates is insubstantial. Even proof of increased turnover would not prevent an inference of harm in the case of substantial discrimination, where there is no reason to doubt that turnover could have increased even

[60] See Transcript 6 August 2004, pages 450and 499; this seems to have become common cause.

[61] See Transcript 4 August 2004, pages 28-29 and 35. Dr Roberts said (Transcript 23 November 2004, page 282): ‘I think if some competitors pay higher prices, then it makes them less able to compete. It makes them less able to invest in new equipment. It makes them less able to price keenly in their output market, etc.’ This seems irrefutable.

more but for the discrimination.[62] As Nationwide Poles argued in par 6.15 of its heads in the Tribunal:

> Price discrimination impairs cash flows and costs relative to that of a preferred competitor. Since cash flows are often crucial to the small business, the reduction in cash flow must be financed from working capital. Working capital is necessary to finance ongoing operations and to tide the manufacturing process over market slumps or over cyclical periods of low demand. Reduced working capital limits the ability to a company to compete for large orders, arrange beneficial supply contracts, arrange loan facilities and ultimately expand the business and compete more aggressively. As a consequence of diminished working capital, the competitive capacity of the small treatment plant is substantially lessened.

A substantial impediment to competition thus follows directly from substantial and sustained discrimination, as Mr Foot argued in the CAC.[63]

40. The CAC seemed ultimately to decide the case on the idea that Mr Foot had not proved that he could not get supplies at a favourable price from Suprachem. But, as I have raised during the second lecture, this idea surely evaporates when one makes a full analysis of the evidence concerning market power, and the interplay between Sasol and Suprachem over creosote customers. It would have been

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[62] In the Nationwide Poles case, the business was effectively moribund until Mr Foot took it over and injected capital. Its increase in turnover is not thus not readily to be judged as proof of an absence of appreciable adverse effect through price discrimination.

[63] See par 48 and the first part of par 49 of his written submissions. Despite the flaws in its interpretive reasoning, the Tribunal came ultimately to conclusions in its reasons for decision which in fact did no violence to a proper construction of section 9(1)(*a*), and were quite consistent with the approach in *Morton Salt*): '[Par 125] • The discount structures for the sale of creosote exhibit a material differentiation as between the most and least favoured customers; • Creosote is a significant input cost of firms such as the complainant who compete in the treated poles market against rivals who benefit from the price discrimination; • That is it is 'likely' that the complainant and firms similarly situated presently in the market and new entrants, will be less effective competitors as a result of the discrimination; …[and, Par 126] It follows that if firms such as the complainant are rendered less effective competitors that this will have an effect on the competitive structure of the market and so it is likely that this will substantially lessen or prevent competition in the market, in the sense understood by the legislature for the purpose of section 9(1)(a).' The attention of the CAC was drawn to these passages by the *amicus curiae*, Adv N H Maenetje, who argued (par 31-32 of his submissions): 'If such conclusion is supported by the facts as reflected in the record, the conclusion should not be disturbed on account of a finding that the Tribunal's interpretation of section 9(1)(a) is incorrect.'

better, indeed, if detailed evidence had been presented of Suprachem's prices and supplies. As it happens, there was evidence (acknowledged in Sasol's heads in the CAC, par 8.14) that Suprachem's creosote prices in 2003 were above those of Sasol. But even in the absence of that, was there nevertheless not a *prima facie* case that small customers were effectively captive under the market power manifested in the persistent price discrimination by Sasol? And that Suprachem did not provide a competitive escape? I would say there was such a case, a case requiring an answer.

41. The ability of a small firm to generate a so-called 'reasonable gross margin' despite price discrimination does not show that price discrimination is unlikely to have a substantial effect in impeding competition, in hindering competitive expansion.[64] What would be the margins, by comparison, of those getting the favoured price? The fact that new entry is relatively cheap and easy in creosote-treatment does not tend to reduce, but on the contrary tends to increase, the likelihood of a substantial impediment to competition resulting from substantial price discrimination. It is precisely in those markets in which small and medium-sized enterprises could be expected to flourish, that price discrimination — all else being equal — should be expected to have its most anti-social effects.

42. In paragraph 87 of its reasons for decision, the Tribunal said (and, with respect, I agree):

> In our view the relevant, that is, the *South African,* legal and political economy context favours competition enforcement that is concerned to protect the market mechanism from conduct that has the effect of undermining it. The expressed concerns of the South African lawmakers

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[64] Cf e.g. Transcript 5 August 2004, pages 172-173.

> and the policy planners support this finding. This is powerfully manifest, *inter alia*, in an industrial policy that places the development of SMEs at the centre of attempts to improve the workings of the market mechanism. This conclusion is grounded not only in an examination of the general industrial policy context in which concern for SME development looms large but also in an examination of the Act itself.

43. What must be emphasised is that the CAC judgment, despite the different result, took pains to confirm the Tribunal's reasoning that the promotion and preservation of the <u>mechanism of competition</u> is a vital object running throughout the Competition Act, and in this regard the fate of small businesses, and the fairness of their opportunities to compete, is of fundamental concern. While the Act seeks to protect competition rather than competitors, as the Tribunal put it: 'no competitors, no competition'.[65]

44. Let me quote to you from the concluding part of Mr Foot's submissions to the CAC: [66]

> It is not classified information that small business has a dismal rate of success. This is common knowledge and has been well publicized. It is unlikely that any entrepreneur would commit capital to a venture that offered sub-normal returns or which seemed bound to failure because of competitive compromise. Effort and commitment are a prerequisite to capital investment in any business, especially small businesses where the owner may stake all on a venture. And yet, small businesses regularly fail, and one reason is not hard to find. The reason is fundamentally related to abuse of power, either monopsony or monopoly. These are structural matters that will only be stopped by process of law, for the profits of anti-trust vastly outweigh the potential costs of being found out. …
>
> Any action or decision that dulls our future competitive edge will do a disservice to our propensity to compete into the future, and hence will adversely affect the lives of forthcoming generations. If we are to compete effectively into the future, the keen edge of entrepreneurial energy is to be cherished, nurtured and supported in the competitive arena of commerce. It should not be diminished. In order to do this, legal process must play its part in ensuring equitable participation.

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[65] Par 86.

[66] Par 79 and par 83.

45. I have stated several criticisms of the CAC judgment. But we must maintain a sense of proportion. The CAC judgment gives no comfort to those, normally representatives of big firms with market power, who would prefer to see section 9 made a dead letter, and for their existing pricing practices to continue without disturbance or re-evaluation. The judgment advances certainty in regard to the policy behind section 9 in very important respects. It is true there are aspects, including important ones, still to be ironed out. But they can be ironed out. It is true that, when it comes to a successful price discrimination prosecution, the mountain has not yet been climbed. But no-one should draw the conclusion that it cannot be climbed. That remains something for the Competition Commission in a suitable case — or, failing it, a complainant itself — to undertake.