IN THE COMPETITION TRIBUNAL OF SOUTH AFRICA

(HELD AT PRETORIA)

CT CASE NO: CR008Apr20

CC CASE NO: 2020Apr0035

In the matter between:

THE COMPETITION COMMISSION Applicant

and

DIS-CHEM PHARMACIES LIMITED Respondent

APPLICANT'S HEADS OF ARGUMENT

INTRODUCTION

1. This case involves the referral of a complaint against the Respondent (Dis-Chem), in terms of section 50(2)(a) of the Competition Act No 89 of 1998, as amended (the Act), in respect of the Dis-Chem's alleged contravention of section 8(1)(a) of the Act, read with Regulation 4 of the Consumer and Customer Protection and National Disaster Management Regulations and

Directions (Regulations)[1] during the period March 2020.

2. Dis-Chem's main business includes, broadly, the operation of retail pharmacies and the retail of personal care products, health and nutrition products and baby care products. Relevant to this complaint, are the surgical face masks blue 50pc, surgical face masks 5pc, and surgical face masks foliodress blue sold by Dis-Chem (complaint products).

3. The Applicant (Commission) contends that Dis-Chem charged materially increased, excessive prices, not corresponding or equivalent to any cost increase, in respect of the complaint products, taking advantage of the increased demand for surgical masks following the onset of the COVID-19 pandemic.

4. The Commission's submissions follow the following sequence:

    4.1. Context of the complaint referral;

    4.2. Cloth masks are not a substitute for surgical masks;

    4.3. The relationship between section 8 and the Regulations;

    4.4. Timeline;

    4.5. Excessive pricing: the legal position;

    4.6. Dominance;

[1] The Consumer and Customer Protection and National Disaster Management Regulations and Directions published in Government Notice No. 350 of Government Gazette no. 43116 (Regulations) on 19 March 2020.

4.7. Dis-Chem's excessive pricing;

4.8. Detriment to consumers;

4.9. Appropriate relief;

4.10. Administrative penalty;

4.11. Conclusion.

CONTEXT OF THE COMPLAINT REFERRAL

5. As Roelofse AJ stated in *Ex Parte van Heerden*[2]*:*

"*Coronavirus disease ("COVID-19") has taken a terrible grip of the World - it is described as an invisible enemy… The drive to curb the COVID-19 menace, its global health and economic effects is unprecedented."*

6. In the recent, as yet unreported decision of *Muhammed Bin Hassim Mohammed and Others v The President of the Republic of South Africa and Others (Case No.21402/20),* Neikircher J said:

"History has taught us that pandemics can have devastating consequences – in October 1347 the Port of Messina welcomed 12 ships from the Black Sea. By the time the Sicilian authorities ordered the ships to leave, the disease that became known as "the Black Death" had spread, and over the following 5 years it killed more than 20 million people in

[2] (1079/2020) [2020] ZAMPMBHC 5 (27 March 2020), at paras [1] – [2].

Europe. The Spanish Flu of 1918 reportedly killed 100 million people. In the past 100 years, the world has seen several examples of this: the SARS-Cov-1 virus in 2003, the Flue Pandemic caused by the H1N1 virus in 2009, the Ebola virus in December 2013, and not to forget the HIV –AIDS virus."[3]

7. In relation to Covid-19 Neukircher J emphasised that:

"9] *Because it is so virulent it has the potential to infect a large number of people in a short space of time and its infection rates are exponential. To demonstrate this, South Africa went from a rate of increase of a few to the number of infected of 5 350 in a matter of 5 weeks with a rise in infections of over 354 in the past 24 hours.*

10] Around the world, as the infection rates exponentially rose, countries saw their healthcare systems overwhelmed overnight with people requiring hospitalisation, intensive care and/or respiratory support for prolonged periods of time. There is insufficient PPE for healthcare workers on the frontlines and test equipment is also insufficient. Of major concern is that the number of ventilators needed to keep people alive in the hopes they recover, is hopelessly inadequate to cater for the overwhelming demand on a global scale."

[3] *Muhammed Bin Hassim Mohammed and Others v The President of the Republic of South Africa and Others* (Case No.21402/20), High Court, Gauteng Division, 30 April 2020.

8. This complaint referral must be considered within the context of the current exceptional and existential health crisis, which has brought about an unparalleled demand for surgical masks.

8.1. This crisis has conferred upon Dis-Chem a temporary market power, which has afforded it the opportunity to exploit consumers and customers, by charging an excessive price for its surgical masks in the midst of a devastating pandemic.

8.2. Dis-Chem's pricing conduct is a direct response to and a result of the COVID-19 pandemic and its unprecedented impact on the world in general and South Africa in particular.

9. Surgical masks are being used by members of the public as a means of protecting themselves and others against the spread of the deadly COVID-19 virus. It is common cause that this has led to panic buying of surgical masks. The importance of surgical face masks in the advent of COVID-19 is recognised by the South African Government, with surgical face masks having been declared an essential good[4].

10. Price increases applied in an emergency situation, such as the present

[4] See Annexures A and B to the Consumer and Customer Protection and National Disaster Management Regulations and Directions in Government Notice No. 350 of Government Gazette no. 43116 (Regulations) published on 19 March 2020, and the Amendments to the Disaster Management Regulations, published in Government Notice No. 398 of Government Gazette 43148 on 25 March 2020 (which identify essential goods during lockdown).

crisis, have the most detrimental impact on poor individuals and families, as well as small businesses, who are already the most vulnerable during such crisis. Such price increases can put basic necessities out of the reach of poor people who desperately need them, or impose high costs on small businesses seeking to protect their employees.

11. The purpose of the Act is, *inter alia*, to promote and maintain competition in the Republic in order to provide consumers with competitive prices and product choices[5] and to **advance the social and economic welfare of South Africans**[6]. As the Competition Appeal Court (CAC) stated in *Mittal Steel South Africa Limited and Others v Harmony Gold Mining Company Limited and Another*[7] (*Mittal*), "*Competition proceedings involve the public interest, and under the Act, the Tribunal has an active role to play in protecting that interest."*[8]

12. The purpose of the Regulations, which seek give effect to the purposes of the Act, is two- fold:

12.1. Firstly, to prevent an escalation of the national disaster and to alleviate, contain and minimise the effects of a national disaster; and

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[5] Section 2(b) of the Act.
[6] Section 2(c) of the Act.
[7] (70/CAC/Apr07) [2009] ZACAC 1 (29 May 2009) at [74].
[8] Some argue that the true goal of competition is "consumer welfare". See M Brassey (ed) Competition Law (Cape Town: Juta 2002).

12.2. Secondly, to protect consumers and customers from unconscionable, unfair, unreasonable, unjust or improper commercial practices during the national disaster.

13. Alleged excessive pricing of surgical masks, within the context of the exceptional COVID-19 pandemic, is accordingly a matter of significant public interest and requires speedy investigation by the Commission and robust determination by the Tribunal. The rights of consumers and customers must be protected during this extraordinary time.

CLOTH MASKS ARE NOT A SUBSTITUTE FOR SURGICAL MASKS

14. Surgical masks have elements that differentiate them from cloth masks.[9] They are significantly more effective than cloth masks at filtering out COVID-19-like particles (89% *versus* 50%).[10]

15. The WHO, the ECDC and the South African Department of Health all draw a clear distinction between cloth masks and surgical masks[11], indicating that surgical masks are critical supplies that should be reserved for healthcare workers and other medical first responders. This confirms the superiority of surgical masks over cloth masks. It is clear that these

[9] Trial Bundle: p 428 para 14.
[10] Trial Bundle: p 429 para 17.
[11] Trial Bundle: pp 195 – 196, p 430 para 20. See also Annexure B to the Regulations, where this distinction is drawn.

authorities do not consider that frontline and healthcare workers could simply substitute surgical masks with cloth masks.[12] There is accordingly no merit in Dis-Chem's contention that cloth masks are a substitute for surgical masks.

16. While cloth masks may be more easily accessible, customers and consumers have sought to procure surgical masks, and continue to do so, in substantial volumes. There is a clear and unprecedented public demand for surgical masks, which are (correctly) perceived by the public as offering better protection than cloth masks against the spread of COVID-19.[13] Dis-Chem itself experienced shortages of surgical masks in February and March 2020, due to the demand increase, and struggled to replenish its stock.[14]

THE RELATIONSHIP BETWEEN SECTION 8 AND THE REGULATIONS

17. Despite Dis-Chem's indication[15] that it intends making submissions regarding the "status and effect" of the Regulations and "their relationship with section 8 of the Act", the nature and extent of these submissions is unknown.

18. The relationship between the Regulations and section 8 of the Act is clearly

[12] Trial Bundle: p 431 para 23.
[13] Trial Bundle: p 431 para 21.
[14] Trial Bundle: pp 79-80 paras 32-33.
[15] Trial Bundle: p 67 para 6.2.

expressed in Regulation 4.

18.1. Regulation 4.1 re-confirms that, in terms of section 8(1) of the Act a dominant firm may not charge an excessive price to the detriment of consumers or customers.

18.2. Regulation 4.2 identifies two relevant and critical factors (in terms of section 8(3)(f) of the Act), either of which may be considered when determining whether the material price increase of a good (contemplated in Annexure A to the Regulations), during any period of the national disaster relating to the COVID-19 outbreak, is excessive or unfair.

18.2.1. The first factor relates to a material price increase that does not correspond to or is not equivalent to the increase in the cost of providing the relevant good; and

18.2.2. the second factor relates a material price increase which increases the net margin or mark-up above the average margin or mark up in the three months prior to 1 March 2020.

19. Regulation 4 derives its legal force and origin from the provisions of the Act itself. Section 8(3) of the Act provides an analytical framework which enables the Tribunal in determining an excessive price to take into account

all the **relevant factors**, which may include, in terms of section 8(3)(f), any Regulations made by the Minister in terms of section 78 regarding the calculation and determination of an excessive price. T he Regulation is binding and has the force of law. . The Regulation seeks to give effect to the purposes of the Act and it does so in a manner that is perfectly compatible the analytical framework of section 8(3) of the Act.

20. Consistent with the framework of section 8(3) of the Act, Regulation 4 simply makes provision for relevant and critical factors in the determination of an excessive price in respect of essential goods and services with the context of the Covid-19 pandemic and the national disaster.. To the extent that these factors have been specifically indicated as relevant and critical within the context of the COVID-19 pandemic, it is submitted that it is appropriate that they should be afforded greater weight by the Tribunal in determining whether or not an excessive price has been charged.

21. As is addressed in more detail below, the list of factors indicated in section 8(3) is not exhaustive. There is accordingly no reason why the Tribunal cannot (even in the absence of the Regulations) take into account the factors indicated in Regulation 4.2 and 4.2 when determining this matter. There is further no reason why the Tribunal should not also consider these factors (even in the absence of the Regulations) as the primary relevant and critical factors in determining whether an excessive price has been charged, within the context of the COVID-19 pandemic. Historic pricing and profitability are, after all, factors listed in section 8(3).

22. To the extent that Dis-Chem intends raising any legal issue in relation to the Regulations and/or its relationship with section 8 of the Act, the Commission records that it reserves its right to object to such legal argument being raised (if warranted) and to make submissions in respect thereof (after receiving clarity on what exactly these legal issues are and after being afforded an opportunity to consider Dis-Chem's contentions in this regard).

TIMELINE

23. The following timeline reflects common cause/undisputed events relevant to the determination of this matter.

12 July 2019	• Amendments proclaimed to the Act render sections 8(1)(a), 8(2) and 8(3) effective in their current form. • The definition of "excessive price" in the Act is deleted.
December 2019	• China announces the emergence of COVID-19. • Dis-Chem sells only [redacted] surgical masks. • Dis-Chem charges R9.52 (ex. VAT) for a packet of 5 (R1.90 per mask) and R41.70 (ex. VAT) for a pack of 50 (R0.83 per mask).[16]
January 2020	• The virus spreads to other countries, culminating in the WHO declaring COVID-19 a Public Health Emergency of International Concern (PHEIC) on 30 January 2020.[17]

[16] Trial Bundle: p 95, Table 5.
[17] Trial Bundle: p 169.

	• Dis-Chem sees surgical mask sales increase [redacted] to [redacted] in January.[18] • Prices remain the same at a gross margin of [redacted]%.[19]
February 2020	• Global demand for face masks escalates with supply shortages emerging internationally. • Surgical masks are recommended for frontline and healthcare workers. • Dis-Chem experiences shortages of surgical masks. • Dis-Chem pushes through two price increases, on 14 February and 26 February[20], despite the average cost per mask declining from [redacted] to [redacted].[21] • By the end of February a 5pc packet sells for R17.35 (ex VAT) or R3.47 per mask and a 50pc packet sells for R78.22 (ex VAT) or R1.56 per mask.[22] • Gross margins climb to [redacted]%.[23]
March 2020	• On 15 March a national state of disaster is declared. • On 19 March the Regulations are published, identifying both "facial masks" and "surgical masks" as goods for which suppliers must take reasoanble measures to ensure equitable distribution and adequate stocks.[24] • On 19 March Dis-Chem informs its store managers that they must place limits on the number of masks an individual customer may purchase.[25]

[18] Trial Bundle: p 101, Table 8.
[19] Trial Bundle: p 101, Table 8.
[20] Trial Bundle: p 95, Table 5.
[21] Trial Bundle: p 101, Table 8.
[22] Trial Bundle: p 95, Table 5.
[23] Trial Bundle: p 101, Table 8.
[24] Regulation 6 and Annexures A and B to the Regulations.
[25] Trial Bundle: pp 235 – 236.

	• Dis-Chem pushes through price increases on 2, 7 and 9 March[26], despite costs per mask dropping again to 83c. A 5pc packet is priced at R19.96 (ex VAT) or R3.99 per mask, and a 50pc packet is at R173.87 (ex VAT) or R3.47 per mask.[27] • Gross margins climb to [redacted]%.[28] • On 25 March the Disaster Management Regulations are amended, classifying personal protective equipment and medical equipment as essential goods.[29] • On 30 March Dis-Chem orders its first additional stock[30]
April 2020	• In April Dis-Chem starts selling its additional, higher priced surgical masks.[31] • On 20 April Dis-Chem secures stock at a lower cost.[32]

EXCESSIVE PRICING: THE LEGAL POSITION

Past and Current Provisions regarding Excessive Pricing in the Act

24. Prior to the amendments effected to the Act on 12 July 2019, the Act contained a definition of "*excessive price*", being "*a price for a good or service which—(aa) bears no reasonable relation to the economic value of*

[26] Trial Bundle: p 95 Table 5.
[27] Trial Bundle: p 95 Table 5.
[28] Trial Bundle: p 101, Table 8
[29] Annexure B to the Disaster Management Regulations.
[30] Trial Bundle: p 91, Table 4.
[31] Trial Bundle: p 391, para 95 & Figure 3.
[32] Trial Bundle: p 94 paras 59 - 60.

that good or service; and (bb) is higher than the value referred to in subparagraph (aa)". This definition has now been excised by the amendments.

25. The concept of "economic value" included in the definition of excessive price, has been considered in numerous local and international cases. Legislature's deliberate removal of any reference to "economic value" in the Act[33] denotes its intention to exclude a consideration of economic value in the determination of excessive pricing complaints. Instead, Section 8 of the Act now specifically references a "competitive price" as the appropriate comparator in determining whether or not a price is excessive.

26. Prior to the 12 July 2019 amendment of the Act, section 8 addressed excessive pricing as follows:

"*8. …. It is prohibited for a dominant firm to—*

(a) charge an excessive price to the detriment of consumers…"

27. Following the 12 July 2019 amendment of the Act, section 8 now contains expanded provisions on excessive pricing. Sections 8(1)(a), 8(2) and 8(3) of the Act currently read as follows:

[33] Save for the reference to economic value in the definition of confidential information in section 1 of the Act.

"8(1) It is prohibited for a dominant firm to—

(a) charge an excessive price to the detriment of consumers or customers"

"8(2) If there is a prima facie *case of abuse of dominance because the dominant firm charged an excessive price, the dominant firm must show that the price was reasonable."*

"8(3) Any person determining whether a price is an excessive price must determine if that price is higher than a competitive price and whether such difference is unreasonable, determined by taking into account all relevant factors, which may include—

(a) the respondent's price cost margin, internal rate of return, return on capital invested or profit history;

(b) the respondent's prices for the goods or services—

(i) in markets in which there are competing products;

(ii) to customers in other geographic markets;

(iii) for similar products in other markets; and

(iv) historically;

(c) relevant comparator firm's prices and level of profits for the goods or services in a competitive market for those goods or services;

(d) the length of time the prices have been charged at that level;

(e) the structural characteristics of the relevant market, including the extent of the respondent's market share, the degree of contestability of the market, barriers to entry and past or current advantage that is not due to

the respondent's own commercial efficiency or investment, such as direct or indirect state support for a firm or firms in the market; and

(f) any regulations made by the Minister, in terms of section 78 regarding the calculation and determination of an excessive price."

Price Gouging

28. Price gouging is the term commonly used to describe situations where firms take advantage of a civil emergency or disaster by charging excessive prices for essential products required for the health, safety and welfare of citizens in the disaster. In such disaster situations, there are typically abnormal disruptions to the market, such as a disruption to the supply of, or a spike in demand for, certain products necessary for citizens to cope with the challenges of that emergency or disaster. These disruptions remove the ordinary competitive constraints faced by certain firms, conferring upon retailers/distributors holding stock or local producers of essential items, a temporary form of market power which enables them to increase prices without constraint for the period of the disaster.[34]

29. This is clearly a species of excessive pricing, where temporary market power affords a firm to raise prices significantly, unconstrained by competition, and earn an excessive profit margin. This was indeed recognised by Mr David Lewis, the architect of our Act and the first Tribunal

[34] Trial Bundle: p 36 para 10.

Chair has expressed the view that our Act accommodates such temporary dominance and excessive pricing, as set out in the Replying Affidavit.[35]

30. Furthermore, prosecution of this type of excessive pricing may not be subject to the same economic criticisms levelled at other forms of excessive pricing. Motta[36] has expressed the view, in the context of the COVID-19 pandemic, that *"Excessive price actions in antitrust are often criticised because (i) they interfere with the regular functioning of the market, and (ii) they may "expropriate" firms of the fruits of their investment and innovation. However, under the current circumstances, objection (i) will not apply if supply is unlikely to respond in the short-run; as for (ii), price spikes are due to sudden increases in demand or captivity of consumers and bear little relation to firms' investment or effort."*

Disaster Regulation

31. The Consumer and Customer Protection and National Disaster Management Regulations and Directions (Regulations) were published[37] in order to (a) promote concerted conduct to prevent an escalation of the national disaster and to alleviate, contain and minimise the effects of the national disaster; and (b) protect consumers and customers from unconscionable, unfair, unreasonable, unjust or improper commercial

[35] Trial Bundle: p 451 para 42, p 523: Annexure H.
[36] Trial Bundle: p 505: Annexure F.
[37] In Government Notice No. 350 of Government Gazette no. 43116 on 19 March 2020.

practices during the national disaster.

32. The Regulations apply to goods including medical and hygiene supplies[38], facial masks and surgical masks[39] during the period of the national disaster, with effect from 19 March 2020.

33. Regulation 4.2 provides that:

> *"In terms of Section 8(3)(f) of the Competition Act during any period of the national disaster, a material price increase of a good or service contemplated in Annexure A which –*
> *4.2.1 does not correspond to or is not equivalent to the increase in the cost of providing that good or service; or*
> *4.2.2 increases the net margin or mark-up on that good or service above the average margin or markup for that good or service in the three month period prior to 1 March 2020,*
> *is a relevant and critical factor for determining whether the price is excessive or unfair and indicates* prima facie *that the price is excessive or unfair."*

34. The Regulations define "*price increase*" as "*a direct increase or an increase as a result of unfair conduct such as, amongst others, false or misleading pricing practices, covert manipulation of prices, manipulation through*

[38] Per Annexure A to the Regulations
[39] Per Annexure B to the Regulations.

raising or reducing grade levels of goods and services".[40]

35. The Commission contends that the Regulations do not detract from the Tribunal's ability to determine whether Dis-Chem has charged excessive prices during the complaint period.

35.1. The Regulations do not change the legislative test applicable to section 8(1) of the Act.

35.2. The essential elements of the contravention under section 8(1)(a) of the Act remain: (a) dominance, (b) an excessive price, and (c) detriment to consumers.

35.3. There is nothing in the framework of section 8(1)(a) to suggest that it does not apply to price gouging.

The Application of the Price Gouging Test to this Referral

36. Whilst section 8(3) applies to all products, the Regulations have identified specific product categories for which the "price gouging test"[41] applies as the "relevant and critical factor" in the determination of an excessive or unfair price. There is however no reason why the Tribunal cannot apply this same test in determining any excessive pricing case in respect of

[40] Regulation 1.5 of the Regulations.
[41] i.e. the test reflected in Regulations 4.2.1 and 4.2.2 of the Regulations.

conduct preceding the publication of the Regulations, since the COVID-19 pandemic was in existence both before and after the publication of the Regulations.

37. The conditions for price gouging behaviour in respect of surgical masks were prevalent from the end of January, when the WHO announced a "Public Health Emergency of International Concern" or PHEIC. From that point there was a rapidly escalating demand for surgical masks, amongst other Personal Protective Equipment (PPE), and growing global shortages. Dis-Chem experienced the same.

38. In the US the absence of a federal excessive pricing law, unlike South Africa, has resulted in most states enacting specific price gouging laws to prevent this species of excessive pricing as it is considered particularly exploitative and inequitably so.

38.1. However, this is unnecessary where existing excessive pricing or consumer protection laws exist, and these instruments may be used to prevent firms from profiteering from situations of necessity.[42]

38.2. Emergency regulations have been used in some cases, but this is often to impose specific price ceilings on specific products, an act

[42] TILEC Discussion Paper DP 2020-007 EU Competition Law and COVID-19 By Francisco Costa-Cabral,Leigh Hancher, Giorgio Monti and Alexandre Ruiz Feases March 22, 2020 ISSN 2213-9419 http://ssrn.com/abstract=3561438 at page 8.

that extends beyond the reach of excessive pricing provisions.

39. As outlined above, Lewis[43] saw no difficulties invoking section 8(a) in the context of a disaster, stating that *"A competition authority may conceivably be called upon to act as a price regulator in instances that may be characterised as price gouging. For example, were Section 8(a) to be invoked in the event of a natural disaster, which had given rise to a temporary monopoly in some or other unregulated product or service that was vital to the life of the affected community, say ambulance services or fuel for heating, and this was exploited to effect a significant temporary price rise, the competition authority could easily assume the role of temporary price setter."*

40. As Motta states[44] "*Instruments for temporary price ceilings* [in response to price gouging] *include emergency regulations (some European countries have issued orders to control prices of hand sanitisers, face masks and funeral services). Existing legal provisions, e.g. in consumer protection, may also be used."*

41. With reference specifically to the Babelegi complaint referral currently pending before the Tribunal, Motta[45] opines that if the facts (a seller allegedly increasing the price of facial masks by more than eight times)

[43] Trial Bundle: p 523: Annexure H.
[44] Trial Bundle: p 502: Annexure F.
[45] Trial Bundle: p 506: Annexure F.

were confirmed, this would indeed be the type of case that merits intervention. The present matter similarly warrants intervention by the Tribunal.

42. Section 8(3) sifts factors that may be considered in determining an excessive price, on the basis of relevance.

43. In the current crisis, the factors that are relevant to the determination of this matter, must include:

43.1. Dis-Chem's prices for the complaint products prior to the COVID-19 pandemic[46];

43.2. the number of price hikes implemented by Dis-Chem over a short period of time, and subsequent to the onset of the COVID-19 pandemic, and the panic buying of consumers and customers;

43.3. the material extent of the increase in Dis-Chem's mark-up during the complaint period[47];

43.4. the absence of any supplier price increase during the complaint period, nor justified by any change in costs of Dis-Chem itself[48];

[46] Per sections 8(3)(a), 8(3)(b)(iv), 8(3)(d)– which accord with Regulation 4.2
[47] Per sections 8(3)(a), (c) and (d)– which accords with Regulation 4.2.
[48] Per sections 8(3)(a) and (c)– which accord with Regulation 4.2.

43.5. the fact that Dis-Chem's advantage (i.e. its ability to price higher without constraint by consumers or customers) is not due to its own commercial efficiency or investment, but rather a direct result of the COVID-19 pandemic, and in relation to surgical masks, which consumers and customers have sought in an effort to mitigate the impact and spread of the virus[49]; and finally,

43.6. the Regulations, which provide an indication of the test that the Minister deems appropriate to apply in response to excessive prices charged as a result of the COVID-19 pandemic.

44. As previously mentioned, the test indicated in Regulation 4, is one that the Tribunal would in any event have been able to apply in determining whether or not a price is excessive.

45. One has to look no further than the CAC judgment in *Mittal* to appreciate that the test of determining if price increases have a corresponding cost justification is an established test for excessive pricing under the Act. This is because an excessive profit margin is detectable if the ordinary prices are increased materially, absent cost increases. As the CAC stated in *Mittal*[50]:

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[49] Per section 8(3)(e).
[50] At [49] – [50].

"Likewise, where the dominant firm raises the normal price for its product substantially without any corresponding rise in costs, this may indicate prima facie that the new price is higher than economic value without the need to quantify the latter more precisely." [emphasis added]

46. Motta[51] concurs from an economic perspective, stating in respect of cases in the COVID-19 crisis that '*Using the pre-crisis price as a benchmark is sensible because demand and supply conditions at that time were presumably "normal".*'

47. The OECD 2011 Excessive Pricing: Policy Roundtables[52] records the US approach to the price gouging test as '*The basic methodology employed is based on a comparison of a (fictitious) "normal" price with the potentially excessive price in periods of abnormal supply disruptions. In determining the "normal" supply price a variety of definitions are used. While some US States do not define the normal price at all, others use the average price over a specified period or the price immediately prior to the supply disruption or the emergency declaration*.'

Smith's/RBB's Legal Contentions

48. Smith, of RBB, in his Expert Witness Statement (RBB Report), espouses

[51] Trial Bundle: pp 505: Annexure F.
[52] OECD. 2011. Excessive Pricing: Policy Roundtables. Available: https://www.oecd.org/competition/abuse/49604207.pdf at para 5.3.1 on p61.

an unfortunate and overwhelming number of legal contentions and arguments, despite his protestations that he himself is not a legal expert, claiming such legal matters emanating from Dis-Chem's legal advisors.

49. Legal contentions and argument have no place in an expert witness statement. The role of the economists in the determination of this matter, is solely to provide economic evidence that may be considered by the Tribunal in making its determination on whether or not the requirements of the Act have been met. All references to issues of law in the RBB Report should accordingly be disregarded.

50. The RBB Report regrettably also refers to statements of fact not placed before the Commission or Tribunal for consideration in any of the affidavits filed. It is further premised on numerous incorrect assumptions and vague references, many of which contradict the concessions and allegations contained in Dis-Chem's Answering Affidavit. It is trite that admissions or concessions made under oath cannot simply be withdrawn by way of subsequent contentions to the contrary (by a third party). It is submitted that where the RBB Report and the Answering Affidavit contradict one another, allegations contained in the Answering Affidavit must prevail.

DOMINANCE

51. Only a dominant firm can act in breach of the excessive pricing prohibition

in section 8 of the Act. In order for a firm to be considered dominant[53] its annual turnover or assets in the Republic must be valued at or exceed R5 million, and it must meet the threshold set out in section 7 of the Act.

52. In the present matter the relevant threshold is that reflected in section 7(3) of the Act, providing that *"A firm is dominant in a market if …It has less than 35% of that market, but has* market power". Any firm that has market power is considered dominant, regardless of its market share. The Act[54] defines market power 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".*

53. It is common cause that Dis-Chem's annual turnover exceeds R5 million.[55]

54. Dis-Chem contends that "temporary market power" is not a relevant concept in fact, law and economics. Smith is silent on the term itself, but appears to resist such a concept by arguing that excessive pricing only relates to a situation where there is persistent exercise of market power.

55. Dis-Chem is plainly wrong on this score, as other economists and jurisdictions seem to have no difficulty with the concept of temporary market power in the context of a disaster. Furthermore, nothing in the

[53] See section 6 of the Act.
[54] In section 1.
[55] Trial Bundle: p 68 para 7.

definition of market power in the Act limits it in such a way.

55.1. Indeed, Prof. Massimo Motta, who is cited approvingly in the RBB Report, recently indicated that temporary market power not only exists as a concept but can arise precisely in this type of COVID-19 context. According to Motta[56] (with specific reference to the South African prosecution of excessive pricing cases in the context of COVID-19), *"[F]irms that may be accused of price gouging **might not necessarily be dominant in ordinary times. However, they may well be in our exceptional times.** Consider markets for food and groceries. Normally, they are defined geographically in a broad way, because consumers can move and shop around. But during a period of confinement, people are obliged to buy their shopping next door, thus becoming captive of local shops. Even if they have very little market share in a "normal times" market, these shops may be dominant during the crisis. Note that in such cases insufficient supply is not the problem: Some firms may simply take advantage of consumers' impossibility to shop around. (And here, one cannot argue that price regulations are inefficient: There is no lack of supply.) In cases of excess demand, even a small firm may have considerable market power. Under normal demand conditions, if any firm tried to set a high price, its rivals would use their spare capacity*

[56] Trial Bundle: pp 504: Annexure F.

to undercut it and sell more. But, if at that high price, each firm's demand is higher than its capacity, there would be no incentive to cut prices. When firms already sell at capacity, by lowering their price they would sell the same amount, but make less profit. In other words, ***when demand is much higher than capacity, even "small" firms may be endowed with significant market power, that is, they may be dominant.****"* [Emphasis added].

55.2. Lewis[57] similarly recognised the concept of temporary market power within the context of section 8(a) where dominance is a requirement.

55.3. The Competition & Markets Authority (CMA) in the UK (previously the OFT) also expressly recognises that the current crisis may confer dominance on a firm, allowing it to price excessively. In discussing business conduct that may harm consumers in the midst of the COVID-19 crisis, the CMA[58] includes the following: "*a business abusing its dominant position in a market (****which might be a dominant position conferred by the particular circumstances of this crisis****) to raise prices significantly above normal competitive levels*" [emphasis added].

55.4. Even established case precedent in competition law has examples of temporary market power brought about by a crisis or disaster. The

[57] Trial Bundle: p 523: Annexure H.
[58] Trial Bundle: p 517: Annexure G.

European Commission decision in respect of *ABG Oil* is one such case[59], where the crisis in question was the Oil Crisis of 1973.

55.4.1. As the decision notes under the discussion of dominance[60], the crisis was caused by "*a simultaneous reduction in the supply of oil offered on the world market combined with a substantial increase in the price demanded for it.*"

55.4.2. The judgment continued to find that it was only the international refiners in the Netherlands which had "*access to oil supplies at economically viable prices*" and that the sudden shortage led to "*a restriction of both actual and potential competition*" between them.

55.4.3. Each of the firms was found to be dominant during the crisis, since "*their customers can become completely dependent on them for the supply of scarce products. Thus, while the situation continues, the suppliers are*

[59] European Commission decision of 19 April 1977 (IV/28.841 – ABG Oil Companies) (77/327/EECApril 19, 1977. The European Court of Justice overturned the decision on appeal, finding that ABG was an occasional and not a contractual customer at the time of the crisis, but did not disagree with the principle that in periods of shortage a dominant undertaking must distribute available quantities "fairly," unless objective reasons justified different treatment (Case 77/77 – BP v Commission ECLI:EU:C:1978:141). It bears mention that the Commission found the relevant oil companies to be temporarily dominant, as their customers were "completely dependent" on them for scarce products, and, given the general shortage, they were unable to compete with each other by supplying a rival's customers.

[60] *Ibid* pp 8-9.

placed in a dominant position in respect of their normal customers."

56. Whilst Smith does inappropriately venture into making legal points, it seems his main economic argument is around when is excessive pricing enforcement appropriate or not. This discussion is centred entirely around the notion that there are potential unintended consequences to excessive pricing enforcement, from blunting the incentives to invest and preventing price signals from spurring on greater investment in supply, which means that its enforcement should be severely constrained to exceptional cases.

57. This line of argument encapsulates the difficulties with Dis-Chem's case in this matter. In particular, it is not the excessive pricing provisions in the Act that are limited legally so as to exclude price gouging cases, rather it is Dis-Chem which seeks to place limits on the provisions to what it sees as appropriate enforcement cases with low risks of unintended consequences.

57.1. Firstly, that is an issue of enforcement discretion rather than a limitation to what can be brought under the law. As outlined above, nothing in the Act precludes temporary dominance as a form of dominance.

57.2. Secondly, even on enforcement discretion, the other difficulty arises because in fact price gouging does not run the risks of the

unintended consequences that are the subject of Smith's critique. In the context of such a disaster, the supply constraint is temporary and the long term structure, investment and entry into a market is not a relevant dimension. This is especially so in respect of the retail level of the value chain.

57.3. Enforcement against the reseller and retailer level of the value chain from exploiting a disaster has no long term negative effects on investment in the economy or structural aspects to competition, either at the retail level or at the upstream supplier level. It even does not impact on the short term supplier responses, as it is the manufacturer that needs to be incentivised to increase supply, not the retailer.

57.4. It is for this reason that in the US, where ideologically they are more aligned to Smith's perspective of not interfering in investment incentives and the normal functioning of the market, 34 States have implemented price gouging laws based on the realisation that this form of exploitation has no redeeming features and will not benefit competition in the long run. It is simply exploitative and inequitable.

57.5. As already outlined above, Motta is of the same view that enforcement against price gouging does not suffer from the usual critiques of excessive pricing enforcement, as rolled out by Smith in

this case, namely that it interferes with the normal functioning of the market and investment incentives.[61]

57.6. As also outlined above, even Lewis[62] saw intervention in such situations in the form of price regulation by the competition authorities as far less fraught with difficulties and with far simpler decision rules to come to the appropriate price (namely the pre-crisis pricing).

58. The Commission contends that there are no limitations in the law which prevent a finding of temporary dominance and excessive pricing based on that dominance, and that there are no risks to the enforcement of the law in such circumstances.

59. Furthermore, in determining whether market power exists or not, the relevant inquiry in terms of the Act is one which focuses on conduct, namely "*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".* [63] In this respect, a distinction needs to be made between an *ex-post* analysis of market conduct in an abuse case and an *ex-ante* analysis in the context of merger regulation. As reflected in the following quote from the European Commission guidelines on market

[61] Trial Bundle: pp 503 - 505: Annexure F.
[62] Trial Bundle: p 523: Annexure H.
[63] In section 1 of the Act.

analysis and the assessment of significant market power in the electronic communications sector[64], an *ex-post* analysis may rely on market behaviour which is indicative of market power, whereas an *ex-ante* analysis may need to rely on other assessment tools, such as market definition and market share, to determine *ex-ante* if the firm will have the power to raise prices and/or restrict output.

"*73.* ***In an ex-post analysis, a competition authority may be faced with a number of different examples of market behaviour each indicative of market power within the meaning of Article 82.*** *However, in an* ex-ante *environment, market power is essentially measured by reference of the power of the undertaking concerned to raise prices by restricting output without incurring a significant loss of sales or revenues.*" [emphasis added]

60. The European Commission is not alone in this regard, as many jurisdictions accept that a firm's conduct in a market or its financial performance may itself provide evidence of market power in the context of an abuse case. The ability to raise prices despite costs remaining the same and to impose a gross margin on the said products of more than double the margin during normal competitive periods epitomises the ability to behave independently of competitors and control prices. Such a test was also cited with approval by the CAC in *Mittal* as one where a *prima facie*

[64] European Commission guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services (2002/C 165/03) paragraph 73

case of excessive pricing existed. The same test is used in price gouging laws and the Regulations.

61. Dis-Chem used the COVID-19 crisis and panic-buying of surgical masks to raise prices for such masks, despite the costs remaining the same, and exploited consumers for its own commercial benefit, to their obvious detriment.

62. The disruption to the normal supply and demand dynamics around surgical masks which rendered a shortage in the market at competitive prices, and the fact that Dis-Chem held considerable stock acquired at a competitive price, afforded it temporary market power as is evidenced by Dis-Chem's ability to effect such material price increases, suddenly, over a short period of time. This confirms that Dis-Chem is a dominant firm, as contemplated in section 7 of the Act, by virtue of the fact that it exerted market power by behaving to an appreciable extent independently of its competitors, and its customers and consumers.

63. Dis-Chem contends that it is subject to countervailing power by suppliers. However, there is both a factual and logical problem with this argument. On the factual side, Dis-Chem instituted all its price increases prior to receiving higher quotes from suppliers. As clearly set out in table 5 of the Answering Affidavit[65], all price increases were complete by 9 March, and

[65] Trial Bundle: p 95.

as set out in table 3[66], high quotes for surgical masks were recorded from this date onwards. Furthermore, the price increases were only felt by Dis-Chem at the end of March 2020, or the very end of the complaint period. On the logical side, even if suppliers had the ability to raise prices to Dis-Chem, this does not preclude Dis-Chem having market power at the next level of the supply chain and imposing its own exorbitant mark-up, which it did.

DIS-CHEM'S EXCESSIVE PRICING

64. Section 8(3) of the Act filters the factors that are relevant in determining whether or not an excessive price has been charged.

65. When a functionary is entrusted with a discretion, the weight to be attached to particular factors, or how far a particular factor affects the eventual determination of the issue, is a matter for the functionary to decide. The weight or lack of it to be attached to the various considerations that go to making up a decision, is that of the decision-maker i.e. the Tribunal.[67]

66. The relevant economic test for determining whether a price is excessive for the purposes of section 8(1)(a), in the context of the COVID-19 pandemic and during the period preceding the national state of disaster

[66] Trial Bundle: p 87.

[67] *MEC for Environmental Affairs and Development Planning v Clairison's CC* (408/2012) [2013] ZASCA 82; [2013] 3 All SA 491 (SCA); 2013 (6) SA 235 (SCA) (31 May 2013) at [20] - [22].

and lockdown, is whether prices increased materially relative to what was previously charged, and if so, whether that increase is justified by any cost increases from a supplier further up the value chain.

67. As indicated hereinabove, this test has found favour by the courts even outside of the pandemic. In *Mittal*[68] the CAC stated that "*where the dominant firm raises the normal price for its product substantially without any corresponding rise in costs, this may indicate* prima facie *that the new price is higher than economic value without the need to quantify the latter more precisely*." Although the comparator is now a competitive price rather than economic value, the same principles apply in this matter.[69]

68. On the admitted facts by Dis-Chem, it is apparent that the pricing was excessive for the complaint products. In particular:

68.1. Dis-Chem admits to a series of successive price increases from 14 February to 9 March 2020[70], which prices then endure throughout March. The price of the different products and the per mask price increase as follows:

68.1.1. For surgical face masks 5pc the price increases from R9.52 (ex. VAT) per pack on 13 February to R19.96 (ex.

[68] At [50].
[69] See also *United Brands Company and United Brands Continental BV v The Commission of the European Communities* [1978] 1 CMLR 429 at [250].
[70] Trial Bundle: p 95, Table 5.

VAT) per pack on 9 March.[71] This represents **a price increase of 110%**. The effective price per mask rises from R1.90 (ex. VAT) to R3.99 (ex. VAT).

68.1.2. For surgical face masks blue 50pc the price increases from R41.70 (ex. VAT) per pack on 13 February to R173.87 (ex VAT) per pack on 9 March.[72] This represents **a price increase of 317%**. The effective price per mask rises from R0.83 (ex VAT) to R3.47 (ex VAT).

68.1.3. For surgical face masks foliodress blue 1pc, the price increases from R1.31 (ex VAT) to R4.31 (ex VAT).[73] This represents **a price increase of 229%.**

68.2. Dis-Chem admits that its costs of supply of these products did not increase over this period, and in fact decreased[74]. This meant that gross profit margins escalated in February and March 2020, which is also evident from figures 4, 5 and 6 of the RBB Report.[75] In respect of Table 8[76]:

68.2.1. In January 2020 the average costs per mask incurred by

[71] Trial Bundle: p 95, Table 5.
[72] Trial Bundle: p 95, Table 5.
[73] Trial Bundle: p 95, Table 5.
[74] As set out in Table 8 of the Answering Affidavit: Trial Bundle: p 101.
[75] Trial Bundle: pp 393 - 395.
[76] Trial Bundle: p 101.

Dis-Chem was [redacted][77] with a gross margin of [redacted]%[78].

68.2.2. In February 2020 the average costs per mask incurred by Dis-Chem declined to [redacted][79], but with the initial price escalations, gross margins increased to [redacted][80].

68.2.3. In March 2020 the average costs per masks incurred by Dis-Chem declined further to [redacted][81], but with the initial and further price escalations, gross margins increased to [redacted][82].

69. Dis-Chem tries to obscure the rise in gross profit margins during the complaint period by repeatedly referring to its behaviour in April 2020 and the lower margins it earned. It implores that it is important to factor in all of this subsequent behaviour and its retail prices in the complaint period. Similarly, Smith seeks to obscure this increase by presenting average margins for periods that include April 2020, simply asserting that this is somehow more relevant. It is not. What matters is the complaint period margins. On the admitted facts, these were [redacted] in March and were [redacted]

[77] Cost of sales (of [redacted]) divided by the volume of masks sold ([redacted]).
[78] Revenue from sales (of [redacted]) less cost of sales (of [redacted]) is then divided by revenue from sales (of [redacted]) in order to arrive at the gross margin.
[79] Cost of sales (of [redacted]) divided by the volume of masks sold ([redacted]).
[80] Revenue from sales (of [redacted]) less cost of sales (of [redacted]) is then divided by the revenue from sales (of [redacted]) in order to arrive at the gross margin.
[81] Cost of sales (of [redacted]) divided by the volume of masks sold ([redacted]).
[82] Revenue from sales (of [redacted]) less cost of sales (of [redacted]) is then divided by the revenue from sales (of [redacted]) in order to arrive at the gross margin.

in the three months prior thereto[83].

70. The primary explanation proffered by Dis-Chem for the increase was that it incurred costs to repackage 50pc surgical masks into 5pc packets, additional costs to extend its sourcing beyond traditional suppliers and pay cash on delivery for new stock. However, these not only cannot justify the price increase, but these costs are also, for the most part, not substantiated by Dis-Chem:

70.1. The first difficulty with most of these contended costs is that they do not coincide with the timing of the price increases.

70.1.1. The price increases mostly take place in February 2020, with some final escalations in early March, ending 9 March 2020.

70.1.2. However, the repackaging primarily took place in March 2020, as is evident from the Point of Sales data[84], which shows mostly 5pc packets sold in this month, unlike prior months where many 50pc were sold.

70.1.3. The evidence on additional quotes from suppliers in

[83] Trial Bundle: p 400: Table 7 of the RBB Report.
[84] Trial Bundle: p 234.

Table 3[85] has its first quote on 9 March 2020, which is the date of the final price increase. Finally, in terms of new orders, the evidence placed on record by Dis-Chem in Table 6[86] was that the first of such orders was only on 30 March 2020, at the very end of the complaint period.

70.2. The next issue is Dis-Chem's failure to quantify these alleged costs.

70.2.1. In terms of the repackaging, Dis-Chem admits that it incurred the cost of a bag at [redacted] each[87].

70.2.2. It does not quantify the staffing costs, but in the investigation indicated that this added [redacted] to the cost whereas the bag contributed [redacted]. Staffing is therefore estimated at a further [redacted] per bag, or [redacted] per 5pc packet overall. This represents a [redacted] per mask cost for the 5pc packets.

70.2.3. However, the price of 5pc masks go from R1.90 to R3.99, a difference of [redacted] or roughly [redacted] times the cost of repackaging. Furthermore, Dis-Chem actually benefits from repackaging, as the price per mask for a 50pc

[85] Trial Bundle: p 87.
[86] Trial Bundle: p 97.
[87] Trial Bundle: p 398 para 105.2.2.

packet was R3.47 at the peak of the price increase, whereas for a 5pc packet it was R3.99 per mask, or a 52c difference. The benefit of repackaging in the form of a higher price per mask therefore was [redacted] times the cost to Dis-Chem of doing so.

70.2.4. No costs are indicated for any alleged sourcing costs and no evidence is provided as to which suppliers demanded cash on delivery, even though both occurred after the price increases were implemented.

70.3. For all these reasons, the claims have the flavour of an attempt at *ex post facto* rationalisation. Moreover, the fact that Dis-Chem is also unable to substantiate the actual costs further indicates that cost escalations were not behind the pricing decision. Otherwise, the costs would have been estimated to make that price adjustment decision.

71. Dis-Chem also argues that the suppliers had market power and it was subject to price escalation from the supplier side. However, the common cause evidence is that, for the period of 30 March 2020 onwards, Dis-Chem bought stock sourced at a higher price[88], but it only started selling this stock in April 2020, after the complaint period. This is self-evident from

[88] Trial Bundle: p 91, Table 4.

not only from the fact that its first order at higher prices was on 30 March 2020 (as per Table 4 of the Answering Affidavit)[89], but also figure 3 of the RBB Report which shows sales of old stock (purchased at the lower prices) and new stock (purchased at the higher prices). The new stock is only sold in April 2020[90].

72. The RBB Report engages in a series of speculations and assertions around the potential that other costs may have changed and should be accounted for in determining the "net margin", but speculation and assertion is all they remain.

72.1. For a multi-product retailer, the mark-up they typically earn on a particular product or SKU reflects the mark-up required to recover overheads and earn a normal return in the context of a competitive retail market for that product.

72.1.1. For this reason, price gouging laws frequently refer to the customary mark-up of the retailer in determining if the price increase in cost-justified, and similarly the Regulations refer to the mark-up in the three months prior.

[89] Trial Record: p 91.

72.1.2. For instance, the California Penal Code § 396[91] which specifically outlaws a price increase of 10% or more that is not cost justified, makes specific reference to the customary mark-up in seeking to determine whether the increase was justified:

> *"However, a greater price increase is not unlawful if that person can prove that the increase in price was directly attributable to additional costs imposed on it by the supplier of the goods, or directly attributable to additional costs for labor or materials used to provide the services, during the state of emergency or local emergency, and the price is no more than 10 percent greater than the total of the cost to the seller* ***plus the markup customarily applied by the seller for that good or service in the usual course of business immediately prior to the onset of the state of emergency or local emergency****."*
> [emphasis added]

72.2. Whilst Smith seems to make much of the term "net margins" in the Regulations, it must be noted that the Regulations refer to both mark-ups and net margins, because they anticipate cases in terms

[91] https://codes.findlaw.com/ca/penal-code/pen-sect-396.html

of retailers or distributors, where mark-ups are relevant, and manufacturers, where net margins are relevant.

72.3. However, even if one was to consider overheads and hence net margins, the evidence placed before the Tribunal in the RBB Report is that March sales for Dis-Chem were [redacted]% higher than the same month the year before and [redacted]% higher than February sales (which is not due to seasonality, as February sales were higher than March sales in 2019). As such, overhead costs would have spread over larger volumes and therefore declined, if anything.

73. Smith also speculates that in competitive environments firms may set prices based on current or future anticipated costs of procurement rather than historical costs.[92] However, this is simply speculation and assertion as Smith provides no actual evidence that this is the case for Dis-Chem (or retailers of its ilk more generally) and nor does Dis-Chem seek to confirm that this is how they operate or the reason why they increased prices[93]. Indeed the factual evidence is against RBB on this one, as the price increases were all pushed through from mid February to 9 March, and yet it is only after this date that Dis-Chem started receiving higher quotes[94] and only on 13 March did it get a higher quote from its existing suppliers[95] In

[92] Trial Bundle: p 361 para 6, p 385 paras 85 – 86.
[93] There is no mention made in the Answering Affidavit of any future anticipated procurement costs.
[94] Trial Record: p 87, Table 3.
[95] Trial Record: p 85 para 50.

contrast to the assertions of RBB, Dis-Chem states that it only reduced prices for masks in late April once it took delivery of lower priced stock[96]. If it priced based on future anticipated costs then it would have reduced prices earlier. This is precisely one of the situations where the RBB Report and the Answering Affidavit contradict one another, and, as such, the Answering Affidavit must prevail.

74. The Commission submits that, during a state of emergency or disaster, the price increase should be no more than 10% greater than the total of the cost to the seller, plus the mark-up customarily applied by it for that good or service in the usual course of business immediately prior to the onset of the state of emergency or disaster.[97] Dis-Chem's mark-up applied substantially exceeds this.

75. In light of Dis-Chem's admitted pricing conduct during the complaint period, its failure to provide any valid justification on the facts for the increased prices charged, and the failure of Smith to provide any economic justification for the pricing conduct, it is submitted that the Commission has made out a case that Dis-Chem charged excessive prices for the complaint products, in breach of section 8(1)(a) of the Act, during the complaint period.

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[96] Trial Bundle: p 94 paras 59 - 60.

[97] Trial Bundle: p 44 para 28 and p 47 para 35, where Aproskie references the Californian Penal Code PEN § 396, Arkansas, California, Delaware, District of Columbia, New Jersey, Oklahoma, Utah, and West Virginia laws on price gouging and the typical US test for price gouging.

Price increase is unreasonable

76. Section 8(3) of the Act provides that the determination of whether a price is excessive, requires a determination of whether or not the difference between the price and the competitive price is unreasonable.

77. The relevant factors indicated in section 8(3) that may be considered in the determination of whether a price is higher than a competitive price, find identical application in the determination of whether or not the difference between the price and the competitive price is unreasonable. The factors indicated above in respect of the determination of an excessive price are equally applicable here.

78. No valid explanation is proffered by Dis-Chem for its significant price increase following the onset of the COVID-19 pandemic. Despite Dis-Chem's contentions of an anticipated price increase by its supplier, no such increase was implemented before 30 March 2020[98]. There is thus no reasonable relation to the costs to justify increasing the price of the complaint products multiple times from 14 February to 9 March such that margins increased from [redacted] in January to [redacted] in March 2020.

79. Dis-Chem seek to argue that the price is reasonable because the category

[98] Trial Bundle: p 91, Table 4; p 93 para 57.

buyer Ms Lynnette Parsons had regard to the price of surgical masks at [redacted] in early March 2020, and that it always prices with reference to competitors (with evidence from late April 2020, which is outside the complaint period).

79.1. However, the price of a competitor does not necessarily equate to a competitive price. This is especially so in a period of disaster where there are demand/supply disruptions to the market. Dis-Chem itself acknowledges the substantial increase in demand for surgical masks and a severe shortage emerging for their supply, resulting in higher prices being quoted by manufacturers.

79.2. In the retail context, the gross margin or mark-up on goods supplied is the competitively relevant variable, as this is the return made by the retailer on the goods which it resells and does not manufacture. The RBB Report cites a fair return on costs as its standard for determining a competitive price, in a retail context that is the mark-up on the product.

79.2.1. The typical gross margin made by Dis-Chem on face masks in December 2019 and January 2020 prior to the pandemic provide a suitable benchmark as to what competitive mark-ups/margins on these products ought

to be. These are [redacted][99] and Smith estimates the margin for the three months prior to March 2020 at [redacted][100].

79.2.2. In contrast, Smith calculates the margins for March 2020 at [redacted] (Table 7 of the RBB report) and this is confirmed by Table 8 of the Answering Affidavit.

79.2.3. These are clearly not competitive gross margins for the retail of such products.

79.3. The reality is that the [redacted] price did not place a constraint on Dis-Chem, as it did not prevent Dis-Chem from almost doubling its gross margins.

79.3.1. So, while Ms Parsons states that prices were referenced as against [redacted] in early March 2020 and adjusted accordingly, the evidence on pricing adjustments indicates that not only had Dis-Chem been adjusting upward the price of face masks since 14 February 2020 already, but the further March 2020 adjustment was to increase prices further on 7 March for 5pc packets from roughly R4 per mask (incl. VAT) to R4.60 per mask and then on 50pc a few days later.

[99] Trial Record: p 457 para 52.1.
[100] Trial Record: p 400, table 7.

79.3.2. This was not an exercise undertaken to reduce the price, but rather to increase the price.

79.3.3. Ms Parsons did so in the full knowledge that the costs of sales for the face masks was around [redacted] on average (as the category buyer) and that Dis-Chem would subsequently be making a margin far in excess of what it would ordinarily be able to earn in a competitive market for retailing face masks.

80. Therefore, the price that Dis-Chem charged for the stock it had on hand and continued to source into March was unreasonable given the cost of procuring that stock and the competitive margins that would customarily be applied to that product.

81. Dis-Chem's excessive price is clearly exploitative and is directed at taking advantage of consumers and customers at a time when surgical face masks are in high demand, in response to the international health crisis being experienced. There is simply no other reason for the repeated price hikes effected, other than an intention to profiteer.

82. The CAC in *Sasol Chemical Industries Limited v Competition Commission*

(*Sasol)*[101] confirmed that a robust approach may be appropriate in certain cases. For example, "*where the actual price is shown … to exceed the normal price for roughly similar products to a degree which is, on the face of it, utterly exorbitant, then the need to quantify economic value more precisely before concluding that the actual price bears no reasonable relation to it may fall away. In this way a* prima facie *case would have been made out, leaving it to the respondent firm to adduce evidence to the contrary if it is to avoid the case against it becoming conclusive*."

83. It is submitted that similar circumstances prevail in the current matter and that Dis-Chem's historical price charged for the identical surgical masks that constitute the complaint products bear no reasonable relation to the prices charged during the complaint period, as reflected in the more than doubling of the gross margin earned by Dis-Chem.

84. In these circumstances it is submitted that the Tribunal should find that the Dis-Chem's price increases effected during the complaint period are unreasonable.

DETRIMENT TO CONSUMERS

85. Section 8(1)(a) requires that the excessive price be charged "to the detriment of consumers". This requires a value judgment. However, it is

[101] *Sasol Chemical Industries Limited v Competition Commission* (131/CAC/Jun14) [2015] ZACAC 4; 2015 (5) SA 471 (CAC) (17 June 2015) at [102].

does not appear to be in dispute that, if the prices complained of are held to be excessive, detriment to consumers and customers will have resulted.

86. In *Mittal*[102] the CAC noted (and did not refute) the Tribunal's finding that the phrase "*to the detriment of consumers*" is subordinate and should be treated as a superfluous description of an excessive price, rather than a qualifier of its likely effects. As the Tribunal correctly pointed out '*What, after all, could more clearly inure to the detriment of consumers than an "excessive price"?* '

87. The detriment to consumers is all the more abhorrent in this complaint referral, because it is in respect of surgical masks in a time of crisis when such masks are seen as essential to protect the health, safety and welfare of consumers and customers, and also frontline and healthcare workers with greater exposure to the disease. High prices not only harm directly those that purchase, but also exclude those that are unable to purchase, primarily the poor. It is for this reason that the Regulations were made in the first place.

88. Competition authorities may prioritise products that protect the health of consumers such as face masks and sanitising gel, as indicated by the ECN, but this priority should extend to any market power created by COVID-19, from the commerce and entertainment required by situations

[102] At para 55.

of lock-down and social distancing to developing therapeutic advances.[103]

89. The complaints made by the Dis-Chem's consumers and customers regarding the excessive prices charged by the Dis-Chem[104] constitute direct evidence of the detriment suffered by customers and consumers.

90. Dis-Chem contends that there has been no detriment to its customers. The basis for such a claim appears to be based on the assertion that its actions were in the interests of consumers. Dis-Chem argue that it broke bulk to ensure supply to individual customers, it instituted rationing and, in April 2020, it made low margins, even reducing prices once it secured lower supplier prices around 20 April 2020. However, there is nothing altruistic in Dis-Chem's behavior.

90.1. First, consumers and customers did not benefit from Dis-Chem raising the price of surgical masks multiple times in a short period when its costs of such masks was in fact declining. Rather, this allowed Dis-Chem to see gross margins rise from [redacted] in January to [redacted] in March.[105]

90.2. Second, it was Dis-Chem and not consumers or customers that

[103] TILEC Discussion Paper DP 2020-007 EU Competition Law and COVID-19 By Francisco Costa-Cabral,Leigh Hancher, Giorgio Monti and Alexandre Ruiz Feases 3.March 22, 2020 ISSN 2213-9419 http://ssrn.com/abstract=3561438 at p 10.
[104] Trial Bundle p 15 para 24.
[105] Trial Bundle: p 442 para 30.

evidently benefited from initially breaking bulk, as outlined in the Replying Affidavit, because the incremental costs of doing so (i.e. repackaging costs of [redacted] per mask) were a fraction of the higher price imposed for smaller packets as opposed to larger packets ([redacted] per mask).

90.3. Third, Dis-Chem only instituted rationing on 19 March 2020, when the Regulations required it to do so. It has not claimed that it rationed surgical masks (or any other product) prior to this point.

90.4. Fourth, its behavior in April 2020 is more likely as a result of the impact of consumer and customer outcry over the price increases of many retailers, including Dis-Chem, and the active enforcement by the Commission of excessive pricing violations and the numerous public announcements made by the Commission that it would urgently and actively take steps to address the scourge of price gouging in the midst of the COVID-19 pandemic.

91. In this case Dis-Chem's prices were exploitative, since it knew full well that there was a significant increase in demand during the complaint period and that consumers and customers were likely to not be able to source the surgical masks elsewhere. The material impact of such excessive pricing is further evident from the significant, increased sales made by Dis-Chem during the complaint period.

THE APPROPRIATE RELIEF

92. In the Notice of Motion the Commission seeks an order, *inter alia,:*

92.1. declaring that Dis-Chem's pricing conduct during the period 5 March 2020, has contravened the provisions of section 8(1)(a) of the Competition Act, read with Regulation 4 of the Regulations;

92.2. interdicting and restraining Dis-Chem from engaging in any further conduct in contravention of section 8(1)(a) of the Competition Act until the end of the national state of disaster; and

92.3. directing Dis-Chem to pay an administrative penalty, in terms of section 58(1)(a)(iii), in the amount of no less 10% of its annual turnover for the preceding financial year.

93. The Commission submits that the facts of this case, as proven by the Commission, warrant extraordinary remedies to address an extraordinary situation, and to immediately put an end to Dis-Chem's exploitative pricing conduct.

94. Within the context of the COVID-19 pandemic, Dis-Chem's pricing conduct during the complaint period must be viewed as a deliberate attempt to

profiteer by hiking up the prices of critically important surgical masks, to the prejudice of frontline and healthcare workers and members of the public. It would be appropriate for the Tribunal, in this matter, to mete out relief that reflects the unacceptable nature of Dis-Chem's conduct, and the prejudice suffered by consumers and customers, as a result thereof.

ADMINISTRATIVE PENALTY

95. The Tribunal may impose an administrative penalty for a prohibited practice in terms of section 8(1)(a).[106] Such administrative penalty may not exceed 10% of Dis-Chem's annual turnover in the Republic during its preceding financial year.[107] The Dis-Chem Group generated a total revenue of R21.4 billion in the 2019 financial year, of which R19.64 billion is from its retail business alone.

96. Determining an appropriate administrative penalty is, like sentencing in a criminal matter, case-specific. It is not, and can never be, scientific.[108]

97. When determining an appropriate penalty, the Tribunal must consider the following factors[109]:

[106] Section 59(1)(a) of the Act.
[107] Section 59(2) of the Act.
[108] *Isipani Construction (Pty) Ltd v Competition Commission* (144/CAC/Aug16CT, 019950) [2017] ZACAC 3 (14 September 2017) at [78].
[109] Section 59(3) of the Act.

97.1. the nature, duration, gravity and extent of the contravention (the exploitation of vulnerable consumers and customers in respect of surgical masks, essential in the fight against COVID-19, during a period when bulk buying and a mass scramble for masks in reaction to the crisis was experienced, must be considered as both grave and reprehensible);

97.2. any loss or damage suffered as a result of the contravention (consumers and customers were forced to pay at materially increased prices, which may have resulted in them having to purchase fewer masks than required);

97.3. the behaviour of Dis-Chem (in the present matter Dis-Chem continues to deny that it priced the surgical masks excessively and justifies its conduct with references to largely unsubstantiated and speculative cost increases);

97.4. the market circumstances in which the contravention took place, including whether, and to what extent, the contravention had an impact upon small and medium businesses and firms owned or controlled by historically disadvantaged persons (the contravention took place subsequent to and in response to the onset of the COVID-19 pandemic – a time when the South African consumers and customers are incredibly vulnerable – which factor Dis-Chem sought

to profiteer from);

97.5. the level of profit derived from the contravention (the Commission estimated that during the complaint period Dis-Chem enjoyed an additional profit attained through its excessive pricing of at least [redacted];

97.6. the degree to which Dis-Chem has co-operated with the Commission and the Tribunal (Dis-Chem continues to deny the contravention, despite its admission that its gross margin in March was [redacted]% for the complainant products and exceeded its margins on the same products in the three months prior of [redacted]% by more than [redacted]fold, requiring the Commission to focus its resources during lockdown towards the prosecution of this matter);

97.7. whether Dis-Chem has previously been found in contravention of this Act (this is not alleged by the Commission); and

97.8. whether the conduct has previously been found to be a contravention of this Act or is substantially the same as conduct regarding which Guidelines have been issued by the Competition Commission in terms of section 79 (the conduct is the same as the conduct expressly prohibited in the Regulations, which were published during the complaint period).

98. The 10% upper limit is reserved for the most egregious conduct, where there is an absence of any mitigating factors.[110] The penalty must be proportional in severity to the degree of blameworthiness of the offending party, the nature of the offence and its effect on the South African economy in general and consumers in particular and must be high enough to have a deterrent effect.[111]

99. In *Isipani Construction (Pty) Ltd v Competition Commission*[112] (*Isipani*) the CAC referenced the six-step approach devised by the Tribunal in *The Competition Commission v Aveng (Africa) Limited t/a Steeledale and others*[113] *(Aveng)* to determine an appropriate administrative penalty. While the six-step approach goes a long way towards achieving a proportionate penalty, the CAC noted that *"There may at some future point be cases where it cannot or ought not to be followed as its application, or the outcome of its application, would not serve the interests of justice."* It is respectfully submitted that the present matter is such a case.

100. In *Southern Pipeline Contractors and Another v Competition Commission*[114] (*Southern Pipelines)* the CAC confirmed that an administrative penalty administrative penalty should promote the important

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[110] *Isipani Construction (Pty) Ltd v Competition Commission* (144/CAC/Aug16CT, 019950) [2017] ZACAC 3 (14 September 2017) at [74].
[111] *Southern Pipeline Contractors and Another v Competition Commission* [2011]2 CPLR 239 (CAC) at [9].
[112] *Isipani supra* at [79].
[113] *Competition Commission v Aveng (Africa) Ltd t/a Steeledale and Others* (84/CR/Dec09, 08/CR/Feb11) [2011] ZACT 18 (6 April 2011).
[114] (105/CAC/Dec10, 106/CAC/Dec10) [2011] ZACAC 6 (1 August 2011) at [9].

objective of deterrence and "*should be proportional in severity to the degree of blameworthiness of the offending party, the nature of the offence and its effect on the South African economy in general and consumers in particular".* The cap of 10% imposed by the Act ensures that the Dis-Chem is treated fairly and its business not prejudiced by the imposition of the penalty.

101. Penalties should be significant and sufficiently onerous to act as a deterrent. Regard should be had, in particular, to the expected benefit of the conduct when considering a deterrent penalty, in order to ensure that the benefit which flows directly or indirectly from the contravention is disgorged by Dis-Chem.[115]

102. The Regulations provide insight into the penalty that the Minister of Trade and Industry deems appropriate to apply in the event of breach of the Regulations, which includes one or more of the following: "*a fine of up to R1 000 000.00, a fine of up to 10% of a firm's turnover, and imprisonment for a period not exceeding 12 months".*

103. The Tribunal has previously applied its six-step methodology to contraventions of section 8. The Commission however submits that for matters in relation to excessive pricing in the context of the current global health crisis, this methodology is inappropriate. The Tribunal should

[115] *Southern Pipelines* at [58] – [59].

determine the appropriate administrative penalty within the context of the current extraordinary circumstances, and should not be bound by any formula or methodology.

104. In the United States, some states apply a “treble damages” methodology in determining damages to be paid in respect of price gouging conduct. This essentially amounts to the penalty being determined by trebling the respondent’s excess profit earned, as a result of its exploitative pricing conduct.

105. The treble damages penalty calculation methodology is consistent with section 59(3) of the Act. The penalty determination in terms of section 59(3) includes the consideration of loss or damage suffered as a result of the contravention, which is what the treble damages methodology seeks to achieve.

106. As calculated in the Commission’s Replying Affidavit, the excess profit earned by Dis-Chem during the period March 2020 is [redacted]. As such, following the treble damages principle outlined above, the applicable penalty would be calculated as indicated below:

Excess profits earned	[redacted]
	*3
Ultimate fine	[redacted]

107. The Commission submits that, even should the treble damages methodology be applied in this matter, it will not result in the imposition of an administrative penalty that is proportional to the extortionate conduct of Dis-Chem.

108. It is respectfully submitted that the facts of this matter, viewed as they must be through the lens of the COVID-19 pandemic, require that a significant administrative penalty be imposed against Dis-Chem. It is accordingly respectfully submitted that this is an appropriate case in which a penalty of 10% of annual turnover should be levied.

CONCLUSION

109. Once the Commission has established a *prima facie* case of excessive pricing, Dis-Chem bears the *onus* to disprove the Commission's case.[116] While the Commission has presented evidence that warrants a finding of excessive pricing in this referral, Dis-Chem has failed to discharge its *onus* to rebut the Commission's case.

110. In the circumstances it is appropriate for the Tribunal to grant the Commission the relief it seeks, including the imposition of an administrative penalty against Dis-Chem.

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[116] Section 8(2) of the Act.

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C SLUMP

THE COMPETITION COMMISSION

3 May 2020