Organisation for Economic Co-operation and Development

DAF/COMP/WD(2023)29

Unclassified

English - Or. English

19 May 2023

DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE

Advantages and Disadvantages of Competition Welfare Standards – Note by South Africa

15 June 2023

This document reproduces a written contribution from South Africa submitted for Item 6 of the 140th OECD Competition Committee meeting on 14-16 June 2023.

More documents related to this discussion can be found at https://www.oecd.org/competition/advantages-and-disadvantages-of-competition-welfare-standards-in-competition.htm

Antonio CAPOBIANCO
Antonio.Capobianco@oecd.org, +(33-1) 45 24 98 08

JT03519217

South Africa

1. Introduction

1. This note sets out the Competition Commission of South Africa's ("the Commission") response to the call by the Organisation of Economic Cooperation and Development ("OECD") for written submissions to inform the roundtable discussion on the Consumer Welfare Standard – advantages and disadvantages compared to alternative standards at the meeting to be held in June 2023.

2. The background note for the Roundtable session recognises that welfare standards in competition policy have been the subject of much debate and that this debate is multi-faceted. Simply put, the standard for competition policy sets out how the relevant authority, be it an administrative body or the court, discerns positive outcomes from negative ones. The standard provides the underlying principle to how competition law is interpreted. Within this context, it is therefore not surprising that the appropriate standard for competition policy is a much-debated topic.

3. The approach undertaken by the Competition Commission of South Africa ("CCSA") with the public interest provisions introduced in our merger analysis, has historically attracted international attention and acted as benchmark of when an 'alternate standard' may be employed in competition policy. The experience of the CCSA in its application of the law given the particular historical context of the country as well as the legislated provisions in the Act has meant that the emerging jurisprudence has provided indicators on how to apply certain standards to the Act. This submission sets out the views of the CCSA on the issue of the consumer welfare standard, along with examples of how alternate standards have been employed by the authority in the various enforcement and merger analysis undertaken.

2. The Consumer Welfare Standard

4. The consumer welfare standard is the economic model for decision-making employed by antitrust enforcers to determine whether a business conduct deserves antitrust restraint or not. It focuses solely on the surplus gains for consumers and disregards the efficiency gains for producers. Thus, a competition system guided by the consumer welfare standard, has as a goal the maximization of consumers' benefits. With the adoption of the consumer welfare standard, other public interest considerations — such as unemployment, discrimination or protection of small businesses — do factor into the antitrust analysis.

5. The benefits of enforcing antitrust norms under the consumer welfare standard are considered to be:

- First, it enhances predictability and legal certainty since businesses have clear guidance about which test their practices will be subject to.
- Second, since the consumer welfare standard is an economic analysis-based test — i.e. non-economic considerations are not factored into this pro-consumer test — enforcement coherence is preserved.

6. However, the inability to consider the impact of mergers and conduct on economic development, inequality and more vulnerable economic actors such as labour and SMEs, is also a clear downside to the consumer welfare standard. In all other areas of economic

policy, decision-making involves trade-offs between economic efficiency and other socio-economic outcomes. For instance, in trade policy, there is a balance between consumer welfare, which may demand a completely free trade regime, and industrialisation or employment objectives which may demand a degree of protection. As consumers are also employees and/or shareholders, a total welfare standard that considers these factors seems appropriate and is widely employed by countries globally in trade policy. In this respect, antitrust is fairly unique in focusing exclusively on consumer welfare and not other economic objectives.

7. A review of contributions by antitrust law scholars indicates that the idea to look beyond consumer welfare (in the narrow sense of price effects) is receiving broader acceptance. Fox (1981) submitted that "antitrust should be modernized" and that the law must become responsive to the societal needs for enhanced efficiency, in the interests of consumers.[1] This was echoed by Stiglitz (2015) where he highlights that use should be made of a 'public interest test' as competition policy should be concerned not just with the existence of competition, but with the nature of competition.[2] He emphasises that a new benchmark model is required, one in which departures from competition are the norm rather than the exception and where authorities, in their role of checking against abuses of power, acknowledge that competition policy is about reducing inequalities in some fundamental sense. Similarly, Johannes Laitenberger (2017), former Director General for Competition at the European Commission also highlighted that the EU legal framework for competition is not only focused on short-term price effects, they are also interested in "competition in the longer term, and not only on price".[3]

8. The ability to achieve a certain level of convergence may also be attributed to the fact that the provisions on competition aspects are similar to the provisions in laws of mature jurisdictions like Canada. Certain public interest provisions as found in South Africa also feature in industrialized countries, namely promotion of small businesses and promotion of the ability of national firms to compete in international markets. The Canadian Competition Act has specifically incorporated such objective and it may be a consideration in certain mergers.[4]

9. Whilst those favouring the consumer welfare standard often argue that these other objectives may be pursued through other policy tools, this is not entirely satisfactory where antitrust decisions may undermine those other socio-economic objectives resulting in economic policy incoherence, or where antitrust can contribute to those objectives but fails to do so. This is in the context where mergers and market conduct directly shape the economy and economic outcomes. It is for this reason that South Africa, and many other African jurisdictions, have sought to incorporate objectives other than consumer welfare into their competition legislation in various ways.

[1] Eleanor M. Fox, Modernization of Antitrust: A New Equilibrium, 66 Cornell L. Rev. 1140 (1981) Available at: http://scholarship.law.cornell.edu/clr/vol66/iss6/3

[2] https://www8.gsb.columbia.edu/faculty/jstiglitz/sites/jstiglitz/files/Towards%20a%20Broader%20View%20of%20Competition%20Policy.pdf

[3] https://ec.europa.eu/competition/speeches/text/sp2017_15_en.pdf

[4] https://ised-isde.canada.ca/site/competition-bureau-canada/en/how-we-foster-competition/promotion-and-advocacy/regulatory-adviceinterventions-competition-bureau/submission-oecd-public-interest-considerations-merger-control

3. The Broader Public Interest in South Africa

10. The South African Competition Act No. 89 of 1998 (the Act) was predominately drafted based on the legislation and jurisprudence of more mature jurisdictions, such as the European Commission, the United States of America (US) and Canada. Whereas the purposes of the Act and merger control provisions uniquely included the public interest, the chapter on prohibited practices reflected both the legal tests and liability standards of those more mature jurisdictions. The legal standards included per se prohibitions for naked cartel conduct[5] and minimum resale price maintenance only, and a rule of reason approach for all other practices where the conduct could be justified by respondents by proving any off-setting technological, efficiency or pro-competitive effects. For prohibited practices, the requisite standard to prove liability under a rule of reason analysis was the consumer welfare standard established through the substantial prevention or lessening of competition (SPLC) test. The same SPLC test prevails in merger control for the competitive assessment, although a separate assessment of the merger's public interest effects is also required which is assessed by measuring the impact on specified public interest factors.[6]

11. It is further noted that the consideration of South Africa's political and economic history underpins the manner in which the Act was drafted. One need only look to the preamble and other parts of the Act in which themes of equity and justice run like a common golden thread. For example, the preamble refers to the political background and motivations for the Act, including policies of equity, distribution and efficiency. It also states that the Act seeks to address past practice of apartheid, which led to excessive concentration of ownership and control, inadequate restraints on anti-competitive trade practices, and unjust restrictions on full and fair participation in the economy. Elsewhere in the preamble, it is stated that a competitive environment which balances the interests of all stakeholders and is focused on development will benefit all South Africans. SME development as well as black economic empowerment received special attention in the Act because of the previous structure of the South African economy. The high levels of concentration that existed in many industries were considered to be barriers to entry especially for smaller enterprises. Further, promoting a broader spread of ownership; especially among historically disadvantaged persons, reflected concerns about the skewed distribution of income and wealth in South Africa. A more even spread of ownership was deemed to be important to ensure longer-term balanced and sustainable development.

12. The Act aside, continuous policy development in South Africa in subsequent years has seen the public interest continue to be a prominent actor. For example, public interest factors have found expression through the Competition Commission's ("Commission") approach to sector prioritization. Public interest considerations have also found expression in market inquiries, for example the health-care inquiry included in its statement of issues a number of theories of harm as well as an assessment of the effect on public interest issues including employment, the impact on small and medium-sized enterprises and the spread of ownership in the economy. The Grocery Retail, Mobile Data and OIPMI inquiry also had particular focus on SMEs.

[5] This included agreements amongst competitors to fix prices, divide markets or tender collusively. See South African Competition Act 1998 s 4(1)(b).

[6] These included, prior to amendment, the effect of the merger on (a) a particular industrial sector or region, (b) employment, (c) the ability of small businesses, or firms controlled or owned by historically disadvantaged persons, to become competitive, and (d) the ability of national industries to compete in international markets. See Competition Act 1998 s12A(3).

13. Given this context, the note below will discuss the experience the Commission has had in competition enforcement with particular focus on abuse of dominance cases compared to the enforcement record of merger analysis.

4. Relevant Standard in Merger Control

14. The inclusion of public interest in merger control legislation has forced the courts to determine the relevant standard in the assessment of public interest, and to do so in a manner that enables the kind of predictability and certainty that is often ascribed to the consumer welfare standard.

15. The first important innovation is in the construction of the Act which seeks to separate the assessment of a merger based on public interest from the assessment on competition grounds. In other words, a merger is assessed first on competition grounds and second on public interest grounds, with each assessment separate from each other. This has the benefit of avoiding the potential difficulty of weighing up the competitive effects against public interest parameters, such as determining whether to approve a merger by contrasting the price effects against employment effects. This means that the consumer welfare standard continues to be utilised for assessment of the competition effect.

16. For the public interest, the standard is in essence whether the welfare of a particular group (e.g employees, SMEs, historically disadvantaged persons), industrial sector or region is diminished or not. This is what would constitute harm to the public interest. The focus purely on the welfare of a specific group is generally determinable by the court. For instance, in determining whether there is a likely employment effect, it can be determined whether the merger creates overlaps in positions. For the effect on participation by SMEs, evidence as to the use of SME suppliers by the acquiring company relative to the target will assist in determining how SME suppliers may be impacted.

17. The other innovation is that the Commission and the courts have sought to resolve any public interest harm through conditions that ensure the welfare of particular groups, sectors or regions are left no worse off. This is a product of the legislative design whereby the public interest assessment is distinct from the competition assessment. As such, remedial action that disposes of the public interest concern then leaves only the competition assessment based on the consumer welfare standard. Another benefit of the separation is that where no conditions are agreed, then the merger may be prohibited based on the public interest welfare standard alone, even if the competition assessment does not point to a lessening of competition.

18. The inclusion of a public interest welfare standard ensures that merger activity does not undermine specific socio-economic objectives embodied in public policy. The approach is that mergers which pass on the consumer welfare standard but fall on the public interest standard can proceed as long as the public interest harm is remedied. Moreover, the legislative design and jurisprudence on public interest has enabled South Africa to integrate public interest considerations into merger control in a manner that ensures ease of assessment from the courts. It has also enabled legal certainty and predictability for business.

19. The recent amendments to the Competition Act do seek to move beyond a harm-based welfare standard, ensuring the welfare of a specific group is not made worse off by the merger, towards a welfare standard that seeks to actively promote the welfare of specific groups. In particular, the amendment requires under a public interest assessment a determination of whether the merger ‘promotes the greater spread of ownership, in particular by historically disadvantaged persons and workers in firms in the market’. This

is an important shift as it seeks to make use of competition law to assist in achieving a public policy objective rather than simply ensuring competition law does not undermine public policy objectives. It recognises that merger activity brings about changes in the ownership of the economy and therefore is an important point at which the greater spread of ownership may be achieved through public policy, as historically disadvantaged persons and workers may be incorporated in the change of control structure.

20. The jurisprudence in respect of the new dimension to public interest is still developing. However, as part of public interest, the legislative arrangement remains the same insofar as the public interest welfare assessment is distinct from that of the competition assessment. This ensures that the public interest welfare can be assessed independently. Moreover, whilst the welfare standard is not simply defensive, it is evident that the welfare test is now whether a merger achieves a promotion of ownership or an improvement in the welfare of a particular group, namely historically disadvantaged persons and workers. This can be easily established by comparing the pre-merger ownership share of these groups compared to the post-merger shareholding. Where the jurisprudence needs to develop is the extent to which a positive welfare improvement is sufficient to satisfy the legislative amendment.

5. Relevant Standard in Abuse of Dominance

21. The South African experience in abuse of dominance cases is that the consumer welfare standard has not necessarily served competition, as well as the public interest, particularly well. Competition law and the courts are particularly weak in dealing with dynamic effects, as forecasting effects further into the future is far more difficult and therefore uncertain. This has been highlighted recently in respect of the debate on digital markets, resulting in calls for a more presumptive legal standard to deal with the difficulty posed by dynamic market characteristics. Whilst the South African experience confirms such difficulties in respect of digital markets, the focus of this submission is in respect of SMEs and new entrants, particularly by historically disadvantaged persons that were previously excluded from the economy.

22. A healthy dynamic competitive environment requires a strong ecosystem of new entrants and small and medium-sized enterprises seeking to grow and contest the incumbents. That ecosystem allows for the entry and expansion of firms that may be more efficient or innovate in a manner that may disrupt entrenched larger firms. This is most obviously the case in tech markets, but is equally true of traditional markets. As a result of its history, South Africa has a particularly small SME sector, accounting for roughly a quarter of economy turnover relative to over half of economy turnover in OECD countries. The lack of a dynamic SME sector has resulted in a persistence of concentration in most markets, and along with barriers to new entrants, has also resulted in a persistence of an inequitable ownership structure in the economy.

23. However, under the consumer welfare standard adopted in abuse of dominance legislation from other jurisdictions, it has been difficult to establish anti-competitive effects where the complainants are SMEs, which has been the majority of cases since the law was promulgated. The challenge for SMEs is aptly demonstrated in the *Normandien* matter, involving an application brought by a small sawmiller against alleged abuse of dominance

practices by Komatiland Forest. The application was unsuccessful due to the inability to establish an SPLC across the entire market, with the Tribunal reasoning as follows:[7]

> *"Viewed in the best possible light, the applicant has depicted that a single player in a market may have been negatively affected (for example by having to pay a higher price). It does not follow necessarily that this translates into a substantial prevention or lessening of competition in the market as a whole. For such a finding to be reached,... it would have to be found that because of the negative effect on the applicant and the applicant's size/ relevance in the defined market, there has in fact been a substantial prevention or lessening of competition in the market as a whole. This has certainly not been shown and section 8(c) allegation is accordingly dismissed."*

24. The problem with the consumer welfare standard in these instances is that if such conduct against SMEs is pervasive then ultimately there is a greater harm to dynamic competition and the economy arising from the muted participation of such firms. It is this dynamic competition that the consumer welfare standard is not capable of determining accurately given the difficulties courts have with determining longer term dynamic effects with any certainty. The same problem with the consumer welfare standards applies to historically disadvantaged entrants or SMEs, where conduct that negatively affects them will systemically undermine the objective of greater equality and transformation of ownership in the economy. A consumer welfare standard cannot adequately progress that public interest policy concern as it only looks at consumers and not the particular group whose welfare policy seeks to advance.

25. One solution may be to adjust the legal standard to a more presumptive one, as advanced in the context of dynamic digital markets. Another solution is to adjust the liability standard away from the consumer welfare standard to one which considers the impact on the particular group of firms, namely SMEs and historically disadvantaged enterprises, much like in the merger control example. The recent amendments to the competition act have sought to adopt both solutions in respect of specific conduct that is most typically abusive to SMEs, namely the price discrimination and the abuse of buyer power.

26. The amendments to price discrimination in section 9 of the Act now incorporate the additional contravention of prohibited price discrimination 'if it is likely to have the effect of impeding the ability of SMEs or firms owned by historically disadvantaged persons to participate effectively' (section 9(1)(a)(ii)). This is a welfare standard that only considers the impact on the welfare of the prescribed group of firms, namely SMEs and firms owned by historically disadvantaged persons, rather than the broader consumer welfare standard that is still contained in the general provision for all firms, namely demonstrating 'the likely effect of a substantial prevention or lessening of competition'. In determining the impact on that prescribed group of firms, the impede participation standard is used which is clearly a lessor standard than one of competitiveness.

27. Moreover, the amendments include a presumptive provision insofar as where a *prima facie* case is established, then the onus shifts to the dominant firm 'to show that its actions did not impede the ability of SMEs and historically disadvantaged persons to participate effectively' (section 9(3)). This change in legal standard enables a presumption of harm if the essential features of the contravention are established, and it is then for the dominant firm to put up a defence. The amendment also limits that defence insofar as it

[7] *Normandien Farms (Pty) Ltd v Komatiland Forests (Pty) Ltd* (2014) Competition Tribunal: (IR194Feb14).

excludes cost differences based on volumes alone. In order to prevent firms from seeking to avoid these provisions by not dealing with this group of firms, the amendments also establish a contravention where a dominant firm 'avoids selling, or refuse to sell, goods or services to a purchaser that is a SME or historically disadvantaged firm in order to circumvent the operation of price discrimination'.

28. In terms of buyer power, the amendments are similar insofar as they involve a shift from the consumer welfare standard and a change in the legal standard to a more presumptive one based on establishing a *prima facie* case before the onus shifts to the dominant firm. The welfare standard draws on the notion of fairness, making it a contravention for a dominant firm 'to directly or indirectly, require from or impose on a supplier that is a small and medium business or a firm that is controlled or owned by historically disadvantaged persons, unfair prices or trading conditions' (section 8(4)(a)). Section 8(4)(c) provides for the shift in onus to the dominant firm to demonstrate why their prices or trading conditions are not unfair once a *prima facie* case is established. Similarly, under section 8(4)(b) there is an anti-avoidance provision much like that for price discrimination.

29. The underlying context to the introduction of this provision is centred around the possibility that there may be circumstances where buyers have bargaining power against SMEs and HDP firms which they may abuse by suppressing prices and transferring costs and/or risks onto SMEs and HDP firms. To this end, the existence and abuse of buyer power is likely to hinder the ability of, or opportunity for, SMEs and HDP firms to sustain themselves in the market. Given this context, buyer power is necessarily viewed as being more than just assessing monopsony behaviour[8] but is rather an assessment that considers the impact of the relative bargaining power between firms on the public interest objectives of the Act. This means that the consideration of buyer power, whilst it is a public interest issue as outlined by section 8(4), is also an assessment of dynamic competition as the benefits of a thriving SME/HDP sector can offer greater choice for consumers and possibly lead to their growth and challenging of incumbents over time.

6. Constitutional Developments

30. The Constitutional Court (ConCourt) is the final court of appeal in South Africa, given the country is a constitutional democracy. In adjudicating the recent *Mediclinic* case involving a merger in the hospital sector prohibited by the Tribunal but overturned by the Competition Appeal Court, the ConCourt sought to set out clearly the constitutional standard to be applied in competition law.

31. The ConCourt stressed the need for a constitutional interpretation of competition law, which has implications for the legal and liability standards where a constitutional right is possibly infringed upon by the conduct of firms. In such instances, the infringement of those rights is itself substantial even if it implicates only a few consumers or businesses, rather than a broader consumer welfare standard. In the South African context, this applies equally to exclusion from the economy of SMEs and HDPs. If that exclusion is a consequence of conduct or a merger, then the right to equity is infringed and that is itself must be considered alongside any consumer welfare standard.

[8] This refers to the traditional consideration of monopsony behaviour premised on the consumer welfare standard—where the focus is on restricting supplier price and not passing on the lower price to consumers. In this instance harm is measured through the resulting restriction in output to the market.

32. This is consistent with the application of express public provisions in the Act where the liability standard is the welfare of the group (be it employees, SMEs or HDPs) over and above consumers more broadly. If the welfare of that group is harmed by a merger or conduct, then liability is established in terms of the Act. The constitutional jurisprudence extends such a liability standard to all parts of the Act where rights or exclusion is implicated. This too is likely to promote a more competitive and inclusive economy.

33. These principles are clearly set out in the judgement as follows:

> *"[3] It ought never to be acceptable for any of us, including the corporate citizens of this land, to indulge, talk less of over-indulge, in the unconscionable practice of seeking to record the highest profit margin possible by any means necessary, in wanton disregard for what that would do to the rest of humanity. Neither should the historic exclusion of some from meaningful participation, particularly in the mainstream economy, be normalised. For, this seems to be one of the most stubborn injustices of our past that require a more deliberate, intentional and systematic confrontation appropriately enabled by independent, incorruptible, efficient and effective law enforcement and justice-dispensing institutions.*
>
> *[4] Colonialism, neo-colonialism and apartheid orchestrated an institutionalised concentration of ownership and control of all things of consequence in our national economy along racial lines. Unsurprisingly, the commanding heights of the corporate sector are seemingly the exclusive terrain of our white compatriots. It is this indisputable reality and our shared commitment to ensuring that South Africa really does get to belong to all who live in it, that the constitutional imperatives, laid out in the Preamble, to improve the quality of life of all citizens and free the potential of each are realised, that the likes of the Competition Act had to and got to see the light of day.*
>
> *[5] Sight must therefore never be lost of the central purpose for the enactment of [the Competition] Act and for the investigative and adjudicatory structures that it gave birth to. …*
>
> *…*
>
> *[7] Institutions created to breathe life into these critical provisions of the Act must therefore never allow what the [Competition] Act exists to undo and to do, to somehow elude them in their decision-making process. The equalisation and enhancement of opportunities to enter the mainstream economic space, to stay there and operate in an environment that permits the previously excluded as well as small and medium-sized enterprises to survive, succeed and compete freely or favourably must always be allowed to enjoy their pre-ordained and necessary pre-eminence. The legitimisation through legal sophistry or some right-sounding and yet effectively inhibitive jurisprudential innovations must be vigilantly guarded against and deliberately flushed out of our justice and economic system."*

7. Concluding Remarks

34. The consumer welfare standard retains an important role in competition law more broadly, by focusing the assessment on competitive outcomes primarily. However, as the South African experience demonstrates, the consumer welfare standard is ill-equipped to cater for three specific situations, namely the protection of:

- Public interest considerations;

- Dynamic competition effects; and
- Constitutional rights.

35. The legislation and jurisprudence in South Africa demonstrates how welfare standards can be developed for these three specific situations to still provide ease of assessment by the courts, but also the predictability and legal certainty to business. This is achieved through including a separate welfare standard focused on a particular group, or constitutional right, that may stand alone, as is the case in abuse of dominance, or operate as an additional standard in conjunction with the consumer welfare standard, as is the case in merger control. Establishing a separate welfare standard ensures the complexity of weighing up consumer welfare as against the welfare of specific groups is avoided.