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

DIS-CHEM'S HEADS OF ARGUMENT

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INTRODUCTION

1. South Africa, along with the rest of the world, is currently in the throes of a global pandemic and national public health disaster caused by the novel coronavirus SARS-CoV-2 which results in the novel coronavirus disease 2019 ("**COVID-19**").

2. Unfortunately, this particular strain of coronavirus is not the only novelty that has arisen here. At least two others are relevant to these proceedings.

   2.1. First, Dis-Chem Pharmacies Limited ("**Dis-Chem**") faces unprecedented and ever-changing challenges to its business, supply chains and customers arising from the national disaster. Its evidence shows the extraordinary market conditions in which it is managing to continue to trade and despite which it is continuing to deliver value to its much-appreciated customers and safe working conditions to its valued staff.

   2.2. The facts of this case are a real-time case study of how a previously stable market was shocked by disruptions on both the supply and demand side. These dislocated it from historical trends momentarily and the market then responded as one would expect -- attracting entry, expanding supply and ensuring effective and efficient market clearing of demand through price signals -- to settle back at levels that are broadly consistent with previous experience.

2.3. Second, the Commission has brought a case to the Tribunal that, at every turn, is novel, unprecedented and untested. Not only does it rely on recently-promulgated regulations to provide its theory of harm pleaded in its complaint referral affidavit, but it does so when it also practically ignores the requirement to apply the recently amended provisions of section 8 of the Competition Act, No 89 of 1998 ("**the Act**") regarding which there is currently no caselaw to guide the Tribunal. It appears common cause that this remains a section 8 complaint referral, but the Commission ignores many of the requirements of that section and fails to establish its case in terms of all of its elements in its founding papers.

2.4. The Commission's case also resorts to unproven economic claims and conjecture that lack a clear foundation or pedigree in the economics literature regarding excessive pricing, and which ignore the evidence.

2.5. All of which, demands caution and circumspection from the Competition Tribunal ("**the Tribunal**"). This complaint referral confirms the prudence of the global approach to excessive pricing, namely that it is rarely prosecuted by competition regulators anywhere due to its manifest complexity, inherent difficulty and obvious pitfalls for the competitive landscape, especially when pursued against a multi-product firm.

2.6. Blunt enforcement without diligent investigation and careful consideration will smother market signals and eliminate the incentives of firms to invest in obtaining supply of essential goods in impossibly challenging market circumstances. The obvious and likely dangers of over-enforcement by competition authorities in this context loom large, and are amplified by the demands of the national public health disaster in which this complaint referral is taking place.

3. The salient facts to be noted and which are expanded upon in the detailed factual account set out below are that:

3.1. Prior to the outbreak of the COVID-19 pandemic, Dis-Chem's sales of surgical masks comprised an insignificant line item.

3.2. Towards late January and early February 2020 the demand for masks at Dis-Chem stores increased substantially, particularly from buyers of large volumes in bulk purchases.

3.3. When Dis-Chem wanted to replenish supply to meet its customers' demand, it was unable to procure the volumes required. Dis-Chem's one local manufacturer supplier had no stock to supply it. Dis-Chem thus had to find new sources of supply. [redacted]

[redacted].[1]

3.4. Faced with customers' demand requirements and the prospect of a short delay in supply responses, Dis-Chem temporarily shifted away from the sale of larger pack sizes of masks in order to ensure that its day-to-day customers had access to masks (rather than potential resellers). Dis-Chem thus focused on selling single masks and adjusted its prices in line with market conditions, specifically taking into consideration -- and pricing below -- the prevailing selling prices of its major competitors and the replacement costs of its inventory of masks.

3.5. To ensure that its customers would have access to masks Dis-Chem purchased significant volumes of masks [redacted], albeit at higher prices and significant cost. Logically, Dis-Chem had to increase its sales price of these masks to cover its increased costs.

3.6. As global mask manufacturing capacity increased in reaction to the high global demand for masks, additional supply has become available. This has meant that Dis-Chem has since been able to procure masks at better prices. Dis-Chem has passed on these

[1] Dis-Chem's Answering Affidavit, paragraph 60, at page 94 of the Pleadings Bundle.

lower input costs to its customers by repeatedly decreasing the price of masks.

3.7. Importantly, Dis-Chem started passing on these costs savings before the Commission indicated to it that it was being investigated for excessive pricing.

3.8. Although, when compared to percentage gross margins in December and January, Dis-Chem's percentage gross margins on mask sales increased in February and early March in anticipation of its significantly higher input costs, these margins have fallen substantially during late March and April, as a result of these very high input costs.

3.9. For the period following 19 March 2020, Dis-Chem's percentage gross margins are significantly lower than the three-month period prior to 1 March 2020. And its pricing remains below that of competitors and below that deemed acceptable by National Treasury going forward.

4. For all of the reasons submitted by Dis-Chem, its conduct is not a contravention of the Act.

4.1. Were the Tribunal to find that a short term price change, in this context, is excessive pricing in contravention of the provisions of section 8 of the Act, then it would be ignoring all that the competition world knows about excessive pricing. It would

discard all of the safeguards that are inherent in the very notion of an “excessive” price, which safeguards prevent undesirable and unintended consequences, including harm to consumers, and in particular poor consumers.

4.2. The global health pandemic does not demand that competition regulators start over afresh. It, rather, requires the careful continuation of decades of thoughtful policy choices to ensure that firms with scale are incentivised to participate in markets even in times of national disaster and global health emergency, and also requires that regulators avoid the temptation to gamble with real-time price regulation in an economy beginning to buckle under the effects of the crisis.

4.3. To do otherwise, as the Commission urges, the Tribunal would have to satisfy itself that the facts of this case justify (i) a radical obliteration of competition policy and economic theory, and (ii) a contortion of the provisions of the Act. This case, in which a multi-product firm momentarily raised prices to below its replacement cost quotations, and below its competitors’ prices.

4.4. Where this firm then incurred significant costs and undertook extraordinary measures to increase supplies thousands of fold in a matter of weeks. And where this firm accomplished all of this during a global pandemic, when global and domestic logistics and supply chains almost ground to a halt.

4.5. This case is about a firm operating at the start of the recession of a lifetime in which consumer spending has cratered, and in which that firm passed on substantial cost savings as they arose, and cut its margins to the bone before the Commission even began its superficial and cursory investigation of a complaint against Dis-Chem.

4.6. The understandable zeal for regulators to respond to the national disaster must be tempered and guided by fidelity to the rule of law and the statutory framework that governs their important work.

5. We, respectfully, expect that the Tribunal could not be persuaded to follow such a reckless path in this case and, instead, will prudently use this case to provide guidance to the Commission as to the characteristics and elements of a true case of excessive pricing of essential goods in this market to enable the Commission to bring other cases against other firms, namely those that in fact engaged in unlawful conduct that contravened section 8 of the Act read with regulation 4 of the the Consumer and Customer Protection and National Disaster Management Regulations and Directions, Government Notice No 350 of Government Gazette No 43116, promulgated on 19 March 2020 ("**the Regulations**").

6. We also record at the outset that:

6.1. First, the urgency for which the Commission contended in its founding papers has fallen away. The Commission belatedly concedes in its replying affidavit that its case is now confined to March 2020 which ended more than a month ago. Even on the

Commission's version, therefore, there is no ongoing consumer harm such that the case must be disposed of urgently. There is therefore no reason that the case must proceed in an unreasonably hurried fashion. Dis-Chem is prejudiced by having to defend itself under these circumstances and reserves its rights in that regard. It is plainly unfair to have a case of this magnitude, complexity and importance determined in less than two weeks (from the date of referral on 22 April 2020 to the date of argument).

6.2. Second, if the Commission's interpretation of the Regulations laid out in its complaint referral is correct (which we deny), then the Regulations are *ultra vires* and Dis-Chem reserves its right to approach the appropriate forum to have the Regulations set aside.

6.3. We set out below how the Regulations may be considered *intra vires* and capable of being read lawfully and that is the interpretation that we advance before the Tribunal in order to have this referral determined.

6.4. Finally, the Commission has elected to proceed by way of application. Any material disputes of fact that have arisen must be decided in Dis-Chem's favour.

RELEVANT FACTUAL BACKGROUND

The failure of the Commission to properly investigate

7. The Commission's investigation of this complaint can generously be described as superficial and cursory. It consisted in its entirety of a single email exchange providing a high-level spreadsheet to the Commission and one telephone conversation with one representative of Dis-Chem who explained the information and actual position in the business to the Commission.[2] No other person was spoken to and no further information was sought from Dis-Chem or any market participant or person with information that would have enabled the Commission to in fact investigate the complaint it had received. That spreadsheet and that telephone call conveyed information and data that already should have given the Commission pause as to the merits of any complaint against Dis-Chem.

8. Unfortunately, it did not.

9. As is obvious from the complaint referral, the Commission made no investigation into the issues of:

    9.1. Dominance;

    9.2. Market Definition;

[2] The Commission's Supporting Affidavit, paragraph 43, page 52 of the Pleadings Bundle.

9.3. Entry;

9.4. Competitors' conduct;

9.5. Costs and supply constraints; or

9.6. Net margins.

10. This investigation fails to meet the obligation on the Commission to investigate a complaint under section 21(1)(c) of the Act, including utilising its extensive powers in terms of section 49A, for example, to obtain information from other market participants at the relevant levels of the supply chain so that it could meaningfully consider the market dynamics, competitive conditions and ease of entry. Even though the world is in unprecedented times, these requirements do not fall away.

11. The consideration of one spreadsheet (containing data that obviously demands greater exploration, interrogation and investigation) and a single cursory telephone call (that ought to have provided comfort that this was not the case and not the conduct to refer to the Tribunal, rather than being ignored), constitute inadequate investigation of the complaint. The Commission's subsequent refusal to meet with Dis-Chem's legal representatives is also regrettable.

12. All of which have resulted in the Commission referring a defective and unsustainable case. Its efforts at refinement and recasting in reply do not assist the Commission. The demands of the COVID-19 pandemic do

not excuse these failures by the Commission. As a result, its pleaded case in the complaint referral is fatally flawed since it does not disclose a contravention of section 8 of the Act or of regulation 4.

13. It ought to be dismissed entirely.

14. We turn to provide an overview of the relevant background and contextual facts, beginning with Dis-Chem's business.

DIS-CHEM'S BUSINESS

15. Dis-Chem is a large pharmaceutical retailer listed on the Johannesburg Stock Exchange. Dis-Chem's main business includes, broadly, the operation of retail pharmacies, and the retail of personal care products, health and nutrition products, baby care products, as well as other FMCG. 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.[3]

16. Dis-Chem has 165 stores located across South Africa, with a further four stores located in Namibia and one in Botswana. Dis-Chem's operations are situated mainly in large and medium-sized metropolitan areas. In this regard, [redacted] of Dis-Chem's stores are located in Johannesburg, Pretoria, Cape Town and Durban; [redacted] are located in medium-sized metropoles such as Port Elizabeth, Bloemfontein and Nelspruit; while just [redacted] of its stores are located in small towns or villages. Within these metropoles, Dis-Chem positions its stores mostly in large malls and retail centres. Importantly, Dis-Chem deploys a national pricing strategy across its national store footprint, with all stores charging the same price for all products.[4]

17. [redacted]

[3] Dis-Chem's Answering Affidavit, paragraph 7, page 68 of the Pleadings Bundle.
[4] Dis-Chem's Answering Affidavit, paragraph 8, page 68 of the Pleadings Bundle.

[redacted][5]

18. As noted above, Dis-Chem's retail activities are focused on five market segments, being pharmacy; personal care; healthcare and nutrition; baby care; and other FMCG. Across these five market segments, Dis-Chem stocks a very large range of products. The sale of surgical masks falls within the personal care segment.[6]

19. Dis-Chem's business has seen rapid growth over the last 5 years, allowing it to grow from 99 stores in 2015, to its current footprint of 170 stores. Dis-Chem's growth strategy has resulted in it gaining an estimated market share of approximately [redacted] in the pharmacy market segment (based on internal market estimates in schedule 0 to 6 medicines, including oncology). Dis-Chem's estimated share in the personal care segment is [redacted], [redacted] in the healthcare and nutrition segment, and [redacted] in the baby care segment.[7]

20. Dis-Chem faces a wide range of competition across the market segments in which it participates. In respect of its core pharmacy business, Dis-Chem's largest competitors are Clicks, Alpha Pharm and various independent pharmacies.[8]

5 Dis-Chem's Answering Affidavit, paragraph 9, page 68 of the Pleadings Bundle.
6 Dis-Chem's Answering Affidavit, paragraph 10, page 69 of the Pleadings Bundle.
7 Dis-Chem's Answering Affidavit, paragraph 12, page 69 of the Pleadings Bundle.
8 Dis-Chem's Answering Affidavit, paragraph 13, page 70 of the Pleadings Bundle.

21. In respect of the other segments in which Dis-Chem competes, it faces staunch competition from the likes of Pick ‘n Pay, Spar, Checkers, Woolworths, Clicks, Makro and Game, depending on the product range under consideration.[9]

22. Dis-Chem also offers online retail sales. In relation to the sale of medicine and pharmaceutical products, Dis-Chem offers a delivery service for repeat prescriptions.[10]

23. Dis-Chem’s business operations also include wholesale activities, such as logistics, warehousing, fine distribution and supply chain management for its stores, which contributes [redacted] to its total revenue.[11]

24. We turn next to describe Dis-Chem’s business operations and how they rapidly evolved and adapted to the unfolding COVID-19 pandemic, in particular as they relate to the use of surgical masks and the explosion in demand for those products, coupled with skyrocketing costs in a challenging logistics and procurement environment.

9 Dis-Chem’s Answering Affidavit, paragraph 14, page 70 of the Pleadings Bundle.
10 Dis-Chem’s Answering Affidavit, paragraph 15, page 70 of the Pleadings Bundle.
11 Dis-Chem’s Answering Affidavit, paragraph 16, page 70 of the Pleadings Bundle.

CHRONOLOGY OF KEY EVENTS AND MARKET CONTEXT

November to December 2019

COVID-19 – Pandemic progression and impact in South Africa (November to December 2019)

25. The first cases of COVID-19 were only identified in Wuhan, China in December 2019, although at this stage the illness was simply being reported to the World Health Organization ("**WHO**") as a pneumonia of unknown cause. South Africa, as was the rest of the world, was at this stage untouched by the virus.[12]

Demand for masks (November to December 2019)

26. With the soon-to-be pandemic still in its nascent stage, Dis-Chem stores were trading as normal in November and December 2019. In respect of masks, and in particular the three surgical mask SKUs stocked by Dis-Chem at the time (i.e. the Surgical Face Mask Blue 50PC; Surgical Face Mask 5PC; and Surgical Face Mask Foliodress Blue, (also in packs of 50 units)),[13] sales volumes were at their typical levels – around [redacted] per month. In other words, masks were a miniscule line item across the multitude of products sold by Dis-Chem.[14]

12 Dis-Chem's Answering Affidavit, paragraph 18, page 71 of the Pleadings Bundle.
13 Dis-Chem's Answering Affidavit, paragraph 30, page 79 of the Pleadings Bundle.
14 Dis-Chem's Answering Affidavit, paragraphs 32 and Table 2, page 79 and 82 of the Pleadings Bundle.

Retail pricing of masks (November to December 2019)

27. The customers responsible for the purchases were likely individuals purchasing masks for their personal use.[15] Details of the prices charged by Dis-Chem (excluding VAT) for masks in November and December 2019 are set out below.[16]

    27.1. Surgical Face Masks 5pc - R9.52;

    27.2. Surgical Face Mask Blue 50pc - R41.70; and

    27.3. Surgical Face Mask Foliodress Blue 50pc - R65.18.

Supply of masks (November to December 2019)

28. Prior to the COVID-19 crisis, Dis-Chem sourced all of its mask supply from [redacted].[17]

29. During this period, Dis-Chem was easily able to procure adequate stock to meet the level of demand. In December 2019, Dis-Chem ordered just [redacted] masks to replenish its existing stocks.[18] Details of the prices paid

15 Expert Witness Statement of Patrick Smith, paragraph 120 and 121, page 404 of the Pleadings Bundle.
16 Dis-Chem's Answering Affidavit, Table 1, at page 81 of the Pleadings Bundle.
17 Dis-Chem's Answering Affidavit, paragraph 48, page 85 of the Pleadings Bundle.
18 Expert Witness Statement of Patrick Smith, Table 3, page 383 of the Pleadings Bundle.

by Dis-Chem for masks in November and December 2019 are set out in the table below.[19]

Table 1: Surgical Facial Mask Historical Purchase Price - November 2019 to December 2019

Product	Cost Price per SKU (excl. VAT)	Cost Price per Unit (excl. VAT)
Surgical Face Mask Blue 50PC (36125)	[redacted]	[redacted]
Surgical Face Mask 5PC (68566)	[redacted]	[redacted]
Surgical Face Mask Foliodress Blue (123335)	[redacted]	[redacted]

January 2020

COVID-19 – Pandemic progression and impact in South Africa (January 2019)

30. By January 2020, COVID-19 had started to spread beyond the borders of China. The causative pathogen of the disease was identified on 7 January 2020. On 13 January 2020 a case of COVID-19 was confirmed in Thailand (the first confirmed case outside of China). At the end of the month, on 30 January 2020, having now spread to many other countries around the world, the WHO declared the COVID-19 outbreak a Public Health Emergency of International Concern ("**PHEIC**").[20]

31. Although no cases had been reported in South Africa at this stage, general news coverage around COVID-19 began to increase in January 2020, and the Department of Health of South Africa ("**DoH**") made its

19 Dis-Chem's Answering Affidavit, Table 1, page 81 of the Pleadings Bundle.
20 Dis-Chem's Answering Affidavit, paragraph 18 and 19, page 71 of the Pleadings Bundle.

first media statement regarding COVID-19 on 23 January 2020. The statement, headed "*Novel Coronavirus (2019-nCoV), No cause for panic*", noted that no cases of COVID-19 had yet been detected in South Africa. Travellers to Wuhan, China were advised to avoid contact with animals, and encouraged to practice good hand hygiene and cough etiquette in order to reduce the risk of infection with respiratory viruses.[21]

32. The Minister of Heath, Dr Zwelini Mkhize, held his first press briefing regarding the COVID-19 outbreak on 29 January 2020.[22]

33. The DoH's first media statement on COVID-19 and the Minister's first briefing on COVID-19 are relevant in one respect – neither made any reference to the use of masks as a measure that could assist in the combatting of the spread of COVID-19 among members of the general populace. The implication being, at this stage, and based on the prevailing government advice (which was no doubt being informed by science and medical advice), that masks would not form a particularly important part of any preventative measures adopted in South Africa.

Demand for masks (January 2019)

34. In January 2020, particularly towards the latter part of the month, Dis-Chem started to experience a surge in the demand for its masks. In this

21 Dis-Chem's Answering Affidavit, paragraph 20, page 71 of the Pleadings Bundle.
22 Dis-Chem's Answering Affidavit, paragraph 21.1, page 72 of the Pleadings Bundle.

regard, the number of masks sold jumped from the typical monthly level of around [redacted] to a staggering [redacted] units in January alone.[23]

35. This unprecedented jump in sales volumes seems to have been triggered by a particular type of buyer, different from the typical purchaser that would have been responsible for purchases prior to the pandemic and different to Dis-Chem's typical FMCG consumer. For instance, a single customer purchased [redacted]. In fact, [redacted] of all the masks purchased in January 2020 were acquired by just [redacted] of the customers. In other words, the vast majority of the customers buying masks in January 2020 were not consumers looking to buy masks for their personal use. Rather, these were bulk buyers. While Dis-Chem's independent expert witness, Patrick Smith, and Dis-Chem itself are unable to conclude whether these masks were purchased to target export or domestic resale opportunities, these would be logical inferences to draw since that volume of masks could not be for personal use.[24]

Retail pricing of masks (January 2019)

36. Notwithstanding the huge surge in demand, Dis-Chem did not alter its prices in January 2020. It did, however, introduce a new pack size for the Surgical Face Mask Foliodress Blue on 30 January 2020. In this regard, Dis-Chem began repackaging the Surgical Face Mask

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23 Dis-Chem's Answering Affidavit, paragraph 36 and Table 2, page 81 and 82 of the Pleadings Bundle.

24 Expert Witness Statement of Patrick Smith, paragraph 120 and 121, page 404 of the Pleadings Bundle.

Foliodress Blue, which until now had typically been sold as a box of 50 units, as single units (as well as units of 5 and 10) to ensure that it had sufficient stock to satisfy the needs of its retail customers (as opposed to bulk buyers that were likely resellers or exporters). The single units retailed for R1.31 (excl. VAT).[25]

37. By breaking down the larger pack sizes into single units, Dis-Chem aimed to ensure that it was able to meet the increased demand while avoiding stock outages and ensuring equitable supply to all customers.[26]

Supply of masks (January 2019)

38. Owing to its existing stock levels in January 2020, Dis-Chem was able to meet the surge in demand experienced during the month. It did, however, start to increase the volume of new mask stocks purchased. In this regard, it ordered an additional [redacted]. However, of these orders, it ultimately only received [redacted] masks. This number was insufficient to replenish the sales of more than [redacted] masks in January. The additional stock was sourced from [redacted].[27]

25 Expert Witness Statement of Patrick Smith, Table 2, page 389 of the Pleadings Bundle.
26 Dis-Chem's Answering Affidavit, paragraph 43, page 83 of the Pleadings Bundle.
27 Expert Witness Statement of Patrick Smith, Table 3 and Figure 4, page 391 and 393 of the Pleadings Bundle.

February 2020

COVID-19 – Pandemic progression and impact in South Africa (February 2020)

39. While the global COVID-19 outbreak continued unabated in February 2020, the South African DoH indicated in a media briefing that it was continuing to monitor the situation relating to COVID-19 in South Africa.[28]

40. Towards the end of February, media reports began to surface suggesting that mask shortages could arise in the next six months. Importantly, these were masks generally used by healthcare workers in the prevention of the spread of TB, the so-called *"N95 masks"*, and not the masks that are the subject of the Commission's complaint.[29]

41. No recommendations in respect of the use of masks as a preventative measure had been made in South Africa by this point.[30]

Demand for masks (February 2020)

42. February 2020 saw another significant increase in demand with Dis-Chem's sales topping [redacted].[31] As with the bulk of the sales in January, the majority of these purchases seem to have been made by bulk buyers, particularly in the first half of the month. The largest single purchase in February 2020 was [redacted] The top 1% of customers bought [redacted] of the total number of masks sold. This is again

28 Dis-Chem's Answering Affidavit, paragraph 21.2, page 72 of the Pleadings Bundle.
29 Dis-Chem's Answering Affidavit paragraph 21.4, page 73 of the Pleadings Bundle.
30 Dis-Chem's Answering Affidavit paragraph 21, page 71 of the Pleadings Bundle.
31 Dis-Chem's Answering Affidavit, paragraph 38 and Table 2, page 82 of the Pleadings Bundle.

suggestive of masks being bought for export or resale as opposed to use by Dis-Chem's individual FMCG consumers.[32]

Retail pricing of masks (February 2020)

43. Likely recognising the developing trend in respect of the demand for masks, Dis-Chem adjusted its price upwards on two of its product lines for the first time. This price increase took place on 14 February 2020. In this regard the price for a box of Surgical Face Mask Blue (50pc) was increased to R47.78 (excl. VAT), while the price for the Surgical Face Mask Blue (5pc) SKU increased to R13.00 (excl. VAT). A second round of price increases was instituted at the end of the month on 26 February 2020, this time in respect of all available mask SKUs. Specifically, the prices (excl. VAT) post the increases are set out below:

43.1. Surgical Face Mask Blue 50pc - R78.22;

43.2. Surgical Face Masks 5pc - R17.35;

43.3. Surgical Face Mask Foliodress Blue 50pc - R78.22;

43.4. Surgical Face Mask Foliodress Blue 10pc - R17.35; and

43.5. Surgical Face Mask Foliodress Blue 1pc – R4.31.[33]

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32 Expert Witness Statement of Patrick Smith, paragraph 120 and 121 and Figure 3, page 404 and 391 of the Pleadings Bundle.

33 Expert Witness Statement of Patrick Smith, Table 2, page 389 of the Pleadings Bundle.

44. It is important to recall that at the time of these increases, the state of National Disaster was yet to be declared, and the Regulations were not yet published.[34] Moreover, as noted above, the prevailing information from the DoH at this time made no mention of masks and did not suggest the importance to the public that masks would develop later on. Viewed in this context, and keeping in mind the prevailing sentiment in relation to masks as it was then and not as it is now, these price increases can only be viewed as a normal response to prevailing market circumstances and cannot be considered to be unreasonable or excessive.

45. Dis-Chem continued to sell the repackaged Surgical Face Mask Foliodress Blue as single units throughout the month of February. The price of these single units remained unchanged for almost the entire month, with an increase being implemented on 26 February 2020. The new price was R4.31 (excl. VAT).

Supply of masks (February 2020)

46. February 2020 saw a number of significant developments in respect of the supply of masks in South Africa.

47. First, in early February 2020, the donation of 30,000 face masks to China by the South African supplier Universal Safety Products was commended by the DoH. The DoH encouraged other private sector businesses to do the same. At the same time, the Chinese government

[34] Government Notice No 350 of Government Gazette No 43116, published on 19 March 2020.

expressed an interest in purchasing an additional 20 million masks from Universal Safety Products. [35]

48. It is submitted that such commendation would not have been made, nor the encouragement of others to do the same, if it was thought that the availability of supply of masks to South African was critical at that stage.

49. Second, new sources of supply of surgical masks began to emerge. Many other local companies swiftly repurposed themselves to meet the increased demand for face masks. For example, Siyasebenza Manufacturing, based in Durban, started producing protective face masks when the pandemic first started in China and the supply of imported masks to South Africa decreased. Interestingly, Siyasebenza Manufacturing noted that due to the relatively high cost of local production, it would never have been able to profitably enter the market prior to the COVID-19 crisis. It only invested and entered the market for the manufacture of masks because of the higher prices it was able to command with the current market for masks.[36]

50. Third, Dis-Chem more than doubled the volume of new mask stocks purchased compared to the previous month. In this regard, it ordered an additional [redacted] masks. It received [redacted] masks, again insufficient volumes to replenish its stocks to meet increases in demand. This was

35 Dis-Chem's Answering Affidavit, paragraph 21.2, page 72 of the Pleadings Bundle.
36 Dis-Chem's Answering Affidavit, paragraph 27, page 77 of the Pleadings Bundle.

the last month in which Dis-Chem was able to secure volumes from its existing suppliers at prices comparable to historical levels.[37]

51. Fourth, a worrying trend started to develop in that Dis-Chem would receive a decreasing percentage of the stock ordered. In February 2020, Dis-Chem only received [redacted] of the volume of masks ordered. This was down from the [redacted] and [redacted] in December 2019 and January 2020, respectively.

52. Finally, as with January and March 2020, Dis-Chem's mask sales exceeded the volume of stock that it was able to purchase from its historic domestic suppliers, meaning that its stock levels were rapidly depleting.[38]

1 March 2020 to 18 March 2020

COVID-19 – Pandemic progression and impact in South Africa (1 March 2020 to 18 March 2020)

53. South Africa reported its first case of COVID-19 on 5 March 2020. Measures aimed at preventing the further spread of the virus in South Africa focused on washing hands, coughing and sneezing etiquette, and avoiding contact with people who were sick. No recommendations regarding the use of masks were being made at this point in time.[39]

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37 Expert Witness Statement of Patrick Smith, Table 3 and Figure 4, page 391 and 393 of the Pleadings Bundle.
38 Dis-Chem's Answering Affidavit, paragraph 48, page 85 of the Pleadings Bundle.
39 Dis-Chem's Answering Affidavit, paragraph 21.5, page 73 of the Pleadings Bundle.

54. On 11 March 2020, as a result of concerns around the alarming levels of spread and severity, the WHO made the assessment that COVID-19 can be characterised as a pandemic.[40]

55. On 15 March 2020, the South African government declared a state of National Disaster.[41]

Demand for masks (1 March 2020 to 18 March 2020)

56. Demand for masks continued to soar in March 2020, particularly in the period 1 to 18 March, i.e. immediately prior to the declaration of the National Disaster and the subsequent state of lockdown. Dis-Chem was unable to meet total demand for masks, and, due to its movement to smaller pack sizes, Dis-Chem's sales of masks (for the whole of March), were [redacted] units, less than 50% of its February volumes.[42]

57. Analysis of the customer data reveals that changes in the customer profile also began to occur in March 2020, in response to Dis-Chem's conversion to smaller pack sizes. Specifically, there was a decrease in the number of very large bulk purchases made – the largest single mask purchase in March was [redacted]. Conversely to the months of January and February, the top 1% of customers were responsible for only [redacted] of total

40 Dis-Chem's Answering Affidavit, paragraph 19, page 71 of the Pleadings Bundle.
41 Government Notice No 312 of Government Gazette No 43096, published on 15 March 2020.
42 Dis-Chem's Answering Affidavit, paragraph 36 and Table 2, page 81 and 82 of the Pleadings Bundle.

mask purchases – still a significant proportion, but indicative of a shift towards personal use buyers.[43]

Retail pricing of masks (1 March 2020 to 18 March 2020)

58. With demand remaining at very high levels, Dis-Chem introduced a further price increase on three of its SKUs. On 2 March 2020, the price of the Surgical Face Mask Foliodress Blue 50pc was increased to R81.70, on 7 March 2020, the price of Surgical Face Mask 5pc was increased to R19.96, and finally, on 9 March 2020, the price of the Surgical Face Mask Blue 50pc was increased to R173.87 (all these prices exclude VAT).[44]

59. In setting the above prices, Dis-Chem gave careful consideration to the competitive landscape around it. At no point did Dis-Chem operate without explicit regard to the prices being charged by its competitors. Indeed, Dis-Chem sought to ensure that its unit price was at all times lower than those charged by its main rivals so as to continue to deliver value and affordable products to its customers. In this regard, Dis-Chem and its buyer responsible for the determination of selling prices took particular note of the prices being charged by [redacted] at the time.[45]

60. Finally, from a timing perspective, the March price increases all occurred before the declaration of the state of National Disaster on 15 March

43 Expert Witness Statement of Patrick Smith, paragraph 120 and 121 and Figure 3, page 404 and 391 of the Pleadings Bundle.
44 Expert Witness Statement of Patrick Smith, Table 2, page 389 of the Pleadings Bundle.
45 Dis-Chem's Answering Affidavit, paragraph 63, page 96 of the Pleadings Bundle.

2020. Similarly, as with previous price increases, the prevailing information from the DoH at this time made no mention of masks and did not suggest the importance to the public that masks would develop later on. Furthermore, and as elaborated upon in the paragraphs below, Dis-Chem began to see significant increases in its cost of supply. Therefore, and again bearing in mind the prevailing sentiment in relation to masks as it was then, the March price increases must be viewed as a normal response to prevailing market circumstances and as a rational, reasonable and restrained response to market intelligence, and cannot be considered to be unreasonable or excessive.

Supply of masks (1 March 2020 to 18 March 2020)

61. As noted above, in March 2020 Dis-Chem's mask sales exceeded the volume of stock that it was able to purchase from its historic domestic suppliers, meaning that its stock levels continued to deplete.[46] Recognising that the demand for masks may not be transitory, Dis-Chem placed its largest volume orders yet – for approximately [redacted] masks.[47]

62. March was also the first month in which Dis-Chem was forced to use new suppliers in order to meet the surge in demand. In this regard, across the whole of March, Dis-Chem sourced masks from [redacted] different traders (as opposed to its usual [redacted] suppliers).[48]

46 Dis-Chem's Answering Affidavit, paragraph 48, page 85 of the Pleadings Bundle.
47 Expert Witness Statement of Patrick Smith, Table 3, page 391 of the Pleadings Bundle.
48 Expert Witness Statement of Patrick Smith, Figure 4, page 393 of the Pleadings Bundle.

63. Throughout the first part of March (and after the 18th), Dis-Chem obtained quotations from multiple traders offering masks. The prices quoted by these traders were significantly higher than the prices at which Dis-Chem had historically been able to procure stock from its traditional suppliers.[49]

64. In addition, the trend identified above in respect of decreasing percentages of the stock ordered actually being delivered continued. In March 2020, Dis-Chem received only [redacted] of the total volume of masks ordered. This was down from the [redacted] in February and the [redacted] and [redacted] in December 2019 and January 2020 respectively.[50]

19 March to 31 March 2020

COVID-19 – Pandemic progression and impact in South Africa (19 March to 31 March 2020)

65. While the COVID-19 pandemic continued to spread around the world, having declared a state of National Disaster on 15 March, the South African government took the further step of passing various regulations aimed at curbing the spread of the virus and coordinating the country's response thereto.

49 Expert Witness Statement of Patrick Smith, Table 4, page 392 of the Pleadings Bundle; and Dis-Chem's Answering Affidavit paragraph 53, page 86 of the Pleadings Bundle.

50 Expert Witness Statement of Patrick Smith, Table 3, page 391 of the Pleadings Bundle.

66. In particular, on 19 March 2020, the Minister of Trade, Industry and Competition, Ebrahim Patel, introduced the Regulations.

67. The status and legality of the Regulations is addressed below. It is sufficient for the moment to note that the Regulations purported to introduce factors that had not previously been considered in excessive pricing cases.

68. Regarding communications from the DoH on the use of masks, these remained unchanged in the second part of March.

69. A further significant development in South Africa's fight against the COVID-19 outbreak was the implementation of the lockdown measures with effect from 23:59 on 26 March 2020, i.e. 27 March 2020.[51]

Demand for masks (19 March to 31 March 2020)

70. While demand for masks remained high, there was a drop off in sales in the second half of March.[52] This is unsurprising given Dis-Chem's discontinuation of sales of larger pack sizes.

71. In addition, and as one of the measures introduced by Dis-Chem to ensure availability of masks to all customers, Dis-Chem introduced a 6 unit per item limit on various products, including masks. This would also account for the drop in sales volumes.[53]

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51 Government Notice No 398 of Government Gazette No 43148, published on 15 March 2020.
52 Expert Witness Statement of Patrick Smith, Figure 3, page 391 of the Pleadings Bundle.
53 Dis-Chem's Answering Affidavit, paragraph 46, at page 84 of the Pleadings Bundle.

Retail pricing of masks (19 March to 31 March 2020)

72. Post the introduction of the Regulations and up to 31 March 2020 (that being the end of the Commission's complaint referral, as narrowed in reply) Dis-Chem did not increase any of its mask prices. Further, as explained in greater detail below, once Dis-Chem managed to procure stock at lower prices (albeit still significantly above the historical prices) it began to introduce price decreases.[54]

73. Therefore, as explained below, no "material price increase" occurred in the period between the Regulations taking effect and the end of the Commission's complaint period.

Supply of masks (19 March to 31 March 2020)

74. In the second half of March, Dis-Chem continued in its global search for additional supply of masks. As is apparent from the numerous quotes obtained, the cost of new supply was going to be magnitudes larger than in previous months, and particularly when compared to the pre-pandemic period.[55]

75. It was also toward the end of March when the popularity of cloth masks as an alternative to surgical masks began to arise. In this regard it is worth recalling that a surgical mask is an item of personal protective equipment normally used in the administration of first aid and other

[54] Expert Witness Statement of Patrick Smith, Table 2, page 389 of the Pleadings Bundle.
[55] Expert Witness Statement of Patrick Smith, Table 4, page 392 of the Pleadings Bundle.

medical treatment. Despite its name, not all surgical masks are appropriate to be used during surgeries. Surgical masks are designed to be worn on a person's face, covering the nose and mouth in order to filter the air that is breathed in or out so as prevent the transmission of disease through airborne particles. As noted above, unlike the N95 mask, surgical masks, dust masks, cloth masks and other facial coverings are worn not to protect the wearer, but those with whom the wearer comes into contact, in case the wearer is infected.[56]

76. A very wide and ever-expanding range of cloth face masks became available to members of the public from this point. Such masks were available for purchase either ready-made from a wide range of retailers, alternatively, constructed at home using items likely to be available in all homes. The Internet, print media and television were (and remain) replete with instructions on how to make these masks at home. Similarly, commercial sellers of cloth masks have mushroomed across the country. These sellers range from large retailers expanding their product ranges to small businesses and even people who are simply making these masks for their immediate family and community. Cloth masks can be purchased in stores and online, with many sellers offering home delivery in a matter of days.[57]

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56 Dis-Chem's Answering Affidavit, paragraph 23, page 76 of the Pleadings Bundle.
57 Dis-Chem's Answering Affidavit, paragraph 25, page 77 of the Pleadings Bundle.

1 April to 23 April 2020

COVID-19 – Pandemic progression and impact in South Africa (1 April to 23 April 2020)

77. While the state of lockdown continued, Dis-Chem was able to keep trading by virtue of its status as an essential service provider (albeit that not all product lines were available for sale).[58]

78. On 10 April 2020, the DoH made its first recommendation in respect of the use of masks. In this regard, the DoH recommended that face masks be used in addition to hand-washing and social distancing. Importantly, the DoH stressed that "*the face mask should never be promoted as our primary prevention strategy and should never be promoted separately from hand-washing and social distancing*".[59]

79. On 14 April 2020, the Commission contacted Dis-Chem for the first time regarding its investigation around potential excessive pricing.[60] On 16 April, Dis-Chem, unrepresented by legal advisors at this point, responded to the Commission's request by providing a range of information and data.

58 Government Notice No 398 of Government Gazette No 43148, published on 15 March 2020.
59 Dis-Chem's Answering Affidavit, paragraph 21.6, page 73 of the Pleadings Bundle.
60 Competition Commission's Founding Affidavit, paragraph 25, page 15 of the Pleadings Bundle.

Demand for masks (1 April to 23 April 2020)

80. The demand for masks remained very high in April. Accordingly, at the beginning of April 2020 Dis-Chem limited sales to single units only. This decision, while helpful in ensuring equitable supply to all customers, along with Dis-Chem's various other measures to ensure supply to all customers, came at a substantial additional cost to Dis-Chem. In this regard, the breaking of bulk mask packages and re-packaging them as smaller pack sizes and single piece packs, along with the other measures introduced added substantial additional costs on a per unit basis. The most important of these are listed below:

80.1. First, substantial human resources were deployed in completing the manual process of repackaging masks from the larger 50 unit boxes into smaller, single unit packs.[61]

80.2. Second, Dis-Chem incurred expense in respect of the cost of the packaging materials for the re-packaged face masks.[62]

80.3. Third, additional sourcing and distribution costs were incurred as a result of the increased number of deliveries required. [63]

80.4. Finally, Dis-Chem was required to pay cash on delivery for the purchase of additional stock. Ordinarily Dis-Chem pays its suppliers on [redacted], so the requirement of cash on

61 Dis-Chem's Answering Affidavit, paragraph 45.1, page 84 of the Pleadings Bundle.
62 Dis-Chem's Answering Affidavit, para 45.2, page 84 of the Pleadings Bundle.
63 Dis-Chem's Answering Affidavit, para 45.3, page 84 of the Pleadings Bundle.

delivery had the potential to negatively impact Dis-Chem's cash flow.[64]

81. Notably, once Dis-Chem was able to secure additional supply, it was able to lift the restrictions on the sale of single masks and sales volumes increased rapidly.[65]

Retail pricing of masks (1 April to 23 April 2020)

82. Owing to the increased availability of supply and cheaper costs of purchase from mid-April 2020, Dis-Chem was able to start introducing multiple price decreases in April. In this regard, Dis-Chem decreased its price twice in April. The first decrease came on 11 April 2020 (R17.35 excl. VAT). The second decrease took effect on 22 April 2020 (R13.00 excl. VAT).[66]

83. Very significantly, the first of these price decreases took place before Dis-Chem was contacted by the Commission regarding its investigation. While the second decrease took place on the date of the complaint referral, the decision to drop the price would have been taken before the complaint was received.

84. In addition, notwithstanding that many of its current sales related to old stock, Dis-Chem always applied the new lower price to all sales,

64 Dis-Chem's Answering Affidavit, paragraph 45.4, page 84 of the Pleadings Bundle.
65 Expert Witness Statement of Patrick Smith, Figure 3, page 391 of the Pleadings Bundle; and Dis-Chem's Answering Affidavit paragraph 44, page 84 of the Pleadings Bundle.
66 Expert Witness Statement of Patrick Smith, Table 2, page 390 of the Pleadings Bundle.

regardless of the price at which the stock had been procured. In other words, Dis-Chem immediately passed on any savings to consumers.[67]

85. What this also demonstrates is that Dis-Chem sets its prices not with reference to the cost of *that* stock but rather the expected replacement cost of that stock. This is important because it means that the correct margin analysis involves comparing Dis-Chem's current prices to its expected replacement costs. The appropriate margin analysis does not compare the cost of current stock to the price of current stock.

86. As Dis-Chem is able to procure further stock at lower prices, it will continue to pass on these savings to customers.

Supply of masks (1 April to 23 April 2020)

87. It was in April 2020 that Dis-Chem was able to arrange its procurement channels such that it was finally able to source adequate supply to meet the increased demand. In this regard, Dis-Chem ordered approximately [redacted] masks from suppliers/traders. Although only [redacted] of these masks were delivered, Dis-Chem's available stock was significantly improved. Accordingly, Dis-Chem lifted the volume restrictions that it had put in place in respect of masks.[68]

88. Cloth masks continued to be widely available throughout April. In the context of the current pandemic, the purpose of a face mask, whether of

67 Dis-Chem's Answering Affidavit, paragraph 59, page 94 of the Pleadings Bundle.
68 Expert Witness Statement of Patrick Smith, Table 3 and Figure 3, page 391 of the Pleadings Bundle.

the cloth or surgical variety, is to assist in the prevention of the spread of the SARS-CoV-2 virus. On the demand side, members of the public looking to wear a face mask can choose between either a cloth mask or a surgical mask. Given the DoH's confirmation that it is satisfied that the scientific evidence shows that a cloth face mask significantly reduces the amount of virus that can be shed, there can be no concerns regarding the functional substitutability of the two mask varieties. It is therefore clear that cloth masks and surgical masks are substitutes for each other.[69]

89. From a supply side perspective, new avenues of supply of both types of masks are constantly opening up in response to the increased demand. As mentioned above, Dis-Chem has identified a wide range of new and alternative suppliers for surgical masks.

90. Similarly, numerous retailers and manufacturers are putting their otherwise idle or underutilised resources to work in the manufacture of cloth masks.

91. Moreover, many members of the public are making cloth masks, both for their own use and in many cases for sale to others. So easy are many of the methods to make an acceptable quality cloth mask that a sewing machine is not even required. The potential sources of supply for masks are therefore almost limitless. Accordingly, from a supply side

[69] Dis-Chem's Answering Affidavit paragraph 28, page 78 of the Pleadings Bundle.

perspective, it is clear that cloth and surgical masks are also substitutes for each other.[70]

92. Against this factual backdrop, we turn to consider the status and lawfulness of the Regulations and, specifically, the relationship between regulation 4 and section 8 so as to set out the approach that ought to be followed in determining this complaint referral.

[70] Dis-Chem's Answering Affidavit, paragraph 29, page 78 of the Pleadings Bundle.

LAWFULNESS OF THE REGULATIONS – *ULTRA VIRES* AND VOID FOR VAGUENESS

93. As set out above, on 19 March 2020, the Minister promulgated the Regulations.

94. First, if the Commission's contentions in its founding papers – that regulation 4 is the new test for excessive pricing and that the remainder of the requirements of section 8 are largely superfluous where regulation 4's elements are present -- is accepted by the Tribunal, the Regulations would have been made *ultra vires* the Minister's section 78 powers. The Minister cannot amend the Act, and section 8 specifically, through his promulgation of regulation 4. Were this contention to prevail, Dis-Chem would be forced to challenge the Regulations in the appropriate forum.

95. To avoid that step, and instead have this case determined by the Tribunal, and Competition Appeal Court if necessary, Dis-Chem proposes below a reading of regulation 4 so that it does not supplant section 8, but is grafted onto section 8(3) (despite its promulgation not complying with the requirements of section 78).

96. Second, it is a trite principle that *"laws must be written in a clear and accessible manner."*[71] The Constitutional Court has held that:[72]

> *"What is required is reasonable certainty and not perfect lucidity. The doctrine of vagueness does not require absolute certainty of laws.*

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71 ***Affordable Medicines Trust and Others v Minister of Health of RSA and Another 2005 (6) BCLR 529 (CC) [108]; Dawood and Another v Minister of Home Affairs and Others; Shalabi and Another v Minister of Home Affairs and Others; Thomas and Another v Minister of Home Affairs and Others*** 2000 (8) BCLR 837 (CC) [47]

72 ***Affordable Medicines Trust and Others v Minister of Health of RSA and Another*** 2005 (6) BCLR 529 (CC) [108] (internal footnotes omitted)

The law must indicate with reasonable certainty to those who are bound by it what is required of them so that they may regulate their conduct accordingly."

97. Where a regulation does not meet this standard, it may be declared *ultra vires* on the ground that it is void for vagueness or uncertainty. The unreasonableness emerges from the failure of the legislation to guide the public effectively; its failure to inform citizens of what they must and must not do.[73]

98. In determining whether a regulation is vague and uncertain, the court must first construe the regulation applying the normal rules of construction, including those required by constitutional adjudication. Then, once so construed, the ultimate question is whether the regulation indicates with reasonable certainty to those who are bound by it what is required of them.[74]

99. Regulation 4 of the Regulations provides:

*"**4. Excessive pricing***

4.1. In terms of section 8 (1) of the Competition Act a dominant firm may not charge an excessive price to the detriment of consumers or customers.

4.2. 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 mark-up for that good or service in the three month period prior to 1 March 2020,

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73 C, Hoexter, *Administrative Law in South Africa*, (2nd Edition) at page 332

74 ***Affordable Medicines Trust and Others v Minister of Health of RSA and Another*** 2005 (6) BCLR 529 (CC) [109]

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."*

100. Regulation 4.2 purports to create a rebuttable presumption. It states that a price will be *prima facie* excessive and unfair:

100.1. if there is *"a material price increase"* on a specified good or service during the specified period which,

100.2. either (i) does not correspond to or is not equivalent to the increase in the cost of providing that good or service,

100.3. or (ii) increases the net margin or mark-up on that good or service above the average margin or mark-up for that good or service in the three-month period prior to 1 March 2020.

101. On a plain construction of the language of regulation 4, the Commission must show that the price increase was "material". However, what is "material" is not defined in the Regulations. Assuming that the Minister intentionally did not define the term *"material"*, this requires the Tribunal to assess what is "material" on the facts of each case. As Solomon J said as long ago as 1929, "*I am not going to attempt a definition of the word "material," which the Act leaves undefined, presumably because the intention is that the Court must in each case decide whether on the facts an omission is or is not material*."[75]

[75] ***Van Zyl v Lloyd*** 1929 WLD 96 [101]

102. In *Sasol Chemical Industries*, the Competition Appeal Court found that:[76]

> *"In its decision, the Tribunal was cognisant of an observation of this Court in* Mittal *that a reasonable assessment involved a value judgment and that there was no single inflexibly clear threshold which could be applied to determine whether a price was excessive in each and every case*."

103. The Commission nevertheless seeks to establish a hard ceiling on price increases through the term "material". The Commission states in Mr Aproskie's affidavit that:[77]

> *"A further question is what threshold should be placed on an increase in price such that it passes the standard of creating an 'unreasonable difference' to the normal competitive price that prevailed historically or passes the materiality test in terms of the Regulations. Both precedent through other price gouging laws elsewhere and economic logic suggest a low threshold is appropriate, with a 10% threshold for a price increase deemed appropriate."*

104. The Commission effectively proposes that the Tribunal must read in a ceiling of 10% in regulation 4 as being the standard or threshold for materiality, even momentarily. This percentage is arbitrary and there is no legal basis for the Commission to contend that it is dispositive criterion.

105. If the Tribunal were to read in a threshold of 10% as the only standard for *"a material price increase"*, this would render the regulation void for vagueness and uncertainty. This is because a person is entitled to know before being prosecuted that there is, in fact, a hard 10% pricing ceiling, which is not apparent from the plain language of the regulation.

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76 ***Sasol Chemical Industries Ltd v Competition Commission*** [2015] 1 CPLR 58 (CAC) [163]

77 The Commission's Supporting Affidavit, paragraph 32, page 46 of the Pleadings Bundle.

106. Further, the Commission's appeal to *"precedent through other price gouging laws elsewhere"* is misplaced. Whilst the Tribunal may have regard to foreign law,[78] it is certainly not precedent which the Tribunal must slavishly follow.

107. In addition, Mr Aproskie's affidavit is replete with legal argument and submissions on the legal interpretation of the Regulations. The Competition Appeal Court has cautioned economic experts providing evidence on the legal interpretation of excessive pricing provisions, which the Commission ought to heed.[79]

108. Reading into the Regulations a hard ceiling of 10% that is not in regulation 4 would amount to the Tribunal making law and usurping the role of the other branches of government. This is a violation of the separation of powers, which recognises that:[80]

> *"policy-determination is the space exclusively occupied by the Executive. Meaning, the Judiciary may, as the ultimate guardian of our Constitution and in the exercise of its constitutional mandate of ensuring that other branches of government act within the bounds of the law, fulfil their constitutional obligations and account for their failure to do so, encroach on the policy-determination domain only when it is necessary and unavoidable to do so."*
>
> (underlining added)

109. The Tribunal must accordingly guard against encroaching on the domain of the other branches of government.[81] Thus, while the Commission may

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78 Section 1(3) of the Competition Act, No. 89 of 1998 (as amended).

79 ***Sasol Chemical Industries Ltd v Competition Commission*** [2015] 1 CPLR 58 (CAC) [178]-[182]

80 ***Electronic Media Network Ltd and others v e.tv (Pty) Ltd and Others*** 2017 (9) BCLR 1108 (CC) [2]

81 ***Electronic Media Network Ltd and others v e.tv (Pty) Ltd and Others*** 2017 (9) BCLR 1108 (CC) [1]-[5]

decide, as a matter of policy, not to refer complaints where the price increase is less than 10%, that does not mean that the Tribunal may read this into regulation 4 as a hard ceiling that if the price increase is more than 10% that there is a *prima facie* contravention of regulation 4.

110. Continuing with the construction of regulation 4.2, the Commission must show, in addition to showing that the price increase is "material", which it has not done, that either the price increase:

110.1. does not correspond to or is not equivalent to the increase in the cost of providing that good or service (regulation 4.2.1), or

110.2. increases the net margin or mark-up on that good or service above the average margin or mark-up for that good or service in the three-month period prior to 1 March 2020 (regulation 4.2.2).

111. Regulation 4.2.1 provides that the price increase must not correspond to or be equivalent to the increase in the cost of providing that good or service. There is no definition of *"costs"* and what costs ought to be taken into account when determining *"the cost of providing that good"*.

112. The Commission appears to have interpreted this provision to mean that it can simply compare the price that Dis-chem paid for the goods to the price at which Dis-chem sold the goods. However, this interpretation is overly simplistic and is based on price regulation (as opposed to market regulation) in circumstances where no price, profit or mark-up threshold has been specified.

113. In this regard, the Competition Appeal Court has cautioned that in excessive pricing cases:[82]

> *"some measure of latitude has to be given to firms with regard to pricing. If not, a court will become a price regulator; hence the importance of sustained expert evidence."*

114. In a disaster situation such as COVID-19, costs can become extremely uncertain for a firm. For example, in order for the firm to operate during the national state of disaster, it must put in place certain safety measures, including limiting the foot traffic into its store, cleaning the store with certain chemicals and increased frequency, providing personal protective equipment to all employees including face masks and protective screens. These measures increase the costs of being able to provide and sell goods.

115. In addition, due to the national shortage in the supply of goods, measures were taken to source goods globally and to do so on an urgent and costly basis. These are significant cost factors that must be taken into account when regulating markets. Unfortunately, regulation 4 is silent on which costs are relevant to an excessive pricing enquiry, and the Commission has not provided any, let alone a cogent, explanation in its founding papers for why the cost of a mask from a supplier is the only cost to be taken into account.

116. On the plain wording of regulation 4.2.1, the Commission's extremely narrow interpretation is unsustainable. The provision does not refer to

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82 ***Sasol Chemical Industries Ltd v Competition Commission*** [2015] 1 CPLR 58 (CAC) [184]

the *"cost of that good"*, rather, it refers to *"the cost of providing that good"*. The costs of *"providing"* that good is broader than simply the cost of the good, and must take into account the increased costs of operating the store, sourcing the goods etc.

117. Regulation 4.2.2 requires the Commission to compare the net margin or mark-up on the goods, to the average margin or mark-up for that good for the three-month period prior to 1 March 2020. The provision expressly refers to *"net margin"*, and Mr Aproskie's reliance on gross margin[83] is misplaced.

118. Having construed the ordinary grammatical meaning of the regulation, the next question is whether regulation 4.2 indicates with reasonable certainty to those bound by it, what is required of them.

119. In this regard, the need for the law to be accessible and precise in circumstances of price regulation is magnified in circumstances where firms do not have sufficient time to understand the impact of the regulation. "*A person should be able to conform his or her conduct to the law*",[84] however, without clear thresholds and specificity, it is not possible in these circumstances for a firm to determine which of its *"costs of providing that good"* can be factored into its price increases.

120. Importantly, if firms cannot determine with reasonable precision what prices they may charge for the specified goods, then the uncertainty is

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83 The Commission's Supporting Affidavit, paragraph 48.5, page 55 of the Pleadings Bundle.

84 ***President of the Republic of South Africa and Another v Hugo*** 1997 (6) BCLR 708 (CC) [102]

likely to result in firms not sourcing the goods globally thereby exacerbating the shortage of those goods (which are desperately needed) in the South African market.

121. The deterrent effect of penalising firms that increase their prices for goods or services, in circumstances where there is an absence of a clearly specified threshold of what constitutes *"material"* and a lack of clarity as to what *"costs"* may be factored into pricing, will disincentivise firms from globally sourcing products to meet South Africa's urgent need for the essential goods.

122. Regulation 4.2 does not create a bright line on price increases for firms. Rather, it requires firms and the Commission to take into account various pricing factors in order to give firms the flexibility required to respond to the volatility of the market. A firm's pricing has to be considered in the context where firms are doing their best to interpret and apply regulation 4, where markets are extremely volatile and unpredictable. Regulation 4 therefore builds in flexibility for firms, by looking only at a *"material price increase"* together with the *"costs in providing that good"* and increases in net margins and mark up's relative to the preceding three-month average margin or mark-up.

123. Thus, firms know with reasonable certainty when reading the regulation, that a price increase must correspond with the increase in the costs of providing that good or service, and must not exceed the average margin or mark-up for that good or service for the preceding three months. In

addition, firms know from reading regulation 4 that the price increase must be material, which suggests a price increase that is significant or substantial. This does not support the Commission's proposal of, what it acknowledges to be *"a low threshold"*[85], of 10%.

124. Indeed, what a person would not know by reading regulation 4 is that there is, for example, a 10% hard ceiling. The regulation is clearly not designed to create safe harbours, ceiling, thresholds, bright lines or tick boxes. If the Tribunal were to interpret regulation 4 in such a manner, it would render the regulation unlawful on the ground that it would be void for vagueness and uncertainty.

125. Accordingly, the vagueness in regulation 4 cannot be weaponised to prosecute Dis-Chem in the formulaic manner pursued by the Commission.

126. We next address the further flaw in the Commission's heavy reliance on regulation 4 in this complaint referral, namely that it cannot be retrospectively applied to Dis-Chem's conduct that occurred prior to its promulgation.

RETROSPECTIVE APPLICATION OF THE REGULATIONS

127. The Commission has referred a complaint against Dis-Chem:[86]

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85 The Commission's Supporting Affidavit, paragraph 32, page 46 of the Pleadings Bundle.

86 The Commission's Founding Affidavit, paragraphs 7, 53 and 55, page 8 and 25 of the Pleadings Bundle.

"in respect of Dis-Chem's alleged contravention of section 8(1)(a) of the [Competition] Act, read with Regulation 4 of the [Consumer Protection Regulations]…, during the period of March 2020 to date."

128. The order initially sought by the Commission includes a declaration that Dis-Chem's pricing conduct "*during the period March 2020 to date*" (for the relevant products) has contravened the provisions of section 8(1)(a) of the Act read with regulation 4 of the Regulations.

129. The Commission's attempt to apply the Regulations to conduct prior to 19 March 2020, which is when the regulations were promulgated,[87] is misplaced. There is no basis for the retrospective application of the Regulations:

129.1. there is a presumption against the retrospective application of legislation (which includes delegated legislation); and

129.2. the Regulations themselves do not provide for retrospective application.

Presumption against retrospectivity

130. There is a presumption against new legislation applying retrospectively. In ***S v Mhlungu & others***,[88] Kentridge AJ held:

"[65] First, <u>there is a strong presumption that new legislation is not intended to be retroactive</u>. By retroactive legislation is meant legislation which invalidates what was previously valid, or vice versa, i.e. which affects transactions completed before the new statute came into

87 On 19 March 2020, the Minister of Trade and Industry ("**Minister**") promulgated the Consumer and Customer Protection and National Disaster Management Regulations and Directions in Government Notice No. 350 of *Government Gazette* no. 43116 ("**Regulations**").

88 ***S v Mhlungu and others*** 1995 (3) SA 867 (CC) [65]-[67]

operation …. It is legislation which enacts that "as at a past date the law shall be taken to have been that which it was not". See Shewan Tomes & Co Ltd v Commissioner of Customs and Excise 1955 (4) SA 305 (A) at 311H, per Schreiner ACJ. There is also a presumption against reading legislation as being retrospective in the sense that, while it takes effect only from its date of commencement, it impairs existing rights and obligations, eg by invalidating current contracts or impairing existing property rights. See Cape Town Municipality v F Robb & Co Ltd 1966 (4) SA 345 (C) at 351, per Corbett J. The general rule therefore is that a statute is as far as possible to be construed as operating only on facts which come into existence after its passing."

131. Absent an express provision to the contrary, legislation should be construed as affecting only future conduct; and should be interpreted as far as possible so as not to take away rights actually vested at the time of their promulgation.[89]

132. Mokgoro J held in ***Veldman v Director of Public Prosecutions, Witwatersrand Local Division***,[90] that the principle that legislation will affect only future matters and not take away existing rights, is founded on the rule of law. In this regard, it also follows that if the court is left in doubt as to the retrospective effect of a provision, the presumption against retrospectivity would not be rebutted.

133. It is clear from the above case law that there is a strong presumption that the Regulations do not penalize conduct prior to the regulations coming into effect, unless the contrary appears from the legislation.

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89 ***Kaknis v Absa Bank Ltd, Kaknis v MAN Financial Services SA (Pty) Ltd*** [2017] 2 All SA 1 (SCA) [12]; ***Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service and Another*** 2017 (6) SA 435 (GP) [18] which refers to ***National Director of Public Prosecutions v Carolus and Others*** 2000 (1) SA 1127

90 ***Veldman v Director of Public Prosecutions, Witwatersrand Local Division*** 2007 (3) SA 210 (CC) [26]

The Regulations do not provide for retrospective application

134. It is a well-established principle of statutory construction that "*the legislature must be taken to be aware of the nature and state of the law existing at the time when legislation is passed.*"[91] Thus, it can be presumed that the Minister was aware of the law concerning excessive pricing prior to promulgating the Regulations.

135. In this context, the Regulations, and in particular regulation 4, were promulgated specifically to supplement the factors to be considered in a section 8(1)(a) excessive pricing case in order to address certain market conduct in light of the COVID-19 outbreak and the declared national disaster.[92] That is common cause.[93]

136. The Minister would have been aware of the presumption against the retrospective application of the Regulations. He thus sought to clarify their application in regulation 2, which states:

> *"2.1. These regulations and directions apply to the supply of goods and services contemplated and listed in Annexures A and B during the period of the national disaster.*
>
> *2.2. These regulations and directions come into effect on the date of their publication in the* Government Gazette*.*
>
> *2.3. These regulations and directions will be of no force of (sic) effect when the COVID-19 outbreak is no longer declared a disaster."*

137. Regrettably, the retrospective application of the Regulations is unclear from regulation 2, and there is some ambiguity as to whether these

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91 ***Boost Sports Africa (Pty) Ltd v South African Breweries (Pty) Ltd*** [2015] ZASCA 93; 2015 (5) SA 38 (SCA) [13]

92 Regulation 2 of the Regulations.

93 The Commissions Founding Affidavit, paragraph 15, page 11 of the Pleadings Bundle.

regulations could apply from 15 March 2020 (when the national disaster was declared) or from 19 March 2020 (when the regulations were published).

138. Regulation 2.1 states that the Regulations *"apply…during the period of the national disaster" "relating to the COVID-19 outbreak declared in Government Notice No. 313 of Government Gazette No. 43096 on 15 March 2020"*.[94] Although the wording of regulation 2.1 appears to suggest that the regulations apply from 15 March 2020, it does not expressly state that the Regulations apply retrospectively.

139. However, regulation 2.2 clearly states that the Regulations *"come into effect on the date of their publication"*, which was 19 March 2020. This provision is unequivocal and contrary to the implied retrospective application in regulation 2.1.

140. Regulation 2.3 unequivocally states that the Regulations *"will be of no force [or] effect when the COVID-19 outbreak is no longer declared a disaster"*.

141. Thus, it is unequivocally clear that the Regulations come into effect on the date of their publication and cease to be of force and effect when the national disaster ends. What is unclear, is whether the Regulations apply to the period between 15 March and 19 March 2020.

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[94] Regulation 2.1 in the Regulations, read with the definition of *"national disaster"* in regulation 1.4 thereof.

142. In *Novartis*,[95] the Competition Appeal Court held that "*[t]o the extent that there is any ambiguity in the legislation, [the relevant provision] must be interpreted to be congruent with the fundamental principles outlined by Kentridge AJ in Mhlungu supra*", namely that there is a strong presumption that the new law is not intended to be retroactive.

143. The basis of the presumption against retrospectivity is *"the elementary consideration of fairness which dictates that individuals should have an opportunity to know what the law is and to conform their conduct accordingly."*[96]

144. In ***Kaknis v ABSA***[97], the SCA held:

> *"[14] It has been held that the crux of the matter is not the prospectivity or retrospectivity of legislation as such, but the fair treatment befalling those subject to the legislation should the legislation be held to apply in that manner. Nevertheless, where the statutory provision confirms the existing law, it is not a case of true retrospectivity, since true retrospectivity means that at a past date, the law shall be taken to have been that which it is not. Thus, if the legal position is A, and enactment X is designed merely to confirm A, then it cannot be said that, subsequent to the promulgation of X, the legal position has become A. Accordingly, true retrospectivity can only become an issue once X replaces, amends of supplements A. (See du Plessis above at 183. See also Unitrans Passengers (Pty) Ltd t/a Greyhound Coach Lines v Chairman, National Transport Commission & others: Transnet Ltd (Autonet Division) v Chairman, National Transport Commission & others 1999 (4) SA 1 (SCA) para 13 and Manyeka v Marine and Trade Insurance Co Ltd 1979 (1) SA 844 (SE) 847H-848A. See also Nkabinde & another v Judicial Service Commission & others [2016] ZASCA 12; 2016 (4) SA 1 (SCA paras 59-84)."*

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95 ***Novartis SA (Pty) Ltd v New United Pharmaceutical Distributors (Pty) Ltd*** (1) [2001-2002] CPLR 74 (CAC) [81]

96 ***Pienaar Brothers (Pty) Ltd v Commissioner for the South African Revenue Service and Another*** 2017 (6) SA 435 (GP) [18]

97 ***Kaknis v Absa Bank Limited; Kaknis v Man Financial Services SA (Pty) Ltd*** (08/16) [2016] ZASCA 206; [2017] 2 All SA 1 (SCA); 2017 (4) SA 17 (SCA).

145. In considering the fair treatment of those subject to the Regulations, we highlight that the Minister did not publish draft regulations for public comment, as he is required to do in terms of section 78 of the Act. Thus, there was no time prior to the promulgation of the Regulations for firms to adjust their conduct as required by regulation 4. Firms were responding to volatile market fluctuations, unprecedented demand and a global shortage of supply. The law should not punish firms retrospectively, when there was no opportunity for firms to adjust their conduct to conform with the Regulations prior to their promulgation.

146. We therefore submit that the Regulations are only applicable to conduct from 19 March 2020.

147. However, even if the Tribunal finds that the Regulations do apply retrospectively, then they can only possibly apply to conduct after 15 March 2020, four days earlier. On either interpretation, the Commission's contention that the Regulations apply for the whole of March 2020 is unsustainable.

What conduct is regulated by the Regulations?

148. Since the Regulations cannot apply retrospectively, it cannot apply to price increases that were effected prior to the regulations coming into effect on 19 March 2020. This is in line with the purpose of the Regulations, which provides:[98]

[98] Regulation 3 of the Regulations.

"The purpose of these regulations is to-

3.1 promote concerted conduct to prevent an escalation of the national disaster and to alleviate, contain and minimise the effects of the national disaster; and

3.2 protect consumers and customers from unconscionable, unfair, unreasonable, unjust or improper commercial practices during the national disaster." (underlining added)

149. It is clear that the Regulations were enacted to address *"the national disaster"*, which is defined as meaning *"the national disaster relating to the COVID-19 outbreak declared in Government Notice No. 313 of Government Gazette no. 4309 on 15 March 2020"*. It therefore does not address conduct which falls outside of the period of the national disaster.

150. As a result, given that the price increases implemented by Dis-Chem pre-date the Regulations, its conduct cannot be condemned in terms of that regulation.[99]

151. Section 8(1)(a) of the Act is concerned with dominant firms charging an excessive price. If the firm is charging a price that meets the test of *"excessive"*, then for the period that the price is charged, the firm will fall foul of the prohibition.[100] The conduct that is therefore prohibited is ongoing conduct. In practical terms, what this means is that a firm may contravene section 8(1)(a) without *increasing* its prices; what is required is the *charging* of an excessive price, irrespective of whether the excessive price is as a result of an increase or not. In short, excessive

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99 The Commission accepts at paragraph 27.6 and 27.7 of its Replying Affidavit that the price increases "that have underpinned the Commission's findings had already occurred by 9 March 2020." See pages 435 and 436 of the Pleadings Bundle.

100 Assuming the excessive price operated "*to the detriment of consumers*".

pricing is not concerned with *price increases*, it is concerned with *charging an excessive price*.

152. By contrast, regulation 4.2 supplements the conduct that constitutes an excessive price under section 8(1)(a) of the Act, by regulating *"price increase[s]"*. Regulation 4.2 creates a presumption that a price is *prima facie* excessive where *"a material price increase"* satisfies the criteria in regulations 4.2.1 and 4.2.2. *"Price increase"* is defined in regulation 1.5 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 raising or reducing grade levels of goods and services".*

153. In contrast to the ongoing pricing conduct prohibited in section 8, regulation 4 does not prohibit the mere charging of a price. Rather, it prohibits a *"price increase"*. The "*price increase*" is a jurisdictional fact triggering regulation 4. Thus, if there is no price increase during the relevant complaint period, regulation 4 is not triggered.

154. The decision to regulate a "*price increase*" as opposed to "*pricing*" was both deliberate and significant. Regulation 4.1 uses the phrase "*charge an excessive price*" whereas regulation 4.2 uses different language. If regulation 4.2 was aimed at the same conduct as regulation 4.1, the same language would have been used. In the construction of statutes a

deliberate change of expression is *prima facie* taken to import a change of intention".[101]

155. There is a presumption in our law that when interpreting legislation, different words should be given a different meaning.

156. If the Commission treats the regulations as capturing "*charging of an excessive price*" instead of "*a material price increase*", very significant complexities arise. The ongoing conduct of charging a price raises numerous difficulties regarding the duration of the offence, compared with a case based on conduct limited to a "*price increase*". The complexities in running an excessive pricing case in respect of conduct that took place for only a very short period is exposed in this case:

156.1. In the Commission's notice of motion and founding affidavit,[102] the Commission's alleged complaint period was "*during March 2020 to date*". But excessive pricing legislation is ill-suited to assessing competitive conduct over such a short period as it may give rise to false positives. Recognising the difficulties in running such a case, the Commission re-focuses its case in reply to limit the complaint period to 31 March 2020 and effectively abandons the conduct during April.[103]

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101 *Port Elizabeth Municipal Council* v Port Elizabeth Electric Tramway *Co Ltd* 1947 (2) SA 1269 (A) at 1279.

102 Notice of motion prayer 3; Commission's founding affidavit, para 7

103 See para 27.3 of the Commission's replying affidavit, where it concedes that Dis-Chem's pricing reduced in early April 2020

156.2. The time period that the Commission has focused on is arbitrary, and has led to difficulties in (i) defining the relevant market, (ii) determining dominance, (iii) assessing whether price decreases can be taken into account, and (iv) which costs and pricing data are relevant to the assessments mandated under section 8.

156.3. In contrast, regulation 4.2 specifically narrows the scope of charging an excessive price to "*a material price increase*", which is narrower and locates the impugned conduct and the section 8 assessment to a particular time more.

156.4. If a firm were able to materially increase its price and its volumes, even for a day, then the market would be more readily ascertainable, and the duration of the contravention and thus cost and pricing data relevant to assessing the contravention would be clearer.

156.5. However, absent "a material price increase", the point from when the section 8 assessment is conducted becomes arbitrary. It is the increase and decrease of the price that signal the period of assessment, thereby narrowing the scope of a section 8 analysis.

157. Since the Regulations cannot apply retrospectively, it cannot apply to price increases that were effected prior to the regulations coming into

effect on 19 March 2020. This is in line with the purpose of the Regulations, which provides:[104]

"The purpose of these regulations is to-

3.1 promote concerted conduct to prevent an escalation of the national disaster and to alleviate, contain and minimise the effects of the national disaster; and

3.2 protect consumers and customers from unconscionable, unfair, unreasonable, unjust or improper commercial practices during the national disaster." (underlining added)

158. It is clear that the Regulations were enacted to address *"the national disaster"*, which is defined as meaning *"the national disaster relating to the COVID-19 outbreak declared in Government Notice No. 313 of Government Gazette no. 4309 on 15 March 2020"*. It therefore does not address conduct that falls outside of the period of the national disaster.

159. As a result, given that the price increases implemented by Dis-Chem pre-date the Regulations and there is no increase during the complaint period (as narrowed by the Commission in reply), its conduct cannot be condemned in terms of that regulation.[105]

160. Regulation 4 is therefore not applicable in this case and that leaves the Commission's case being an ordinary section 8 case. In other words, it is not to say that the Commission is not able to pursue cases of price increases and/or excessive pricing that occurred prior to the promulgation of Regulation 4. However, should it do so, then it is

104 Regulation 3 of the Regulations

105 The Commission accepts at para 27.6 and 27.7 of its replying affidavit that the price increases "that have underpinned the Commission's findings had already occurred by 9 March 2020"

squarely within a section 8 complaint and cannot rely on regulation 4 to supplement its complaint.

161. Despite that, we assume for purposes of the section below that the Tribunal somehow finds that Regulation 4 applies despite Dis-Chem never having effected a price increase while the Regulations were in force.

THE APPLICABLE TEST FOR EXCESSIVE PRICING

Introduction

162. The Commission alleges that Dis-Chem is guilty of "price gouging". There is, however, no law in South Africa that specifically deals with "price gouging". And so the Commission has had to contort the excessive pricing provisions under section 8 of the Act to bring a "price gouging" case.

163. It is necessary to preface these heads of argument with the following comment: The Commission's founding papers[106] are brimming with emotive language about the ills of price gouging and the horrors of COVID-19.[107] Dis-Chem agrees with all of that but points out that the existence of a disaster does not alter the fact that until the Commission has made out a case, Dis-Chem – like any other litigant in our Constitutional democracy – is presumed innocent. In these heads of

106 Comprising the Commission's Notice of Motion, the Commission's Founding Affidavit and the Commission's Supporting Affidavit.

107 The Commission's strategy seems to be that if it creates enough hostile sentiment against Dis-Chem, the Tribunal will adopt the Commission's novel test for excessive pricing and ignore the facts of the case or the provisions of the law.

argument, therefore, we have elected to adopt more appropriate language, language rooted in the express provisions of the applicable legislation and regulations, and grounded in authority. We do so because despite COVID-19, the only relevant question remains whether Dis-Chem has contravened section 8(1)(a) of the Act.

Material disputes of fact

164. The Commission seeks final relief[108] and has asked the Tribunal to decide this case on the papers,[109] i.e. without hearing oral evidence. Being an application for final relief, the *Plascon-Evans* test applies in respect of factual disputes, namely that the application must be determined based on Dis-Chem's factual averments.[110] Harms JA explained the effect of *Plascon-Evans* as follows in ***NDPP v Zuma***:[111]

> *"Motion proceedings, unless concerned with interim relief, are all about the resolution of legal issues based on common cause facts. Unless the circumstances are special, they cannot be used to resolve factual issues because they are not designed to determine probabilities. It is well established under the Plascon-Evans rule that where in motion proceedings disputes of fact arise on the affidavits, a final order can be granted only if the facts averred in the applicant's affidavits, which had been admitted by the respondent, together with the facts alleged by the latter, justify such order. It may be different if the respondent's version consists of bald or un-creditworthy denials, raises fictitious disputes of fact, is palpably implausible, farfetched or so clearly untenable that the court is justified in rejecting them merely on the papers.*"

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108 The Commission seeks declaratory relief (prayer 3), interdictory relief (prayer 4) and the payment of an (grossly exorbitant) administrative penalty (prayer 5). See page 3 of the Pleadings Bundle.

109 The Commission's Notice of Motion, prayer 2.4, page 3 of the Pleadings Bundle.

110 ***Plascon-Evans Paints Limited v Van Riebeek Paints (Pty) Limited*** 1984 (3) SA 623 (A) [634E–635C].

111 National Director of Public Prosecutions v J G Zuma 2009 (2) SA 277 (SCA) [26].

165. This approach was squarely endorsed by the Competition Appeal Court (CAC) in *Dawn*:[112]

> *"Where a case is argued before the Tribunal solely with reference to the affidavits (other than a case for interim relief), the Tribunal should apply the same test as civil courts when final relief is sought on motion, namely that the respondent's version is to be accepted unless a purported dispute of fact is not real or genuine or bona fide or unless the respondent's version is so far-fetched or clearly untenable that the court is justified in rejecting it on the papers.*"

166. Therefore, if the Tribunal finds that it cannot reject Dis-Chem's version on the papers, the Commission cannot succeed. The only basis upon which the Tribunal could do so is if Dis-Chem's version is far-fetched or untenable, or that the factual disputes are not genuine or not *bona fide.*

167. The Commission has put up no facts that contradict those put up by Dis-Chem.

168. Accordingly, Dis-Chem's factual evidence must prevail and be accepted by the Tribunal. That evidence has not been contradicted, and it cannot establish a contravention of section 8 of the Act because it does not establish any of the elements required to prove a contravention of that section.

Market definition and dominance

169. The obligations in section 8 only apply to dominant firms. Stated differently, dominance is a jurisdictional requirement of any section 8

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112 ***Dawn Consolidated Holdings (Pty) Ltd and others v Competition Commission*** (Case no. 155/CAC/OCT2017) [16].

case. The Regulations are silent on dominance and so do not alter that position.[113] Therefore, if the Commission fails to discharge its onus under section 7, the complaint referral must be dismissed.

170. Dominance is determined by defining the relevant market, and then asking whether the firm in question has sufficient market shares or "*market power"* within the market so defined. The position is explained in *A Practical Guide to the South African Competition Act* thus:

> *"… the definition of the relevant market is an important initial step in establishing whether or not a particular firm qualifies as dominant or not…"*[114]

171. The importance of the market definition exercise cannot be overstated. In his most recent work, Professor Whish*[115]* explains the importance thus:

> *"If the notion of 'power over the market' is key to analysing many competition issues, it becomes immediately obvious that it is necessary to understand what is meant by 'the market' or … the 'relevant market'…*[116]
>
> *First, market definition is an analytical tool that assists in determining the competitive constraints upon undertakings: market definition provides a framework within which to assess the critical question of whether a firm or firms possess market power. Secondly, both the product and geographic dimensions of the market must be analysed…"*[117]

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113 The Commission accepts this at paragraph 32.1 of its Founding Affidavit, page 19 of the Pleadings Bundle.

114 M, Neuhoff et al, A Practical Guide to the South African Competition 2nd edition, Lexis Nexis, at page 140.

115 R. Whish, *Competition Law*, Oxford University Press (9th edition 2018).

116 R. Whish, *Competition Law* at page 26.

117 R. Whish, *Competition Law* at page 27.

172. The European Commission's ("**EC**") *Notice on the definition of the relevant market for the purposes of Competition Law*[118] provides that:

> *"Market definition is a tool to identify and define the boundaries of competition between firms. It serves to establish the framework within which competition policy is applied by the Commission. The main purpose of market definition is to identify in a systematic way the competitive constraints that the undertakings involved face. The objective of defining a market in both its product and geographic dimension is to identify those actual competitors of the undertakings involved that are capable of constraining those undertakings' behaviour and of preventing them from behaving independently of effective competitive pressure."*[119]

173. The EC Notice explains that *"[t]he definition of the relevant market in both its product and its geographic dimensions often has a decisive influence on the assessment of a competition case*."[120]

174. What is clear is that the complainant (in this case the Commission), irrespective of whether it relies on market shares or market power must define the relevant market. The Commission's case on dominance appears at paragraphs 35 – 41 of its complaint referral affidavit and can be summarised as follows:

174.1. The Commission's case is not one of market shares, it is one of market power,[121] i.e. "*the ability of a firm to control prices or to*

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118 Available at https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A31997Y1209%2801%29.

119 The EC's Notice on the definition of the relevant market for the purposes of Competition Law at paragraph 2.

120 The EC's Notice on the definition of the relevant market for the purposes of Competition Law at paragraph 4.

121 The Commission's Founding Affidavit, paragraph 38, page 20 of the Pleadings Bundle. The Commission's reference to section 7(3) seems to be a mistake and ought to have been a reference to section 7(c).

exclude competition, or to behave to an appreciable extent independently of its customers, competitors or suppliers."[122]

174.2. "*The WHO's declaration of a PHEIC[123]… coupled with increased international demand for face masks, and the panic buying by consumers … have provided conditions for Dis-Chem to hold temporary market power that it may not hold otherwise."*[124]

174.3. "*Dis-Chem is a dominant firm… [as] is evident from its ability to engage in price gouging when it independently increased the mark-up earned on surgical face masks blue 50pc, surgical face masks 5pc and surgical face masks foliodress blue from March 2020 to date, while still growing volumes."*[125]

175. Those paragraphs must be read with Aproskie's submissions on dominance and market definition which are that: "*in the context of an abuse case, market definition is primarily undertaken in order to determine the firm's market share and whether that share exceeds the thresholds for a presumption of market power.*"

176. Reduced to its essence then, the Commission's position in respect of dominance is that Dis-Chem has "*temporary market power*" because it increased prices while growing sales volumes.

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122 The Commission's Founding Affidavit, paragraph 40, page 21 of the Pleadings Bundle; and the definition of *market power* in section 1(1) of the Competition Act, No. 89 of 1998 (as amended).
123 Public Health Emergency of International Concern.
124 The Commission's Founding Affidavit, paragraph 39, page 21 of the Pleadings Bundle.
125 The Commission's Founding Affidavit, paragraph 41, page 21 of the Pleadings Bundle.

177. There are material flaws in treating an increase in sales volumes coupled with an increase in market shares as evidence of acting to an appreciable extent independently of customers, competitors or suppliers.

178. The Commission is guilty of precisely what Bishop and Walker warn against when they say:

> *"It would therefore appear intuitive that the level of profits that a firm is earning could be used as a proxy for the degree of competition in the market in which it operates. … we argue that this apparently simple and obvious relationship holds only rarely and should not be used generally as the basis for assessing the competitiveness of particular markets or industries."*[126]

179. The Commission says almost nothing about why it has chosen the relevant markets for which it contends. The Commission seems to justify the absence of a proper market definition exercise on the basis that its case does not rely on market shares, and there is therefore no role to be played by market definition. That is fundamentally flawed, both as a matter of law and economics.

180. Another important consequence of the Commission's case being one of market power (instead of market shares), is that the onus in respect of dominance remains on the Commission throughout.[127]

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126 Simon Bishop & Mike Walker, *The Economic of EC Competition Law: Concepts Application and Measurement*, (2nd edition Thomson Sweet & Maxwell 2002), paragraph 3.58, page 74-75.

127 There is not shift in the onus in respect of market power as there is under s7(b) in terms of which, once the Commission has established that the firm has a market share of at least 35%, in order to challenge dominance, the firm must prove that it lacks market power.

181. The Commission is correct that market power[128] can be inferred from a firm's economic behaviour.[129] But what the Commission fails to appreciate is that economic conduct does not occur in a vacuum, it occurs in a relevant market and so to be properly analysed requires that a market be defined.

182. The *locus classicus* for the proposition that *market power* can be inferred from conduct[130] is the case of *South African Airways.*[131] Importantly, in that case, the Commission *had* properly pleaded and proven the relevant market(s),[132] thereby placing the Tribunal in a position to reliably determine whether *South African Airways* was indeed capable of exerting *market power* within the market so defined. In that case, and notwithstanding having accepted that market power can be inferred from conduct, the Tribunal nevertheless acknowledged that:

> *"As this case concerns an alleged abuse of dominance, it is trite law that the Commission needs to establish that SAA is dominant in respect of some market."*[133] (Emphasis added.)

183. That market definition is an unavoidable step in the analysis flows naturally from the definition of *market power* which is "*the ability of a firm to control prices or to exclude competition, or to behave to an appreciable extent independently of its customers, competitors or*

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128 Or, more correctly, dominance.
129 The Commission's Supporting Affidavit, paragraph 15, page 38 of the Pleadings Bundle.
130 As opposed to inferred/presumed from market shares.
131 Competition Commission / South African Airways (Pty) Ltd, Case 18/CR/Mar01 [2005] ZACT 50 (28 July 2005).
132 The first market being "the market for the purchase of domestic airline ticket sales services from travel agents in South Africa" (see para 44) and the second "the market for scheduled domestic airline travel…" (see para 53).
133 ***Competition Commission / South African Airways (Pty) Ltd***, Case 18/CR/Mar01 [2005] ZACT 50 (28 July 2005) [33].

suppliers."[134] For example: How could one determine whether a respondent has the ability to behave independently of its competitors when one can't identify those competitors because one doesn't even know what market(s) the respondent operates in?

184. The Commission's "temporary market power" approach is also flawed because it is silent about what the competitive price is. As explained in *A practical Guide to the South African Competition Act:*

> *"Simply put, market power provides the firm with the ability to set prices above the competitive price level…"*[135]

185. But the Commission has not even suggested what it considers the competitive price level to be. We deal more fully with this point below.

186. Not only is a proper market definition exercise necessary in *every* abuse case, it attracts heightened significance when the Commission posits a geographic market that is "*in stark contrast to … case precedent on the geographic markets for grocery retailers …*"[136] The Commission thus advances a geographic market definition that, on its own version, constitutes a drastic departure from established precedent but it declines to carry out the standard hypothetical monopolist test which has been

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134 The Commission's Founding Affidavit, paragraph 40, page 21 of the Pleadings Bundle; and the definition of *market power* in section 1(1) of the Competition Act.

135 Neuhoff et al, A Practical Guide to the South African Competition Act (2nd edition, Lexis Nexis), page 141.

136 The Commission's Supporting Affidavit, paragraph 25, page 42 of the Pleadings Bundle.

accepted as the correct approach to market definition, both in all established jurisdictions abroad,[137] and our own.[138]

187. Furthermore, section 8(3)(e) provides that one of the factors for consideration is "*the extent of the respondent's market share*".

188. By declining to meaningfully define the market, the Commission avoids the *SSNIP*[139] test and that has very significant implications for this case.

189. *First*, had the Commission carried out the hypothetical monopolist/SSNIP test, it would have been confronted by the reality that however one defines the relevant market, it is characterised by very low barriers to entry and demonstrated new entry/expansion. Those facts are fundamentally at odds with the existence of market power.

190. *Second*, the 'N' in *SSNIP* stands for 'non-transitory' and the phrase plays an important role. As explained in Economics for Competition Lawyers:[140]

> *"The main rationale for considering a 'non-transitory' as opposed to a transitory price increase is that competition authorities are not normally concerned with transitory market power… if it suddenly starts to rain in a busy market place, vendors who sell umbrellas find themselves controlling a scarce good that is in strong demand… The same is true for car hire and taxi companies when the European airspace is closed due to volcanic ash, and stranded passengers across Europe desperately try to get home. Such a position of market power will not last, and does not usually merit a separate market definition by time of*

137 Simon Bishop & Mike Walker The Economics of EC Competition Law: Concepts, Application and Measurement (2002) 85, 88, 128–130.

138 ***South African Raisins (Pty) Ltd v SAD Holdings Ltd 04/IR/Oct/1999 5; Patensie Sitrus Beherend Beperk v Competition Commission*** 16/CAC/Apr02 [16] – [17].

139 Small but Significant Non-transitory Increase In price.

140 Niels G, Jenkins H and Kavanagh J, *Economics for Competition Lawyers* Oxford University Press, (1st Edition 2011).

consumption… Only market power that persists over time is of concern. The small but significant increase in price must therefore be 'non-transitory'."[141]

(emphasis added)

191. We also point out that the 'non-transitory' concept (or an equivalent concept with a different name) finds application in the USA,[142] Canada[143]and the European Union.[144] The Office of Fair Trading treats market power as '*the ability to raise prices consistently and profitably over competitive levels*'.

192. That is also the economic test recognised by the CAC in *Sasol Chemical Industries*[145] and which is binding on the Tribunal.

193. As Bishop and Walker point out, "*Any firm can choose to raise price at any time, but this does not mean that every firm has market power".*[146]

194. In conclusion then, the Commission has elected to rely on market conduct (as opposed to market shares) as a proxy for dominance. One simply cannot test for market power in a vacuum as the Commission does in its founding papers. By failing to define a market, the

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141 Niels G, Jenkins H and Kavanagh J, *Economics for Competition Lawyers* Oxford University Press, (1st Edition 2011), page 45.

142 The Federal Trade Commission's Horizontal Merger Guidelines speak of "*lasting for the foreseeable future*"; (available at https://www.justice.gov/atr/horizontal-merger-guidelines-0)

143 The Competition Bureau (2004), *'Merger Enforcement Guidelines'*, September [3.4] define non-transitory as one year.

144 The EC's Notice on the definition of the relevant market for the purposes of Competition Law refers at paragraph 17 to a "permanent" increase in price.

145 ***Sasol Chemical Industries Limited v Competition Commission***, Case No 131/CAC/Jun14, judgment of 17 June 2015 [2].

146 S. Bishop & M. Walker, *The Economic of EC Competition Law: Concepts Application and Measurement*, 2nd ed, Thomson Sweet & Maxwell 2002, paragraph 3.01, page p 42.

Commission does away with the 'non-transitory' element of the SSNIP test, thereby nullifying the policy considerations that underpin it.

195. In the circumstances, the Commission has failed to properly define the market and has failed to establish dominance. Section 8 cannot apply without establishing dominance and therefore the complaint referral should be dismissed.

THE LEGISLATIVE SCHEME: HOW THE REGULATIONS FIT INTO AN EXCESSIVE PRICING ANALYSIS[147]

196. In determining whether Dis-Chem is guilty of a contravention, the departure point is, of course, the legislation. Apart from dominance which is dealt with above, the relevant provisions under the Act are sections 8(1)(a), 8(2) and 8(3). They provide as follows:

> *"8(1)(a) – it is prohibited for a dominant firm to 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;*

147 For purposes of this section, we assume (but do not concede) that the Regulations are valid and binding upon Dis-Chem.

(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."

197. For purposes of this case, those section 8 provisions must be read with the Regulations. The relevant regulation for purposes of this case is regulation 4 which provides as follows:

"4.1 In terms of section 8(1) of the Competition Act a dominant firm may not charge an excessive price to the detriment of consumers or customers.

4.2 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 mark-up 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."

198. And finally, Annexure A includes medical and hygiene supplies, which include surgical masks.

199. The legislative framework[148] therefore lays down the following approach (for onus purposes, it is important that the analysis be carried out in the order set out below):

199.1. *First*, one asks whether the respondent is dominant. If not, that is the end of the case. If dominance is proven, section 8 applies and one proceeds to step two.

199.2. *Second,* any person determining whether a price is excessive, must determine if the difference between that price and the competitive price is unreasonable.[149] The competitive price and the reasonableness of the difference must be determined by having regard to <u>all relevant factors,</u> which may include those set out in section 8(3)(a) – (f). The Regulations have as their source section 8(3)(f) and so the effect of the Regulations is to add two further factors to the list set out in sections 8(3)(a) – (e). Those additional factors are (i) a price-cost analysis,[150] and (ii) a margin analysis with regard being had to the respondent's historical margins.[151]

199.3. *Third,* and only if the Commission, having taken account of all relevant factors, has made out a *prima facie* case,[152] then the

148 Comprising sections 8(1), (2) and (3) of the the Competition Act along with regulation 4 of the Regulations.
149 That much is plain from section 8(3) of the the Competition Act.
150 Regulation 4.2.1 of the Regulations.
151 Regulation 4.2.2 of the Regulations.
152 That being the exercise in terms of section 8(3) of the Competition Act discussed above.

respondent, Dis-Chem, attracts an onus to show that the price was reasonable.[153]

199.4. *Fourth*, one asks whether a price that is excessive operates to the detriment of customers/consumers.[154]

200. In stark contrast, the Commission posits a fundamentally different approach. In developing what *it* considers the appropriate test to be, the Commission's departure point is that "*the practice of price gouging is a relatively specific practice … and therefore requires a relatively simple test in order to detect excessive pricing.*"[155] That of course ignores the fact that price gouging is, on the Commission's version, a species of excessive pricing. Excessive pricing cases are anything but simple, as expressly recognised by the CAC in *Mittal*,[156] where it referred approvingly to *Napp Pharmaceuticals*[157] as follows:

> *"Measuring whether a price is above the level that would exist in a competitive market is rarely an easy task. The fact that the exercise may be difficult is not, however, a reason for not attempting it."*

201. David Lewis remarks in *Thieves at the Dinner Table* that excessive pricing in competition law is fraught with complexity and controversy. His remarks were referred to approvingly by the CAC in *Sasol Chemical Industries*.[158]

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153 Section 8(2) of the Competition Act.
154 Section 8(1) of the Competition Act.
155 The Commission's Supporting Affidavit, paragraph 27, page 43 of the Pleadings Bundle.
156 ***Mittal Steel South Africa Limited and Others v Harmony Gold Mining Company Ltd***, Case No 70/CAC/Apr07, judgment of 29 May 2009, [48].
157 ***Napp Pharmaceuticals Holdings Ltd & Others v General of Fair Trading*** [2002] CAT 1 [392].
158 ***Sasol Chemical Industries Ltd v Competition Commission*** [2015] 1 CPLR 58 (CAC) [2].

202. Stated differently, the fact that determining a competitive price is difficult is simply no basis for the Commission to decline to conduct the exercise. The Act prescribes the exercise and so the Commission must oblige. From that flawed assumption, the Commission proceeds to lay down the test it believes applies as follows:

> *"The test 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."*[159]

203. It restates its preferred test thus: "*The test is whether there has been a material price increase in an essential good or service (as listed in Annexure A)…"*[160] And the same overly simplistic test appears in the complaint referral affidavit at para 45.1.

204. The Commission's position, therefore, seems to be that the effect of the Regulations is to introduce into the excessive pricing analysis two factors, either of which is determinative of whether a *prima facie* case of excessive pricing has been made out. We deny that such an interpretation is the correct one and if the Tribunal interprets the Regulations in the manner contended for by the Commission, Dis-Chem reserves its right to challenge the Regulations as being *ultra vires*.

205. The only lawful reading is that the Regulations merely introduce two further factors to the section 8(3) analysis and that the onus referred to in section 8(2) only shifts onto the respondent if the Commission has

159 The Commission's Supporting Affidavit, paragraph 27, page 43 of the Pleadings Bundle.
160 The Commission's Supporting Affidavit, paragraph 29, page 45 of the Pleadings Bundle.

made out a *prima facie* case having regard to **all relevant factors**, not just the factors listed in regulation 4.2.1 or 4.2.2.

206. It is not clear whether the Commission's position is that the competitive price is irrelevant or whether it accepts that the competitive price is relevant but treats Dis-Chem's prices in the lead up to the complaint period as a proxy for the competitive price. Irrespective of which of those arguments the Commission ultimately advances, its approach is deeply flawed.

207. If the Commission contends that the Regulations create a novel approach in terms of which the competitive price plays no role, that is incorrect on a number of bases. Section 8(3) contains a number of clear textual indicators that the legislature intended the competitive price to be the benchmark against which to test an (allegedly) excessive price. Section 8(3) says that "*Any person determining whether a price is an excessive price must determine if that price is higher than a competitive price …*" The use of the phrase "*Any person*" coupled with the peremptory "*must*" leaves no doubt that the Commission is required to plead and prove what it considers the competitive price to be.

208. Alternatively, if the Commission's position is that the Regulations serve to equate the competitive price (in section 8(3)) with the respondent's historical prices, then what the Commission has done is to allow the Regulations to swallow their enabling legislation. It is common cause that the source of the Regulations is section 8(3)(f). What that means is that

the Regulations are just one of the many factors that must be taken into account in the 8(3) analysis, i.e. when one determines the competitive price and the reasonableness of the difference between that price and the actual price. On the Commission's interpretation, the Regulations clamber up the hierarchy of section 8 and amend the foundational test for excessive pricing, namely the relationship between actual prices and the competitive price.

209. In short, the Commission treats the Regulations as decisive. But it can never be that subordinate and lesser directives that are passed under section 8(3)(f) somehow amend section 8(3) itself. If that is what the Regulations (purport to) do, they will be set aside.

210. Quite apart from the Commission's suggested test being precluded by a proper construction of the legislation, the CAC has already rejected an approach that relies directly and exclusively on margins. It remarked in *Sasol Chemical Industries:*

> *"While a comparison of prices and costs, which reveals the profit margin, of a particular company may serve as a first step in the analysis (if at all possible to calculate), this in itself cannot be conclusive as regards the existence of an abuse..."*[161]

211. Further, the Commission's position is also internally inconsistent: The Commission accepts that (i) in passing the Regulations, the Minister was acting under *inter alia* section 8(3)(f), and (ii) "*[t]he Consumer Protection Regulations do not change the legislative test applicable to section 8(1)*

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161 See paragraph 104, quoting, with approval, the decision the decision in ***Scandlines Sverige AJ v Helsingborg*** (unreported decision of the European Commission Case No: COMP/A 36.568/D3).

of the Competition Act."[162] In direct conflict with those material concessions, the Commission then advances an entirely novel test, and one that involves the Regulations overhauling, even replacing, the section under which they were promulgated.

212. It is therefore clear that the Commission's suggested approach is simply unsustainable and incorrect.

212.1. First, it finds no support in the text, nor the structure of the Act (in fact, it would require a most contorted reading of the legislation).

212.2. Second, it has effectively been rejected by the CAC in *Sasol Chemical Industries*.

212.3. Third, it runs contrary to a number of established economic principles dealt with below.

212.4. Fourth, it is inconsistent with certain concessions made by the Commission which render its position internally inconsistent.

213. By contrast, Dis-Chem's suggested approach (i) is consistent with the most natural reading of the legislation, (ii) pays due regard to the jurisprudence, and (iii) is firmly rooted in sound economic principles.

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162 Commission's Heads of Argument, in the recent case of ***Competition Commission v Babelegi Workwear Overall Manufacturers & Industrial Supplies CC***, 2020MarC0010/ 2020Mar0063, paragraph 21.

THE CORRECT APPROACH, APPLIED TO THE FACTS OF THIS CASE

The starting point: "*a competitive price*"

214. Assuming the Commission were able to establish dominance (addressed above) its next obstacle would be to prove the competitive price. For all of those reasons, it is obvious that the departure point must be the competitive price. The real question is what is meant by "*a competitive price*". Although the excessive pricing provisions recently underwent significant amendment, those amendments were in large part a codification of what the jurisprudence had already established. The effect being that a number of significant principles established by the CAC in *Mittal* and *Sasol Chemical Industries* remain relevant.

215. Although the test is no longer '*economic value'*, as it was prior to the amendment, and now refers rather to a *"competitive price"*, the substance of the test remains largely unchanged.[163] In *Mittal*,[164] the CAC made reference to *Napp Pharmaceuticals*[165] where it was held that:

> *"Measuring whether a price is above the level that would exist in a competitive market is rarely an easy task. The fact that the exercise may be difficult is not, however, a reason for not attempting it. In the present case, the methods used by the Director are various comparisons of (i) Napp's prices with Napp's costs, (ii) Napp's prices with the costs of its next most profitable competitor; (iii) Napp's prices with those of its competitors and (iv) Napp's prices with prices charged by Napp in other markets. Those methods seem to us to be among the approaches that*

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163 Just last week, the Commission advanced the argument in *Babelegi* that despite COVID-19 and the Regulations, the test laid down in *Mittal* remains the test. See the Commission's Heads of Argument in ***Competition Commission v Babelegi Workwear Overall Manufacturers & Industrial Supplies CC****,* 2020MarC0010/ 2020Mar0063, paragraph 58.

164 ***Mittal Steel South Africa Limited and Others v Harmony Gold Mining Company Ltd***, Case No 70/CAC/Apr07, judgment of 29 May 2009 [50].

165 ***Napp Pharmaceuticals Holdings Ltd & Others v General of Fair Trading*** [2002] CAT 1

may reasonably be used to establish excessive prices, although there are, no doubt, other methods."

216. And so the jurisprudence, which the Commission seems to accept applies to excessive pricing cases while the Regulations are in force,[166] has already established that the appropriate benchmark is "*the level that would exist in a competitive market*." The level that would exist in a competitive market is the "*price [that] would arise under long-run competitive equilibrium in which there is free entry and exit of firms, and firms are able to recover all of their efficient total costs of operation, including a fair return on capital, commensurate with risk*".[167] We consider each of those elements under the section 8(3) sub-headings below.

Dis-Chem's prices relative to the competitive price, and whether the difference is unreasonable:

217. Once the competitive price has been determined, section 8(3) asks whether the difference between that price and the respondent's actual price is unreasonable. The CAC in *Sasol Chemical Industries* accepted that under the reasonableness assessment, one takes account of capital assets,[168] the appropriate rate of return on capital,[169] and the allocation of group costs[170] and common costs.[171]

166 The Commission's Heads of Argument in ***Competition Commission v Babelegi Workwear Overall Manufacturers & Industrial Supplies CC***, 2020MarC0010/ 2020Mar0063, paragraph 58.
167 Expert Witness Statement of Patrick Smith, paragraph 1, page 360 of the Pleadings Bundle.
168 ***Sasol Chemical Industries Ltd v Competition Commission*** [2015] 1 CPLR 58 (CAC) [122]
169 ***Sasol Chemical Industries Ltd v Competition Commission*** [123] et seq.
170 ***Sasol Chemical Industries Ltd v Competition Commission*** [132] et seq.
171 ***Sasol Chemical Industries Ltd v Competition Commission*** [143] et seq.

218. In that case, the CAC found that in addition to the competitive return on capital (which is assessed under the calculation of economic value)[172] Sasol's price-cost margin was between 12% and 14%.[173] The CAC held that returns above economic value are not *per se* unreasonable[174] and concluded that "*a price which is significantly less than 20% of the figure employed to determine economic value falls short of justifying judicial interference in this complex area."*[175]

219. The caution signalled by the CAC finds equal application in this case, and indeed in all excessive pricing cases. Because judicial interference has the potential to result in unintended outcomes, we respectfully submit that the competition authorities should exercise restraint, and allow the market to self-regulate in all but the clearest of cases. As explained by RBB:

> *"Due to the risks inherent in excessive pricing enforcement, as discussed above, it is widely accepted among economists that excessive pricing regulation should only be applied in a limited subset of situations that fulfil certain specific criteria".*[176]

220. As regards what the Commission considers reasonable, it (without laying any basis) imports a test from "*other price gouging laws elsewhere*"[177] and couples that with "*economic logic*"[178] to conclude that a price

172 ***Sasol Chemical Industries Ltd v Competition Commission*** [174]
173 ***Sasol Chemical Industries Ltd v Competition Commission*** [160]
174 ***Sasol Chemical Industries Ltd v Competition Commission*** [174]
175 ***Sasol Chemical Industries Ltd v Competition Commission*** [175]
176 Expert Witness Statement of Patrick Smith, paragraph 47, page 372 of the Pleadings Bundle.
177 The Commission's Supporting Affidavit, paragraph 32, page 46 of the Pleadings Bundle.
178 The Commission's Supporting Affidavit, paragraph 32, page 46 of the Pleadings Bundle.

increase will be material and unreasonable if it is at least 10% above "*the normal competitive price that prevailed historically.*"[179]

Section 8(3)(a) and Regulation 4.2.1: Dis-Chem's price-cost margin, internal rate of return, return on capital invested or profit history

221. We address section 8(3)(a) and regulation 4.2.1 simultaneously because both envisage a price-cost analysis.

222. The Commission and Dis-Chem disagree on the manner in which one views costs in the analysis. Dis-Chem's position is that 'costs' should be taken to include all reasonably incurred costs. The Commission equates 'cost' with marginal cost, i.e. the price Dis-Chem paid for procuring one additional unit. Dis-Chem also contends that where replacement costs bear no reasonable relation to historic procurement costs (as is the case in many price gouging cases), firms are permitted, and indeed ought, to take account of replacement costs.

223. The Federal Trade Commission ("**FTC**")[180] has considered this point and concluded that:

"*A price gouging bill also should account for increased costs, <u>including anticipated costs</u>, that businesses face in the marketplace. Enterprises that do not recover their costs cannot long remain in business, and exiting businesses would only exacerbate the supply problem.*

179 The Commission's Supporting Affidavit, paragraph 32, page 46 of the Pleadings Bundle.

180 In its report titled 'Investigation of Gasoline Price Manipulation and post-Katrina Gasoline Price Increases' ("**The FTC Report**"), available at: https://www.ftc.gov/sites/default/files/documents/reports/federal-trade-commission-investigation-gasoline-price-manipulation-and-post-katrina-gasoline-price/060518publicgasolinepricesinvestigationreportfinal.pdf

Furthermore, cost increases should not be limited to historic costs, because such a limitation could make retailers unable to purchase new product at the higher wholesale prices."[181]

224. The simple point is that when Dis-Chem was setting its prices in March 2020, its primary reference was not what it had *paid* for the stock on hand, its dominant concern was *the price it was going to be required to pay to replace that stock* to ensure that its customers continued to have access to masks. That is intuitively sound and indeed prudent: If a firm fails to have regard to anticipated replacement costs, and those costs turn out to far exceed historical costs, then the firm necessarily encounters material cash flow difficulties and may be unable to replenish stock.

225. The only costs taken into consideration by the Commission are Dis-Chem's marginal costs (i.e. the cost of procuring one additional face mask). Such an approach is blatantly flawed because it outright ignores a whole host of other costs necessarily and/or prudently incurred by Dis-Chem. By way of example, the Commission ignores overheads, other fixed costs, as well as capital costs, and the costs and returns required on any upfront investments.

226. Regulation 4.2.1 requires one to consider any "inc*rease in the cost of providing that good or service*". The Commission's analysis does not properly account for the increase in Dis-Chem's costs because the costs relied upon by the Commission relate in large part to the costs of locally

181 The FTC Report at page 196.

produced masks. But the evidence is that that, due to a positive demand shock that commenced in early 2020, local demand far exceeded supply and so Dis-Chem was forced to source masks abroad.[182] This resulted in a "*substantial increase in the costs of new masks ordered from March 2020*."[183] Figure 4 on pp 36 of the RBB report provides a compelling graphic demonstration of the fact that (i) changes in Dis-Chem's prices correlate very closely with changes in its costs, both upwards and downwards, and (ii) for a significant portion of the complaint period, Dis-Chem's costs exceeded its prices.

227. The Commission excludes a range of costs that are properly considered under any sophisticated analysis of the competitive price.

228. Focusing for the moment just on the marginal cost of masks, Dis-Chem has averaged out the prices that it paid in November and December 2019,[184] and compared them to:

228.1. the quotes that it received for masks for the period 9 March to 24 April 2020;[185] and

228.2. the prices that it paid for masks between end March and 20 April 2020.[186]

182 Expert Witness Statement of Patrick Smith, paragraph 117 and 118, page 402 of the Pleadings Bundle.
183 Expert Witness Statement of Patrick Smith, paragraph 9, page 36 of the Pleadings Bundle.
184 Dis-Chem's Answering Affidavit, Table 1, page 81 of the Pleadings Bundle.
185 Dis-Chem's Answering Affidavit, Table 3, page 87 of the Pleadings Bundle.
186 Dis-Chem's Answering Affidavit, Table 4, page 91 of the Pleadings Bundle.

229. The results of that analysis are staggering: For surgical masks, Dis-Chem was quoted as much as [redacted],[187] and given the prevailing market conditions, Dis-Chem was a price taker with no real bargaining power vis-à-vis suppliers.

230. Ultimately Dis-Chem made additional stock purchases at prices that were between [redacted] higher than the average prices it had paid in November and December 2019.[188] In actual terms, whereas Dis-Chem's weighted average per unit cost was [redacted] in early February 2020, that figure had grown to [redacted] in the last week of March and [redacted] by the first week of April.[189]

231. Furthermore, much of the stock that Dis-Chem had 'secured' was in fact never delivered to it, presumably because suppliers had secured higher prices elsewhere and thus diverted supply away from Dis-Chem.[190] This was disproportionately true in respect of masks 'secured' by Dis-Chem at (reasonably) low prices. In the last week of March 2020, Dis-Chem paid [redacted] per mask for those masks that were actually supplied to it.[191]

232. The cost of masks then began to decrease. By 20 April 2020, Dis-Chem managed to secure four separate shipments of masks (a little under

187 This quote was received from [redacted].
188 Dis-Chem's Answering Affidavit, paragraph 57, page 93 of the Pleadings Bundle.
189 Dis-Chem's Answering Affidavit, paragraph 57, page 93 of the Pleadings Bundle.
190 Dis-Chem's Answering Affidavit, paragraph 57, page 93 of the Pleadings Bundle.
191 Dis-Chem's Answering Affidavit, paragraph 57, page 93 of the Pleadings Bundle.

[redacted]masks in total) with a weighted average unit cost of slightly under [redacted] per unit.[192]

233. As soon as this occurred, Dis-Chem reduced its selling prices despite the fact that the stock it was selling had been procured at much higher prices. That is because in setting current prices, Dis-Chem applied a forward-looking approach with regard being had to the anticipated replacement costs. If Dis-Chem expects its costs to increase, it increases its current prices and if Dis-Chem expects its costs to decrease, it drops its current prices.

234. There can be no doubt that Dis-Chem indeed relies on this forward-looking approach because the daily weighted average gross margin earned by Dis-Chem on mask sales shows that once the cost of masks decreased, Dis-Chem reduced its prices such that it was in fact selling masks below the prices at which those masks had been procured. This resulted in Dis-Chem earning a negative gross margin on the basis of its MAC.[193]

235. As Dis-Chem continued to source masks from abroad, its costs fell and it accordingly lowered its prices.[194] Of critical importance, this price reduction preceded the Commission contacting Dis-Chem and calling for information. What this demonstrates is that even before Dis-Chem was

192 Dis-Chem's Answering Affidavit, paragraph 60, page 94 of the Pleadings Bundle.
193 Expert Witness Statement of Patrick Smith, paragraph 99 and Figure 6, page 394 and 395 of the Pleadings Bundle.
194 Expert Witness Statement of Patrick Smith, paragraph 10, page 361 of the Pleadings Bundle.

aware that it was in the Commission's sights, it had taken steps to reduce its prices in accordance with its rapidly fluctuating costs.

236. Dis-Chem's prices for the period 1 November 2019 to 22 April 2020 are set out in the RBB report in Table 2 on page 32. Broadly, Dis-Chem adjusted its prices upwards between 14 February and 9 March 2020. These adjustments were in line with staggering increases in Dis-Chem's actual costs and its anticipated replacement costs. As of 9 March 2020, Dis-Chem's prices plateau – in line with its actual and anticipated replacement costs – and towards the end of March 2020, Dis-Chem's prices start to come down. Importantly, they come down before Dis-Chem is made aware om 14 April 2020 that the Commission has received any complaint(s) against it.

237. A number of crucial conclusions flow axiomatically from this set of facts.

238. When Dis-Chem's costs are properly computed (i.e. across all masks, not just those produced and procured locally), it becomes apparent that "*Dis-Chem's percentage gross margins were far <u>lower</u> in the period following 19 March 2020, than in the three month period prior to 1 March 2020*."[195] Therefore, even if a case founded solely on the Regulations were permissible, the Commission would (even under that far less exacting standard) not have made out a case.

[195] Expert Witness Statement of Patrick Smith, paragraph 12, page 362 of the Pleadings Bundle.

239. Notably, Dis-Chem's prices are significantly *lower* than the prices published by government on 28 April 2020, when National Treasury issued an Instruction, No 05 of 2020/21 regarding emergency procurement in response to the national state of disaster, establishing maximum prices that state institutions must use to procure basic preventative PPE and cloth masks to contain and manage the transmission of the COVID-19 virus. It sets maximum pricing for surgical masks at R10.22 per mask or R511,00 per box of 50 masks.[196] This is significantly higher than Dis-Chem's highest price of R173,87 per box of 50 masks.[197]

240. Even if one applies the Commission's test, in light of the above, can it be said that Dis-Chem is guilty of (i) effecting a material price increase, (ii) during the disaster period, (iii) that does not correspond with an increase in its relevant costs or increases Dis-Chem's net margin above its average margin in the three-month period before 1 March 2020? The answer is 'no'.

Section 8(3)(b) – Dis-Chem's prices (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

241. Dis-Chem deploys a national pricing strategy across its national store footprint, with all stores charging the same price for all products.[198]

196 Dis-Chem's Answering Affidavit, paragraph 62, page 95 of the Pleadings Bundle.
197 Dis-Chem's Answering Affidavit, Table 5, page 95 of the Pleadings Bundle.
198 Dis-Chem's Answering Affidavit, paragraph 8, page 68 of the Pleadings Bundle.

242. From RBB's pricing analysis, it is evident that Dis-Chem's price per mask increased with Dis-Chem's moving average cost ("**MAC**"), which is the measure of procurement costs that it utilises, and then falls as more favourable procurement prices are attained.[199]

243. RBB's analysis also shows that Dis-Chem's MAC reflects a sudden increase in the costs of masks ordered during March 2020, followed by a gradual decrease in the costs of masks ordered from the beginning of April 2020.[200]

244. The daily weighted average gross margin earned by Dis-Chem on mask sales shows that Dis-Chem decreased mask prices by more than the reduction in MAC following the decrease in purchase prices received by Dis-Chem. [redacted].[201]

245. Dis-Chem had various price changes for the masks between 1 November 2019 to 9 March 2020.[202] None of the price increases are after 15 March 2020:

199 Expert Witness Statement of Patrick Smith, paragraph 98 and Figure 5, page 393 and 394 of the Pleadings Bundle.
200 Expert Witness Statement of Patrick Smith, paragraph 98 and Figure 4, page 393 of the Pleadings Bundle.
201 Expert Witness Statement of Patrick Smith, paragraph 99 and Figure 6, pages 394 and 395 of the Pleadings Bundle.
202 Dis-Chem's Answering Affidavit, Table 5, page 95 of the Pleadings Bundle.

245.1. the prices for “SURGICAL FACE MASKS 5PC” and “SURGICAL FACE MASK BLUE 50PC” were each increased on 14 February 2020;

245.2. on 26 February 2020 the prices for these two products, as well as those of “SURGICAL FACE MASK FOLIODRESS BLUE 50PC” and “SURGICAL FACE MASK FOLIODRESS BLUE 1PC”, were increased;

245.3. between 2 March and 9 March 2020 further price increases were made to three of the stock keeping units corresponding to masks sold by Dis-Chem.[203]

246. As soon as Dis-Chem was able to start procuring masks at cheaper prices, it passed these savings on to consumers, notwithstanding that it was still selling masks that had been purchased at a higher price.[204]

Section 8(3)(c): Comparator firms’ prices and profit levels in a competitive market

247. The Commission’s founding papers[205] are silent on this score. There is no evidence of the Commission having even investigated what comparator firms’ prices were during the complaint period. There is no mention whatsoever about (i) what firms the Commission considers to

203 Expert Witness Statement of Patrick Smith, paragraph 92 and Table 2, page 388 and 389 of the Pleadings Bundle.
204 Dis-Chem’s Answering Affidavit, paragraph 59, page 94 of the Pleadings Bundle.
205 Comprising the Commission’s Notice of Motion, the Commission’s Founding Affidavit and the Commission’s Supporting Affidavit.

be suitable comparators, (ii) comparator firms' prices, or (iii) profit levels in a competitive market. This is a further reason why the Commission was required to determine the competitive price.

248. There will no doubt be cases in which *some* of the section 8(3) factors are not relevant,[206] but it hard to conceive of a reasonable justification for declining to consider the prices of Dis-Chem's comparators/competitors. Had the Commission taken account of these obviously relevant factors, it would have discovered that for the duration of the complaint period, Dis-Chem's prices have consistently remained lower than those of its main rival, [redacted].[207]

249. The evidence is that in order to be cheaper than its closest rival, in early March 2020, Dis-Chem conducted an analysis of [redacted] prices and established that [redacted] was retailing surgical masks at R10.99 for two units. (i.e. R5.49 (including VAT) per mask).[208] Dis-Chem relied directly on that information in determining the prices of its various mask SKUs, ensuring that for each SKU the unit price remained below that of [redacted].[209]

250. That is direct, incontrovertible evidence of Dis-Chem having close regard to its nearest rival's prices in determining its own market conduct. That

206 For example: under section 8(3)(b) of the Competition Act it is envisaged that one considers the respondent's prices in other geographic markets but that factors would simply not apply when the respondent in question sells only into a single geographic market.

207 Expert Witness Statement of Patrick Smith, paragraph 7, page 361 of the Pleadings Bundle.

208 Dis-Chem's Answering Affidavit, paragraph 63.1, page 96 of the Pleadings Bundle; see too **Annexures** "**RG 45**" **and "RG 46"** to Dis-Chem's Answering Affidavit, page 296 and 304 of the Pleadings Bundle.

209 Dis-Chem's Answering Affidavit, paragraph 63.1, page 96 of the Pleadings Bundle.

is fundamentally at odds with a firm that enjoys market power (i.e. the ability to act independently of competitors).

251. On 24 April 2020 (that date falling squarely within the complaint period), Dis-Chem charged R13.00 per mask whereas its most expensive competitor charged R24.35[210] and the cheapest competitor charged R11.24.[211] Of the 11 firms considered, only three firms' prices were cheaper than those of Dis-Chem.

Section 8(3)(d): The length of time the prices have been charged at that level

252. The Commission's case is that Dis-Chem charged excessive prices "*during the period of March 2020 to date*".[212] The Regulations, however, only took effect on 19 March 2020 and because they don't apply retrospectively,[213] the complaint period is (at best for the Commission) 19 March 2020 to 31 March 2020. Therefore, "*the length of time the prices have been charged at that level*" is 11 days.

253. The reason the legislature included the "*length of time*" factor under 8(3) is because it is accepted the world over that unusually high profits tend to trigger new entry,[214] which in turn results in those supra-competitive profits being competed down to competitive levels. As RBB explains:

"When considering which industries would be suitable for excessive pricing regulation, a number of different sets of criteria have been proposed in the literature. The most important of these criteria, and the

210 That being Florida pharmacy at Spar.
211 Expert Witness statement of Patrick Smith, Table 5, page 396 of the Pleadings Bundle.
212 The Commission's Founding Affidavit, paragraph 7, page 8 of the Pleadings Bundle.
213 Dealt with above at paras 130 -150.
214 Assuming for the moment that barriers to entry and expansion are not prohibitively high.

one that is most consistently cited, is that the industry in question must be subject to high and non-transitory barriers to entry and expansion, such that high prices in the industry in question are not likely to constitute efficient signals for new investment and entry."[215]

254. There is no evidence of barriers to entry or expansion being high and/or non-transitory. In fact, the Commission says nothing at all about barriers. Absent any evidence of significant entry/expansion barriers, it is generally considered unwise for competition authorities to intervene, particularly because of the real potential for unintended consequences. As the CAC cautioned in *Sasol Chemical Industries*:

"A measure of deference is called for in these enquiries not only because of the importance of freedom of pricing but also to obviate converting courts into price regulators."[216]

255. As the RBB report makes clear, there is unanimity among the leading economic commentators that "*competition authorities should not intervene in markets where it is likely that normal competitive forces over time will eliminate the possibilities of a dominant company to charge high prices.*"[217] Stated differently, "*the threshold for intervention should be … a monopolist … whose position is not likely to be challenged by entrants.*"

256. The question of precisely when a competition authority ought to intervene to correct an excessive price came to the fore in the recent *Latvian Copyright Society* case.[218]

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215 Expert Witness Statement of Patrick Smith, paragraph 49, page 373 of the Pleadings Bundle.
216 ***Sasol Chemical Industries Ltd v Competition Commission*** [2015] 1 CPLR 58 (CAC) [109].
217 Expert Witness Statement of Patrick Smith, paragraph 52, page 374 of the Pleadings Bundle.
218 ***Autortiesību un komunicēšanās konsultāciju aģentūra / Latvijas Autoru apvienība vs Konkurences padome***, (Case 177/16, 14 September 2017).

257. In that case, the Latvian Supreme Court was confronted with an excessive pricing case and referred certain legal questions to the European Court of Justice (ECJ). The ECJ was asked to determine:

> *"… above what threshold the difference between the rates compared is to be regarded as appreciable and, therefore, indicative of an abuse of a dominant position …"*[219]

258. In other words, when will a price be considered to be <u>appreciably</u> above the competitive level. Advocate General Wahl laid out the position thus:

> "*At the outset, let us start by recalling the economic rationale of the unfair pricing abuse: when a dominant undertaking applies prices above competitive levels, there is an inefficient allocation of resources and consumer welfare is reduced (part of the welfare is transferred to the dominant company, whereas part is simply lost). <u>Accordingly, from a theoretical point of view, any deviation from the competitive price in a regulated market might justify an intervention of the competition authorities</u>. Indeed, any difference between the benchmark price and the actual price implies a certain loss in consumer welfare that would not have been there had the market been competitive*.[220]
>
> *However, <u>such an approach would, for a competition authority, neither be realistic nor advisable</u>.*[221]

259. The ECJ then lays down a number of reasons why restraint must be exercised and why, other than in very specific circumstances, courts should defer to market forces.

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219 ***Autortiesību un komunicēšanās konsultāciju aģentūra / Latvijas Autoru apvienība vs Konkurences padome****,* [52]. This is how the ECJ explained the question before it.

220 ***Autortiesību un komunicēšanās konsultāciju aģentūra / Latvijas Autoru apvienība vs Konkurences padome***, [101]

221 ***Autortiesību un komunicēšanās konsultāciju aģentūra / Latvijas Autoru apvienība vs Konkurences padome***, [102]

260. First, the Court explained that "*type I errors in competition decisions concerning unilateral conduct involve a much larger cost for the society than type II errors: 'the economic system corrects monopolies more readily than it corrects judicial errors …*".[222]

261. The Court went on to explain:

> "*That is why — in line with the approach adopted by the relevant authorities and courts both at the EU level and at the Member States level, and as suggested in economic writings — I take the view that a price can be qualified as excessive … only if two conditions are fulfilled: it ought to be both significantly and persistently above the benchmark price*."[223]

262. The European Union therefore requires that in order for a price to be appreciably above the competitive level, two requirements *must* be present: prices that are (i) significantly and (ii) persistently above the benchmark price.

263. In respect of the 'persistence' requirement, the Court gave meaning to the requirement as follows:

> "*the fact that the price of a given product or service is sporadically above the benchmark price is, to my mind, of little relevance … Only when a price remains (or is recurrently) above the benchmark price for a substantial period of time may that price be abusive under Article 102 TFEU. Support for that approach can be found in General Motors.*"[224]

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222 ***Autortiesību un komunicēšanās konsultāciju aģentūra / Latvijas Autoru apvienība vs Konkurences padome***, [103]

223 ***Autortiesību un komunicēšanās konsultāciju aģentūra / Latvijas Autoru apvienība vs Konkurences padome***, [106]

224 ***Autortiesību un komunicēšanās konsultāciju aģentūra / Latvijas Autoru apvienība vs Konkurences padome*** [108]

264. The case is therefore authority for the proposition that the ECJ considers judicial interference to be wholly inappropriate unless and until the price in issue remains significantly above the benchmark price for a substantial period of time.

265. This accords squarely with the understanding of the CAC in the opening paragraphs of its judgment in *Sasol Chemical Industries* where it stated that "*economists define excessive prices as those which are significantly and persistently above the competitive level.*"[225] (The submissions above regarding persistence or durability of market power find equal application in this section and we respectfully ask the Tribunal to have regard to them at this stage of the analysis too.) As explained in Economics for Competition Lawyers, *"Only market power that persists over time is of concern."*[226]

266. The evidence, however, is to the contrary: Even on the Commission's version, there were high prices for an extremely short period of time, after which they dropped significantly. The Commission does not even contend that prices were persistently high. The Commission's approach is to ignore section 8(d)(3), and to provide no reason for why the policy considerations underpinning it don't find application on the facts of this case.

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225 ***Autortiesību un komunicēšanās konsultāciju aģentūra / Latvijas Autoru apvienība vs Konkurences padome*** [2].

226 Niels G, Jenkins H and Kavanagh J, *Economics for Competition Lawyers* Oxford University Press, (1st Edition 2011), page 45.

Section 8(3)(e): The structural characteristics of the relevant market

267. Excessive pricing regulation is aimed at addressing markets characterised by enduring/persistent high barriers to entry and expansion; those in which there is relative certainty that despite the incumbent enjoying supracompetitive profits, market forces are simply incapable of correcting obvious inefficiencies. In fact, we have been unable to find a single case (in any jurisdiction) in which a FMCG firm was guilty of excessive pricing.

268. This case has none of the hallmarks of an excessive pricing case. The market is characterised by a large number of suppliers, very low barriers to entry and a high degree of substitutability. The market is also perfectly contestable.

269. That the market has many existing suppliers is evidenced by the many quotes that Dis-Chem was able to source very quickly. These quotes varied widely, but were typically many times higher than Dis-Chem's historical procurement costs.[227]

270. In addition, these suppliers wielded significant market power, rendering Dis-Chem a price taker in the true sense. Dis-Chem's suppliers were in a position to dictate payment terms and prices,[228]something never witnessed in respect of a firm that wields market power.

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227 Expert Witness Report of Patrick Smith, paragraph 96, Table 4, page 92 of the Pleadings Bundle.

228 Dis-Chem's normal trading terms are to pay suppliers on 30-day terms. Dis-Chem's Answering Affidavit, paragraph 71, page 102 of the Pleadings Bundle.

271. There is also direct evidence of barriers to expansion being very low. Existing producers of masks sought to ramp up their production capabilities.[229] For example, Universal Safety Products has given notice that it is expanding capabilities and aiming to increase the size of its workforce by more than 65% over a few weeks.[230]

272. In the context of the current pandemic, the purpose of a face mask, whether of the cloth or surgical variety, is to assist in the prevention of the spread of the SARS-CoV-2 virus. Therefore, cloth masks and surgical masks are, from a demand side, perfectly substitutable for one another. Given the DoH's confirmation that it is satisfied that the scientific evidence shows that a cloth face mask significantly reduces the amount of virus that can be shed, there can be no concerns regarding the functional substitutability of the two mask varieties.[231]

273. From a supply side perspective, new avenues of supply of both types of masks are constantly opening up in response to the increased demand.[232] Dis-Chem itself has managed to identify a wide range of new and alternative suppliers for surgical masks. Similarly, numerous retailers and manufacturers are putting their otherwise idle resources to work in the manufacture of cloth masks. Moreover, many members of the public are making cloth masks, both for their own use and in many cases for sale to others. So easy are many of the methods to make an

229 Dis-Chem Answering Affidavit, paragraph 26, page 77 of the Pleadings Bundle.
230 Dis-Chem Answering Affidavit, paragraph 26 and "**Annexure RG 6**" thereto, page 77 and 179 of the Pleadings Bundle.
231 Dis-Chem's Answering Affidavit, paragraph 28, page 78 of the Pleadings Bundle.
232 Dis-Chem Answering Affidavit, paragraph 29, page 78 of the Pleadings Bundle.

acceptable quality cloth mask that a sewing machine is not even required. The potential sources of supply for masks is therefore almost limitless. Accordingly, from a supply side perspective, it is clear that cloth and surgical masks are substitutes.[233]

274. Barriers to entry and expansion are therefore negligible.

275. As regards contestability, "*a contestable market is one where even an apparent monopolist has no market power, because sunk costs do not exist and barriers are so low that the threat of entry is sufficient to constrain the incumbent.*"[234] The Commission has not – and nor could it have – pointed to any features of the market that render even a small part of it incontestable. There are almost no sunk costs and barriers are negligible.

Section 8(3)(f): The Regulations

276. Regulation 4.1 merely restates the position under the Act itself and so doesn't call for any separate discussion. We have dealt with regulation 4.2.1above (under the section that deals with section 8(3)(a)). That leaves regulation 4.2.2 which envisages a margin analysis with regard being had to the respondent's margins in the three-month period prior to 1 March 2020.

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233 Dis-Chem Answering Affidavit, paragraph 29, page 78 of the Pleadings Bundle.

234 Niels G, Jenkins H and Kavanagh J, *Economics for Competition Lawyers* Oxford University Press, (1st Edition 2011), page 138.

277. RBB's analysis shows that Dis-Chem's gross margins on masks were far lower in the period following 19 March 2020 than in the three-month period prior to 1 March 2020.[235] That alone disposes of a case under regulation 4(4)(2) which requires an increase in margins above the three-month average.

278. As RBB notes, a simplistic assessment of only changes in prices and margins for a selective sub-sample of the relevant products, is insufficient to distinguish excessive pricing from normal competition on the merits in the prevailing market conditions.[236]

279. While Dis-Chem's overall turnover [redacted] relative to March 2019, this was coupled with a [redacted], indicating Dis-Chem's [redacted]. Turnover in April 2020 also showed a [redacted].[237]

280. Importantly, masks account for only a small proportion of Dis-Chem's sales.[238] In March and April 2019, masks accounted for approx. [redacted] of Dis-Chem's total sales in each month, whereas in March 2020, masks accounted for [redacted] of total sales, and in the period 1-23 April 2020 masks accounted for [redacted] of total turnover.[239]

235 Expert Witness Statement of Patrick Smith, paragraph 108 and 109, and Table 7, page 400 of the Pleadings Bundle.
236 Expert Witness Statement of Patrick Smith, paragraph 15, page 362 of the Pleadings Bundle.
237 Expert Witness Statement of Patrick Smith, paragraph 80, page 383 of the Pleadings Bundle.
238 Expert Witness Statement of Patrick Smith, paragraph 82, page 384 of the Pleadings Bundle.
239 Expert Witness Statement of Patrick Smith, paragraph 82, page 384 of the Pleadings Bundle.

281. [redacted]. If one were to apply a simple proportional allocation of common fixed costs (such as staff, utilities and head office costs) to all the different products sold by Dis-Chem, in proportion to each of their contribution to total sales revenues, then the allocation of these common fixed costs to the sales of masks in March 2020 would have been around [redacted] higher than in March 2019, and around [redacted] higher in April 2020 relative to April 2019.[240]

282. In this context, where the margin on masks is so small and masks account for such a small percentage of Dis-Chem's turnover, it brings into sharp focus the counterfactual that absent a price increase, there is no incentive for firms to expend the resources to source additional masks.

"To The Detriment Of Consumers"

283. Although the Commission's approach jettisons almost all of the excessive pricing provisions in the Act, one thing it does accept is that the excessive price(s) must be "*to the detriment of consumers or customers*".[241] The Commission deals with detriment to consumers in the complaint referral affidavit at paras 54 *et seq.* It commences by remarking that consumers are unhappy with Dis-Chem having increased

240 Expert Witness Statement of Patrick Smith, paragraph 82, page 384 of the Pleadings Bundle.
241 The Commission's Founding Affidavit, paragraph 32.3, page 19 of the Pleadings Bundle.

its prices.[242] It then stridently asserts that "*it is trite that if a firm charges excessive prices, harm to consumers and customers will follow.*"[243]

284. That is a paragon of circular reasoning. If consumer harm flows axiomatically from an excessive price, then the legislature would not have inserted the phrase "*to the detriment of consumers*" because no purpose would be served by it.

285. Apart from being conclusory, the Commission's interpretation of the section is also unsustainable because our law contains a presumption against tautology/superfluity. In *Wellworths Bazaars Ltd*,[244] Davis AJA quoted approvingly of the following passage:

> *"It is . . . a good general rule in jurisprudence that one who reads a legal document, whether public or private, should not be prompt to ascribe … to its language tautology or superfluity, and should be rather at the outset inclined to suppose every word intended to have some effect or be of some use."*

286. The phrase "*to the detriment of consumers*" therefore means *something*. The real question is what. By requiring a showing of detriment to consumers, the legislature clearly appreciates that in *some* circumstances, a price will be excessive but will not be treated as having harmed consumers.

287. We respectfully submit that the answer lies in the counterfactual. The Commission's position (at least impliedly) is that Dis-Chem, when faced

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242 The Commission's Founding Affidavit, paragraph 54, page 25 of the Pleadings Bundle.
243 The Commission's Founding Affidavit, paragraph 57, page 26 of the Pleadings Bundle.
244 ***Wellworths Bazaars Ltd v Chandlers Ltd*** [1947] 2 All SA 233, 1947 (2) SA 37 (A).

with rapidly increasing costs and demand, and increased scarcity of supply had two options at its disposal: (i) set prices as it did, or (ii) set prices significantly lower than it did. If that were the appropriate counterfactual, the Commission may have a case on detriment. But positing that scenario is self-serving from the Commission's perspective. Those are not the only options available to a firm in Dis-Chem's shoes.

288. If the Commission's approach is upheld, the massive risks associated with stocking items on Annexure A of the Regulations will result in firms declining to stock those goods/sell those services. Like any responsible corporate citizen, Dis-Chem carries out a risk/reward analysis, it may well determine that selling the goods listed in Annexure A to the Regulations exposes it to unacceptable levels of risk, and it declines to stock the goods listed in the Regulations.

289. Accordingly, the appropriate counterfactual is not a world in which face masks are sold cheaply. The true counterfactual is a world in which Dis-Chem – and any other firm that carries out any form of risk/reward analysis – declines to stock essential goods.

290. On the unique facts created by COVID-19, detriment to consumers is being unable to source face masks and other essential goods. *"[T]o the detriment of consumers*" is not satisfied by the Commission demonstrating that in line with supply shortages, Dis-Chem faced increased costs and increased its prices accordingly. Faced with a

choice between higher priced masks[245] and no masks at all, customers chose the former.

291. The Commission suggests that the affected customers are "*poor consumers*" who are "*cut off … from goods essential to maintain their health, safety and welfare in a disaster context.*"[246] That is not correct in a few respects. As recognised in Competition Law of South Africa:[247]

> *"The requirement that the excessive price is "to the detriment of consumers" has two important implications. First, charging an excessive price to an intermediate buyer who is not a consumer of the product is not prohibited by section 8(a) unless it also causes detriment to consumers. The term "consumers" includes all those who consume the product, whether productively or as final consumers.[248] This does not mean that the excessive price must be charged directly to consumers, but only that, where the price is charged to an intermediate buyer, there should be some resulting detriment to consumers. In some cases, this may occur because the excessive cost of an input is necessarily passed on to consumers, rather than simply resulting in a "commercial division of revenues" between suppliers at different [Page 7-49] levels of the supply chain."*[249]

292. The evidence is that the surge in demand that Dis-Chem faced was substantially driven by very large volumes of purchases by a relatively small number of customers.[250] The overwhelming likelihood is that they

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245 Higher priced because of an increase in the costs faced by Dis-Chem.

246 The Commission's Supporting Affidavit, paragraph 11, page 36 of the Pleadings Bundle.

247 Sutherland & Kemp, *Competition Law of South Africa*, Lexis Nexis updated as at November 2019, paragraph 7.9.3.

248 The CAC, while noting that the Act treats "customers" and "consumers" as distinct concepts, expressed the view that "where customers of the dominant firm themselves consume the product – whether productively or as final consumers – it would seem artificial to exclude the from the ambit of the term ['consumers']" in section 8(a): ***Mittal Steel South Africa Ltd v Harmony Gold Mining Co Ltd*** 70/CAC/Apr07 [55].

249 The latter was found to be the case in ***Attheraces Ltd v The British Horseracing Board Ltd*** [2007] EWCA Civ38.

250 Which is established by data on Dis-Chem's loyalty cards. It thus appears that the increased demand volumes for masks around the end of January 2020, beginning February 2020 was mainly as a result of seemingly opportunistic bulk buying trading purposesRBB report, para 14.

were acting as intermediaries, simply buying masks from Dis-Chem and on-selling them.

293. It is also instructive to consider how the FTC has approached price gouging. In the week following Hurricane Katrina, gasoline prices in the United States rose significantly.[251] This led to allegations of price gouging and Congress directed the FTC to investigate whether these developments resulted from market manipulation or price gouging practices in the sale of gasoline. The FTC duly carried out its investigation and released its report titled 'Investigation of Gasoline Price Manipulation and post-Katrina Gasoline Price Increases'

294. Part III of the FTC report is headed 'Policy Implications and Recommendations', and Section B thereof is titled 'Federal Price Gouging Legislation'. The section commences with the FTC explaining (i) that it is preferable to allow the market to self-correct, and (ii) how legislative intervention often results in harm to consumers:

> "*Consumers understandably are upset when they face dramatic price increases within very short periods of time, especially during a disaster. In a period of shortage, however… higher prices create incentives for suppliers to send more product into the market...*"[252]

251 The FTC Report, page (vi).
252 The FTC Report, page 196.

"If pricing signals are not present or are distorted by legislative or regulatory command, markets may not function efficiently and consumers may be worse off. Accordingly, our competition-based economy generally … relies on market forces – rather than government intervention – to determine the prices a seller can seek."[253]

295. The ultimate conclusion of the FTC is that it "*cannot say that federal price gouging legislation would produce a net benefit for consumers*" but that "*if Congress nevertheless proceeds with passing federal price gouging legislation… any price gouging legislation should:*

"*define the offense clearly. A primary goal of a statute should be for businesses to know what is prohibited. An ambiguous standard would only confuse consumers and businesses and would make enforcement difficult and arbitrary."*[254]

"A price gouging bill also should account for increased costs, including anticipated costs, that businesses face in the marketplace. Enterprises that do not recover their costs cannot long remain in business, and exiting businesses would only exacerbate the supply problem. Furthermore, cost increases should not be limited to historic costs, because such a limitation

253 The FTC Report, page 196.
254 The FTC Report, page 196.

could make retailers unable to purchase new product at the higher wholesale prices."[255]

"The statute also should provide for consideration of local, national, and international market conditions that may be a factor in the tight supply situation. International conditions that increase the price of crude oil naturally will have a downstream effect on retail gasoline prices. Local businesses should not be penalized for factors beyond their control."[256]

"Finally, any price gouging statute should attempt to account for the market-clearing price. Holding prices too low for too long in the face of temporary supply problems risks distorting the price signal that ultimately will ameliorate the problem. If supply responses and the market-clearing price are not considered, wholesalers and retailers will run out of gasoline and consumers will be worse off."[257]

296. The Commission's approach is at odds with each of those requirements.

297. *First*, there is great ambiguity about precisely what is prohibited and what the appropriate test is while the Regulations are in operation.

298. *Second*, the Commission rejects an approach that takes account of an anticipated increase in costs. The evidence is that when Dis-Chem

255 The FTC Report, page 196.
256 The FTC Report, page 197.
257 The FTC Report, page 197.

decided to increase prices as it did, that decision was directly and materially influenced by the prices that Dis-Chem predicted it would have to pay to replace that stock. Determining prices with regard to anticipated replacement costs is perfectly legitimate because if replacement costs are not factored in, the firm won't be in a position to replenish stock and consumer harm flows axiomatically.

299. *Third*, Dis-Chem's price increases were underpinned by a rapid surge in its costs and the Commission ignores many of these costs.

300. *Fourth*, the Commission's approach is silent on the market clearing price and, as we have said elsewhere, risks creating a position far worse in terms of which suppliers simply decline to stock essential goods because the fear of punishment outweighs any potential profits.

301. Accordingly, the Commission has failed to plead and establish a case under section 8 of the Act, read with regulation 4. Its complaint referral was ill-conceived following an inadequate investigation, and has not been sufficiently bolstered by its recreation in its replying affidavit.

302. There is no basis to find that Dis-Chem is a dominant firm in the relevant market that charged a price that is unreasonably higher than a competitive price, where the competitive price represents the price that would pertain under conditions of long run competitive equilibrium in which there is free exit and entry of firms, and firms are able to recover all of their efficient total costs of operation, including a fair return on

capital, commensurate with risk and that price was to the detriment of consumers or customers.

303. The complaint referral should be dismissed.

ADMINISTRATIVE PENALTY

Introduction

304. Given that the Commission has failed to establish a contravention of section 8 of the Act, there is no need to address the issue of administrative penalty in terms of section 59. However, it has been so-directed by the Tribunal.

305. The Regulations set out a section dealing with penalties to be imposed on parties which contravene it. Section 7 states:

*"7. **Penalties***
7.1 A dominant firm that contravenes or fails to comply with regulation 4 must be investigated by the Competition Commission and, if found to be in contravention, is liable for the penalties imposed upon it as provided for in the Competition Act.
7.2 Subject to the requirements of the Competition Act, the Consumer Protection Act and the regulations published in terms of section 27(2) of the Disaster Management Act, a person of firm which contravenes these regulations could have one or more of the following penalties imposed –
7.2.1 A fine of up to R1 000 000;
7.2.2 A fine of up to 10% of a firm's turnover; and
7.2.3 Imprisonment for a period not exceeding 12 months."

306. The Commission prays for an administrative penalty to be imposed on Dis-Chem in respect of each contravention, in terms of section 58(1)(a)(iii) of the Act, equal to 10% (ten percent) of its annual turnover in the Republic and its exports from the Republic during its preceding financial year.[258]

[258] The Commission's Notice of Motion, paragraph 5, page 3 of the Pleadings Bundle.

307. The question that arises is whether the Commission is entitled to a prayer for an admin penalty equal to 10% (ten percent) of Dis-Chem's annual turnover in the Republic and its exports from the Republic during its preceding financial year in respect of each alleged instance of contravention of section 8(1) of the Act read with regulation 4 of the Regulations.

The test for administrative penalties

308. The relevant provisions of the Act are sections 58 and 59 of the Act. In particular, section 59(3) provides that:

> *"When considering an administrative penalty, the Competition Tribunal must consider the following factors:*
> *(a) the nature, duration, gravity and extent of the contravention;*
> *(b) any loss or damage suffered as a result of the contravention;*
> *(c) the behaviour of the respondent;*
> *(d) 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 ;*
> *(e) the level of profit derived from the contravention;*
> *(f) the degree to which the respondent has co-operated with the Commission and the Competition Tribunal; and*
> *(g) whether the respondent has previously been found in contravention of this Act."*
> *(h) 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.*

309. Section 59(2) states: *"An administrative penalty . . . may not exceed 10 percent of the firm's turnover in the Republic and its exports from the Republic during the firm's preceding financial year."*

310. Determining an appropriate administrative penalty is, like sentencing in a criminal matter, case-specific. It is not, and can never be, scientific.[259]

311. In calculating the administrative penalty, the Tribunal follows the approach adopted by it in the Tribunal in the ***Competition Commission v Aveng***[260]. In that case the Tribunal identified a six-step approach for determining a fine in accordance with section 59 of the Act. These steps are as follows:

311.1. **Step one**: determination of the affected turnover in the relevant year of assessment;[261]

311.2. **Step two**: calculation of the 'base amount,' being that proportion of the relevant turnover relied upon;

311.3. **Step three**: where the contravention exceeds one year, multiplying the amount obtained in step 2 by the duration of the contravention;

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259 ***Isipani Construction (Pty) Ltd v Competition Commission*** (144/CAC/Aug16CT, 019950) [2017] ZACAC 3 (14 September 2017) [78]

260 ***The Competition Commission vs Aveng (Africa) Limited t/a Steeledale and Others*** (84/CR/DEC09); ***Competition Commission v Isipani Construction (Pty) Ltd and Another*** (CR128Nov14) [2016] ZACT 88 (18 July 2016) [15]

261 Affected turnover commonly refers to the turnover of the firm in the relevant product market affected by the anti-competitive conduct. However, the Tribunal has stated that the affected turnover of the respondent firm will be based on the sales of the products or services that can be said to have been affected by the contravention. See *Competition Commission v Aveng (Africa) Ltd* 84/CR/Dec09 para 134. See also *Commission Guidelines*, GN 323, *Government Gazette*, 17/04/2015, pars 1.1.5, 5.3–5.4, indicating that the Commission will generally have regard to the firm's affected turnover during the "base year", that is, "the most recent financial year in which there is evidence that the firm participated in the contravention"

311.4. **Step four**: rounding off the figure obtained in step 3, if it exceeds the cap provided for by section 59(2);

311.5. **Step five**: considering factors that might mitigate or aggravate the amount reached in step 4, by way of a discount or premium expressed as a percentage of that amount that is either subtracted from or added to it;

311.6. **Step six**: rounding off this amount if it exceeds the cap provided for in section 59(2). If it does, it must be adjusted downwards so that it does not exceed the cap.

312. Here, the Commission seeks an administrative penalty in respect of each contravention equal to 10% of Dis-Chem's annual turnover. The Commission has previously asked the Tribunal to impose a penalty of up to 10% of a firm's turnover for each instance of contravention in *Isipani*.[262]

313. The Tribunal agreed with the Commission that each instance of a cover pricing constitutes a separate self-standing infringement of the Act. It went on to say that such an approach is consistent with the approach followed by the ***Office of Fair Trading*** **and the** ***Competition Appeal Tribunal*** **in** ***Kier Group PLC and others v Office of Fair Trading***[263]

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262 ***Competition Commission v Isipani Construction (Pty) Ltd and Another*** (CR128Nov14) [2016] ZACT 88 (18 July 2016) [17].

263 ***Office of Fair Trading and the Competition Appeal Tribunal in Kier Group PLC and others v Office of Fair Trading***, 2011 CAT 3.

where each of the Appellants were fined separately for each cover pricing infringement.[264]

314. However, the Tribunal made it clear that it must exercise its discretion based on the facts of each case in the interest of fairness and the doctrine of proportionality to decide how to levy an appropriate administrative penalty pursuant to section 59(3) of the Act.

315. This discretion was confirmed by the CAC when it stated:[265]

"*The power of the Tribunal to impose a penalty on an errant party is one that lies within its discretion. It is a discretion that is wide and cannot be fettered even by its own Guidelines or policies.*"

316. In exercising its discretion, the Tribunal held:[266]

"In this case we have decided to levy a single administrative penalty in respect of the two separate incidences of cover pricing. In our decision we were cognizant of, the fact that there was a second, separate contravention of the Act in our final calculation of the single penalty amount."

317. On appeal, the Commission sought to challenge the Tribunal's discretion not to levy a penalty in respect of each contravention of the Act. However, the CAC stated the following in respect of the Tribunal's decision to levy one penalty:

"*We know from [20] of the Tribunal's decision that it understood its unfettered discretion to include the power to consolidate more than one penalty, in this case two, into a single one. From the Tribunal's*

264 ***Competition Commission v Isipani Construction (Pty) Ltd and Another*** (CR128Nov14) [2016] ZACT 88 (18 July 2016) [18].

265 ***Isipani Construction (Pty) Ltd v Competition Commission*** (144/CAC/Aug16CT, 019950) [2017] ZACAC 3 (14 September 2017) [30]

266 ***Competition Commission v Isipani Construction (Pty) Ltd and Another*** (CR128Nov14) [2016] ZACT 88 (18 July 2016) [20].

perspective, as long as the ultimate penalty fell within the scope of s 59 of the Act, it would have acted within its statutorily conferred powers. It is empowered, in terms of s 59(1)(a) to impose a penalty for a contravention of s 4(1)(b); the penalty must take into account the factors and circumstances listed in s 59(3) and must comply with the restriction set in s 59(2) of the Act. As long as the performance of its task was consistent with the provisions of these sub-sections, its manoeuvrability was elastic enough for it to combine two or more penalties into one. Viewed from a different angle, as long as the single penalty took account of all the contraventions and as long as the penalty took full account of everything said in s 59 of the Act it acted intra vires."

318. In the *Isipani CAC decision*, the Commission went on to say that the Tribunal imposed a single penalty for the August 2010 contravention and used the November 2010 penalty as an aggravating factor. Hence, to the extent that it has discretion to impose a single penalty, it exercised the discretion injudiciously. In contrast, it should have imposed two penalties and then adjusted the sum of the two penalties in order to meet the requirements of proportionality and fairness.[267]

319. However, the CAC found the Commission's submissions problematic stating:[268]

"*But it is here that the logic propounded by the Commission becomes problematic. If the end result of the combined penalty has to be one that is proportionate and fair then there should be no problem with imposing a single penalty, as long as there is no absolution inherent in the penalty for any contravention of which the firm was found guilty. There could be a legitimate argument to this effect if the single penalty imposed was too low considering that the firm is being punished for more than one contravention. In other words, the ultimate penalty must be fair and proportionate to the number of offences. In this case, the Tribunal asserted that it was. It said:*

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267 ***Isipani Construction (Pty) Ltd v Competition Commission*** (144/CAC/Aug16CT, 019950) [2017] ZACAC 3 (14 September 2017) [48].

268 ***Isipani Construction (Pty) Ltd v Competition Commission*** (144/CAC/Aug16CT, 019950) [2017] ZACAC 3 (14 September 2017) [48].

'In our decision we were cognizant of, the fact that there was a second, separate contravention of the Act in our final calculation of the single penalty amount.'"

320. The CAC went on further to state:[269]

"*[the Commission] merely asks for the matter to be referred back to the Tribunal to be re-considered afresh on the basis that it should impose a separate penalty for each contravention. In other words, the error of law complained of is one on the merits and not one where the Tribunal failed to understand the nature of its discretion. But, we would only refer the matter back to the Tribunal if we were to find that the error it is supposed to have committed could be remedied with an instruction to issue two penalties and if the combined penalty would be different from the present one. Then too, we would also only send it back if the result would be indeterminate.*"

321. Ultimately the CAC held:

"This court can interfere with an administrative penalty on appeal if the discretion was exercised on the wrong principle See MacNeil Agencies v Competition Commission 121.CACJul12. That having been said, it is obviously necessary to impose a fine sufficient to deter Isipani and other companies to refrain from the cover price infringement."

322. It is clear from the *Isipani CAC decision* that the ultimate test to be undertaken by the Tribunal is whether the penalty imposed is fair and proportional.

323. We now perform the six step calculation required.

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269 ***Isipani Construction (Pty) Ltd v Competition Commission*** (144/CAC/Aug16CT, 019950) [2017] ZACAC 3 (14 September 2017) [49].

Step one: determination of the affected turnover in the relevant year of assessment

324. Affected turnover commonly refers to the sales of the products or services that can be said to have been affected by the contravention.[270] In this regard, Dis-Chem's starting position is the combined turnover of its mask sales for the period 19 to 31 March 2020, being [redacted].[271]

325. It is important to contrast this amount to the amount that the Commission in its replying affidavit estimates is the overcharge at issue in this case, namely of [redacted] for February 2020 and [redacted] for March 2020, bringing the total overcharge to [redacted][272]

Step two: calculation of the 'base amount,' being that proportion of the relevant turnover relied upon

326. The base amount will be calculated as a proportion of the affected turnover on a scale from zero percent (0%) to thirty per cent (30%)[273]. The proportion applied will be based on some of the factors listed in section 59(3), specifically section 59(3)(a), (b), and (d), which are:

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270 ***The Competition Commission vs Aveng (Africa) Limited t/a Steeledale and others*** (84/CR/DEC09) [14]; See also Commission Guidelines, GN 323, Government Gazette, 17/04/2015, pars 1.1.5, 5.3–5.4 ("**Administrative Penalty Guidelines**"), indicating that the Commission will generally have regard to the firm's affected turnover during the "base year", that is, "the most recent financial year in which there is evidence that the firm participated in the contravention

271 Dis-Chem's Answering Affidavit, paragraph 68 and Table 8, page 101 of the Pleadings Bundle.

272 The Commission's Replying Affidavit, paragraph 54, page 458 of the Pleadings Bundle.

273 ***The Competition Commission vs Aveng (Africa) Limited t/a Steeledale and Others*** (84/CR/DEC09) [147].

326.1. The nature, gravity and extent of the contravention;

326.2. Any loss or damage suffered as a result of the contravention; and

326.3. The market circumstances in which the contravention took place.

327. In determining whether the proportion of the base amount will be at the higher end or lower end of the scale (i.e. 0 to 30%), in light of the factors listed above, the Commission will consider the following:

327.1. The nature of the affected product(s);

327.2. The structure of the market;

327.3. The market shares of the firms involved;

327.4. Barriers to entry in the market; and

327.5. The impact of the contravention on competitors and consumers, and the likely impact on small and medium-sized enterprises and on low income consumers.

328. At the outset, it is important to note that there is no evidence that that the alleged contravention impacted small and medium-sized enterprises and/or on low income consumers.

329. Dis-Chem acknowledges that there was increased demand for surgical masks resulting in a sales volumes to purchasers of bulk volumes increased from around [redacted] masks per month to [redacted] masks in

February 2020. However, cloth masks and surgical masks are substitutes for each other.

330. On the demand side, members of the public looking to wear a face mask can choose between either a cloth mask or a surgical mask. Given the DoH's confirmation that it is satisfied that the scientific evidence shows that a cloth face mask significantly reduces the amount of virus that can be shed, there can be no concerns regarding the functional substitutability of the two mask varieties.[274]

331. In addition, the DoH recommended that face masks be used in addition to hand-washing and social distancing. Importantly, the DoH stressed that "*the face mask should never be promoted as our primary prevention strategy and should never be promoted separately from hand-washing and social distancing*". Therefore, surgical masks are one of many measures that the public could implement to prevent themselves from contracting the virus.[275]

332. The barriers to entry in respect of the production, wholesale and/or retail of masks are low. There is a very wide range of cloth face masks available to members of the public. These can be purchased ready-made from a wide range of retailers, alternatively, constructed at home using items likely to be available in all homes. The Internet, print media and television are replete with instructions on how to make these masks

[274] Dis-Chem's Answering Affidavit, paragraph 21.7, page 74 of the Pleadings Bundle.
[275] Dis-Chem's Answering Affidavit, paragraph 21.6, page 73 of the Pleadings Bundle.

at home. Similarly, commercial sellers of cloth masks are mushrooming across the country. These sellers range from large retailers expanding their product ranges to small businesses and even people who are simply making these masks for their immediate family and community. Cloth masks can be purchased in stores and online, with many sellers offering home delivery in a matter of days.[276]

333. Although the Commission indicates in its Administrative Penalty Guidelines that that higher end of the scale will be reserved for the most serious contraventions such as excessive pricing, we are of the view that in light of the market circumstances that Dis-Chem found itself in, as well as the chaos in procurement that was created by the COVID-19 pandemic, the base of the penalty should be at the lower end of the scale being no more than 10% of the affected turnover, being an amount of [redacted].

Step three: where the contravention exceeds one year, multiplying the amount obtained in step 2 by the duration of the contravention

334. The alleged contravention endured for thirteen days, therefore there is no need to multiply the base amount.

[276] Dis-Chem's Answering Affidavit, paragraph 25 and **Annexure RG 14** thereto, page 77 and 212 of the Pleadings Bundle.

Step four: rounding off the figure obtained in step 3, if it exceeds the cap provided for by section 59(2)

335. The base amount of [redacted] does not exceed the 10% of Dis-Chem's annual turnover for the immediately preceding financial year.

Step five: considering factors that might mitigate or aggravate the amount reached in step 4, by way of a discount or premium expressed as a percentage of that amount that is either subtracted from or added to it

336. Although the Commission accuses Dis-Chem of excessive pricing and exploiting its mask customers, at no stage did Dis-Chem extract unfair super-profits or excessive margins by exploiting its customers. Dis-Chem's reaction to the drastic and urgent changes in the demand and supply of surgical masks has been to deal with these consistent with its normal business practices: ensure sustainable supply to its customers at competitive prices. This is evident by Dis-Chem's sourcing and pricing behaviour. When inputs costs increased, Dis-Chem increased its prices and held prices below those charged by its competitors. Where Dis-Chem has managed to secure supply at more favourable prices, it decreased its sales prices of masks.

337. In addition, Dis-Chem co-operated fully with the Commission during its investigation. Its legal team offered to meet with the Commission in the week of 20 April 2020 (prior to any referral) to explain again and in greater detail the justifications for Dis-Chem's price adjustments on masks, but the request was rebuffed.

338. In light of the efforts by Dis-Chem to meaningfully engage with the Commission on the case and by taking steps to lower the prices of masks as costs have come down, Dis-Chem's efforts warrant a further 30% reduction to the base amount of [redacted], resulting in a penalty amount of [redacted]

***Step six**: rounding off this amount if it exceeds the cap provided for in section 59(2). If it does, it must be adjusted downwards so that it does not exceed the cap*

339. The maximum amount of an appropriate penalty in the facts and circumstances of this case is an amount of no more than [redacted] which does not exceed 10% of Dis-Chem's annual turnover for the immediately preceding financial year.

CONCLUSION

340. For all of the reasons set out above, and placed before the Tribunal in evidence by Dis-Chem, the complaint referral does not establish any contravention of section 8 of the Act, read with regulation 4.

341. It should be dismissed in its entirety.

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