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# DENEYS REITZ
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## COMPLEX MONOPOLIES AND MARKET INQUIRIES

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The primary concern from a competition law perspective for merging parties has to date been whether the merger will receive approval from the competition authorities. Emerging trends and changes to the competition legislation have introduced additional factors that dealmakers should be aware of.

This presentation will provide a brief overview of two particular amendments to the Competition Act, 1998, namely the introduction of complex monopoly provisions and the formalisation of the market inquiry process. It will also address possible risks in the context of mergers and acquisitions.

**Complex Monopoly Conduct**

Once the Act comes into force, the Commission will have new powers to investigate and prohibit "complex monopoly conduct".

According to the DTI the complex monopoly provisions were introduced because the Commission's ability to investigate and take action against multi-firm conduct is inhibited by the requirement that a specific contract or agreement must exist. It seems that this new provision is intended to assist the competition authorities to address conduct by firms in concentrated industries, like fertilizers or

chemicals, where the Commission has found it difficult prove that conduct regulated in section 4(1)(b) of the Act, namely price fixing, market division or collusive tendering, is occurring.

This has been a much debated amendment to the Competition Act, primarily because the concept of complex monopolies is based on English legislation which was ultimately abandoned, as unworkable, in favour of general market inquiries. The amendments also introduce formal market inquiries and consequently many of the arguments around this topic have centred on whether the complex monopoly provisions are required at all. What we do know however, is that these provisions are here to stay and it is therefore important that you are aware of the possible implications of these provisions.

So what exactly is a complex monopoly? According to the DTI "*complex monopoly occurs where two or more firms act in a cooperative manner or conduct their business affairs in a coordinated way without specific contact or agreement e.g. parallel pricing, common trading policies, exploitative pricing to downstream players/consumers".*

The amendments to the Act define complex monopoly conduct as existing in a market if:

> *"(a) at least 75% of the goods or services in that market are supplied to, or by, five or fewer firms;*
> *(b) any two or more of the firms contemplated in paragraph (a) conduct their respective business affairs in a parallel conscious manner or co-ordinated manner, without agreement between or among themselves; and*
> *(c) the conduct contemplated in paragraph (b) has the effect of substantially preventing or lessening competition in that market,*
> *unless a firm engaging in the conduct can prove that any technological, efficiency or other pro-competitive gain resulting from it outweighs that effect."*

Conscious parallel conduct is defined as occurring when *"two or more firms in a concentrated market, being aware of each other's action, conduct their business affairs in a cooperative manner, without discussion or agreement."* The obvious difficulty with this definition is that the majority of South African businesses operate in a concentrated market and being aware of your competitors' activity is the only way to ensure that you pitch your products at the correct level and pricing.

Due to our history, the South African market is one defined by significant concentration and in many cases hugely dominant players. Consequently one does not have to search far to find an industry that would fall within the definition of a complex monopoly, for example, cement, reinsurance, telecommunications, and pharmaceuticals. The Commission recently announced its investigation into the retail supermarket sector. What is interesting about this is that the complaints are not cartel complaints but rather are based on abuse of dominance contraventions and restrictive agreements. It seems that the retail supermarket industry would have been the perfect candidate for the application of the complex monopoly provisions.

The Commission is empowered to initiate an investigation into what it believes to be complex monopoly conduct without having received a complaint from a customer or competitor.

If the Commission concludes that firms are engaged in complex monopoly conduct, and establishes that two or more firms in the relevant market have at least 20% of the market, then it may apply to the Tribunal for an order "*reasonably requiring, prohibiting or setting conditions upon any particular conduct by the firm, to the extent justifiable to mitigate or ameliorate the effect of the complex monopoly conduct on the market"*.

The conditions that must exist in order for the Tribunal to order a remedy are extremely broad and include not only conduct which resulted in "high barriers to entry" or "excessive pricing within that market" but also any "other market characteristics that indicate co-ordinated conduct". There is speculation as to the extent of remedies that may be imposed on firms engaging in complex monopoly conduct, that is, whether they will merely be behavioural remedies or whether a remedy so drastic as divestiture would be required by the Tribunal. Importantly, contravening of such an order is a prohibited practice and subject to the payment of an administrative penalty of up to 10% of turnover. A contravention in terms of this provision does not fall within the ambit of possible criminal liability.

**Market Inquiries**

The concept of a market inquiry is not new to South Africa as the Commission has already conducted a market inquiry into the retail banking sector. There was however, no statutory basis for that inquiry. The Commission relied on its general powers to "*inquire into any matter concerning the purposes of*

*the Competition Act"*, but there is no express provision authorising market inquiries or setting out the extent of the Commission's powers in relation to market inquiries. As there was no express provision authorising the banking inquiry, the process was effectively voluntary in nature. Therefore, the outcome of the banking inquiry was dependant on the assistance of those wishing or willing to submit relevant information to the inquiry. The new section 4A makes explicit provision for the initiation and conduct of market inquiries and therefore provides a statutory basis for the conduct of market inquiries.

Such an inquiry may be initiated in response to a request by the Minister, or the Commission can decide to undertake a market inquiry by simply publishing a notice in the government gazette, even without receiving any complaints.

The new provisions confer on the Commission the power to issue summonses and question any person under oath. They are also empowered to conduct dawn raids in relation to a market inquiry. As a result any market inquiries embarked on in future are likely to be significantly more formal and robust than the banking inquiry. There are still concerns however, regarding the significant drain on the Commission and inquiry participants' resources.

What are the possible outcomes of a market inquiry?

Based on information obtained through a market inquiry the Commission may:

- initiate a complaint with or without further investigation. That complaint may then be settled with the Commission or immediately referred to the Tribunal;
- may report to the Minister of Trade and Industry and recommend new or amended policy legislation or regulation or make recommendations to other regulatory authorities in respect of competition matters;
- take any other action within its powers in terms of the Act and included in the report of the market inquiry ;
- take no action.

## International Trends

If there is one thing that we have learned is that there is definite 'collusion' between enforcement agencies around the world. The competition authorities talk to one another and one can almost be certain that if there has been an investigation or inquiry into a particular sector elsewhere in the world that South Africa will not be far behind in looking into those sectors. This has been seen in relation to the construction industry, cement, retail banking and now retail supermarkets. As such it is wise to be aware of some of the international trends.

Market inquiries are a regular feature of EU and UK competition law which enable the relevant authorities to understand particular markets and make recommendations regarding the redress required to ameliorate deficiencies in the market adversely affecting consumers.

The EU has conducted market inquiries into the following sectors:

- Pharmaceuticals;
- Insurance;
- Energy (Gas and Electricity); and
- Retail Banking.

Market inquiries conducted by the OFT include:

- Grocery Stores;
- New Cars;
- Package Holidays;
- BAA airports (the first CC market investigation where structural remedies were imposed – BAA ordered to divest 3 major airports, despite there being no evidence of anticompetitive conduct by BAA);
- Payment protection insurance;
- Personal banking;
- Home credit; and
- Store cards.

**Risks for Deal Makers:**

So what does this mean to you, as deal makers? These developments significantly expand the Commission's investigative powers and in particular the scope of what they may investigate. There are significant risks in entering into a market that is subject to or likely to be subject to a complex monopoly investigation or market inquiry:

- Lengthy inquiries/ investigations do result in high legal costs and substantial lost management time
- Obtaining merger clearance in sector involved in these proceedings may be delayed and/or difficult.
- The costs of restructuring because of conditions imposed after complex monopoly investigation or legislative changes introduced as a result of a market inquiry.
- Decrease in profitability as a result of structural changes to the market
- Costly Administrative Penalties

Consequently, when considering the viability of a deal, these costs need to be factored into valuations and investment decision making. Based on the Commission's current focuses in its investigations, as well as taking international trends into consideration, the sectors that are potentially at risk of such investigations or inquiries are construction, retail banking, food value chain (including supermarkets), insurance, telecommunications, chemicals and pharmaceuticals.

**Conclusion:**

It remains to be seen how effectively the Commission will use the new weapons in its arsenal however, the Commission has been increasing its capacity and is likely to take full advantage of the extended powers given to it by these amendments. Parties should ensure that due diligence exercises are comprehensive to reduce potential difficulties down the line.

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