COMPETITION TRIBUNAL
REPUBLIC OF SOUTH AFRICA

Case no. 66/IR/May00

In the matter between

JJP Bezuidenhout **Claimant**

and

Patensie Sitrus Beherend Limited **Respondent**

DECISION ON APPLICATION FOR INTERIM RELIEF IN TERMS OF SECTION 59 OF THE COMPETITION ACT, 89 OF 1998

Introduction

1. This is an application for interim relief brought by an eastern Cape citrus farmer, Mr JJP Bezuidenhout, against local Gamtoos River Valley citrus packing and distribution company, Patensie Sitrus Beherend Limited ("Patensie Sitrus"). Mr Bezuidenhout alleges that certain provisions of Patensie Sitrus's articles of association contravene the Competition Act in that they lock farmers, who are shareholders in the company, into an exclusive supply arrangement with Patensie Sitrus, thus excluding potential competitors from the market for the packing and distribution of citrus fruit in the Gamtoos River Valley.

2. Until July 1998 Patensie Sitrus had conducted its packing and distribution operations as a co-operative under the Co-operative Society's Act before being converted to a company following the repeal of the Marketing Act 59 of 1968, in 1996. The Marketing Act, which was the key statute underpinning single-channel marketing in South Africa's agricultural sector, was repealed by the Marketing of Agricultural Products Act 47 of 1996 in an attempt to promote competition in the marketing of agricultural products. This objective is unequivocally confirmed by a reading of the Hansard record of the parliamentary debate at the time of the repeal of the old act and the introduction of the new bill. The then Minister of Agriculture made it clear that the anti-competitive practices with which he was principally concerned derived from the actions of monopsonistic processors; that is dominant purchasers of agricultural produce for the purpose of further processing and marketing. Declaring that 'the days of single channel marketing, fixed prices and control board domination are over', the Minister went on to state that 'I look forward to taking initiatives, through the legislation at my disposal and in co-operation with the Minister of Trade and Industry, to ensure that there are no unreasonable concentrations of power in the marketing chain between the producer and the consumer'(Hansard, 13 September 1996, 4358). This concern was shared by other speakers in the parliamentary debate. We note this in order to provide the context for subsequent developments in the agricultural sector. It appears that certain of the processors responded to

the legislature's intervention by establishing companies whose articles of association enshrined precisely the practices complained of in the legislature. In the short lifespan of the Competition Tribunal, we have already encountered this with respect to two important segments of the agricultural sector, namely, in an earlier matter involving the raisin industry, part of the larger dried fruit industry, and now in part of the citrus industry.

3. This application for interim relief follows an earlier High Court application by Patensie Sitrus in which it sought an urgent interdict compelling Mr Bezuidenhout and another citrus farmer, Mr JD du Preez, to comply with their contractual supply obligations in terms of the company's articles of association. The two farmers wanted to sell their fruit to an alternative packer, which, they maintained, had offered them a better price than the price they would receive from Patensie Sitrus. They therefore attempted to terminate their relationship with Patensie Sitrus, arguing that the purported limitations contained in the articles of association did not restrict their right to sell their shares and thus win their freedom to supply their produce to whomever they chose. In addition, they contended that the particular provisions of the articles were anti-competitive in terms of the Competition Act, 89 of 1998. The court found in favour of Patensie Sitrus but, as it recognised the possibility that the relevant provisions in the company's articles may be anti-competitive, the court limited its order to preserving the *status quo* between the parties in the interim pending a referral of the matter to the Competition Tribunal for adjudication of the competition aspects which the farmers had raised, in terms of Section 65(2)(b) of the Competition Act.

4. Mr Bezuidenhout and Mr Du Preez filed a joint Complaint Referral with the Competition Tribunal on 26 May 2000, pursuant to the High Court's order. Having previously lodged a complaint with the Competition Commission in terms of Section 44, they filed an application for interim relief in terms of Section 59 simultaneously with their Complaint Referral. It is this application for interim relief that we must rule on in these proceedings; the Complaint Referral is not yet ripe for hearing.

5. Mr Du Preez subsequently reached a settlement with Patensie Sitrus, leaving Mr Bezuidenhout as the sole claimant before the Tribunal. According to the draft order annexed to the claimant's Notice of Motion, he is asking us for an interim order declaring the alleged anti-competitive provisions of the articles of association null and void, pending the conclusion of a full investigation into these allegations by the Competition Commission.

Finding and order

6. The respondent raised a number of points *in limine* at the hearing of this matter. We dismissed each of these points for the reasons that follow below.

7. We also found that there is sufficient evidence that –

   (a) certain provisions of the respondent's articles of association have the effect of substantially preventing or lessening competition in the relevant market and therefore constitute a prohibited practice in terms of Section 5(1); and

   (b) the respondent is abusing its dominance by engaging in the exclusionary act of requiring or inducing a supplier to not deal with a competitor, as contemplated in Section 8(d)(i).

8. In addition, we found that the other requirements for granting interim relief specified in Section 59(1) have been met.

9. We accordingly allowed the application for interim relief and made the following order:

The claimant's application for interim relief in terms of Section 59 of the Competition Act 89 of 1998 is granted in respect of the respondent's alleged contravention of Sections 5(1) and 8(d)(i) of the said Act.

The Competition Tribunal orders that –

1. the respondent is interdicted and restrained from enforcing its option to purchase the claimant's citrus crop in accordance with Article 112 of the respondent's Articles of Association, and from fining the claimant in terms of Article 112.6.3, or imposing any other remedy against the claimant, for not complying with Article 112;

2. this order remains in force until the earlier of -

(a) the conclusion of the hearing into the prohibited practices alleged by the claimants to have been committed by the respondents; or
(b) the date that is six months after the date of the issue of this order;

3. the respondent is ordered to pay the claimant's costs in the application on the scale as between party and party, including the costs of one counsel and one attorney.

10. Our reasons for finding in favour of the claimant and for making the above order follow below.

Reasons

Points in limine

Final adjudication by the Competition Tribunal

11. The respondent's first argument *in limine* was that the claimant could not at this stage approach the Tribunal for interim relief only, because the High Court had referred the matter to the Tribunal for **final** determination of the dispute between the parties in terms of section 65(2) of the Act.

12. It is true that a referral to the Tribunal in terms of Section 65, read with the relevant rules in Part 4 (Division A) of the Tribunal Rules, contemplates a final determination by the Tribunal. But this does not mean that a party that obtains a Section 65 referral from the High Court cannot also approach the Tribunal for interim relief in terms of Section 59. Provided the claimant has lodged a complaint with the Competition Commission it is entitled at any time to bring an interim relief application in terms of Section 59. As the claimant correctly pointed out at the hearing, this can give rise to two parallel proceedings being brought before the Tribunal, as in the present case – the one being a referral in terms of a Section 65, and the other being an interim relief application in terms of Section 59.

13. What was brought before us at the hearing on 28 June 2000 was an application for interim relief. If we are satisfied that the claimant has succeeded in establishing the requirements laid down in Section 59 we are competent to grant interim relief. We need not concern ourselves in these proceedings with the status of the referral from the High Court. Neither do we have to consider the status of our interim order in relation to the High Court's order. The claimant has asked us for an interim relief order and that is what we have granted. Having done so, our function is complete.

Conflicting orders

14. The second point *in limine* submitted by the respondent was that the Tribunal has no power to grant the relief sought in terms of this application because such relief would be in direct conflict with the High Court's order, which upheld the enforceability of the respondent's articles of association. According to the respondent, the Tribunal has no power to set aside an order of the High Court because the Tribunal is a creature of statute – the Competition Act – and the Act confers no such power on it.

15. On this point the claimant persuasively argued that an order of the Tribunal in terms of Section 59 would not conflict with the High Court's order. The High Court decided the matter on the contractual relationship between the parties as contained in the respondent's articles of association. It did not consider whether the contractual rights and obligations contained in the articles of association contravened the Competition Act. For this enquiry, the judge referred the matter to the Competition Tribunal, which, along with the Competition Appeal Court, has exclusive jurisdiction in terms of Section 65(3) to assess whether the relevant provisions in the respondent's articles of association constitute prohibited practices in terms of Chapter 2 of the Act, and whether the circumstances of the case justify an order for interim relief in terms of Section 59 (Chapter 6). In other words, the criteria we must use to evaluate the merits of the claimant's application are different to the criteria that the High Court used in its evaluation. Consequently, the order we have made on competition grounds does not contradict the existing High Court order.

Declaration as Interim Relief

16. The third *in limine* objection raised by the respondent was that the claimant is seeking a declaratory order as interim relief. A declaratory order which strikes down the relevant provisions in the articles of association, would, in the respondent's submission, constitute a legal and logical anomaly as it was impossible for the articles to be void in the interim only.

17. The claimant in turn insisted that the draft order it had submitted was not in effect a final declaratory order camouflaged as an interim order. Counsel for the claimant explained that the claimant did not require the relevant portions of the articles of association to be struck down. Instead the claimant sought an order declaring those provisions inoperative for a limited period only pending finalisation of the hearing into the complaint currently being investigated by the Competition Commission.

18. The order we have made in this case does not strike down the relevant provisions – it is couched as an interim interdict, and therefore in our opinion does not fall foul of the respondent's objection.

Non-joinder of certain interested parties

19. As a fourth point *in limine*, the respondent claimed that the matter could not proceed on the day of the hearing as the other shareholders in Patensie Sitrus would be directly affected by the requested order and should therefore be joined in the application. Counsel for the respondent contended that if the relevant articles were declared void they would cease to govern the relationship between the company and other shareholders as well, with the effect that the company would not be bound by them even in cases where these other shareholders wished to hold the company to them, which would lead to possible prejudice to these other shareholders. The respondent accordingly asked us to stay the proceedings until the other shareholders had been afforded an opportunity to make representations to the Tribunal.

20. The issue of non-joinder was considered at some length by a panel of this Tribunal in *Cancun Trading No. 24 CC and others v Seven-Eleven Corporation SA (Pty) Ltd* (Case no. 18/IR/Dec99) in circumstances very similar to these. We concur with the finding of that panel that "(t)he Tribunal … has no power or jurisdiction to dismiss the case … on the basis of non-joinder because its rules do not provide for it to do so"[1]. The panel based this conclusion on the following reasoning: "The Tribunal Rules are silent on the issue of dismissal of matters for non-joinder and regard to the High Court Rules is similarly unhelpful as these rules also do not cover the issue. The Tribunal cannot refer to any other statute or jurisprudence regarding this matter since Rule 54 only gives the Tribunal powers to consider High Court Rules in instances where the Tribunal Rules do not provide answers." This reasoning would apply equally in the present request for postponement pending joinder of the other shareholders.

21. The respondent criticised this approach and argued that the common law principle of joinder applies to the Tribunal as well, irrespective of its status as a creature of statute. In support of its argument, the respondent pointed out that the common law principle of joinder applies to Magistrates' Courts, who are also creatures of statute, despite the fact that their empowering statute and rules do not explicitly provide for it.

22. We need not, however, go into the merits of this argument, as we are convinced that even in terms of the common law joinder is unnecessary in this case. As pointed out in the *Cancun Trading* case, the common law right of a defendant to raise non-joinder is limited[2]. The courts have restricted this right to persons who have a direct and substantial legal interest in the subject-matter of the litigation, as opposed to a mere commercial or financial interest[3].

23. We do not think that the other shareholders in Patensie Sitrus have such a legal interest in this matter, as we have couched our order in such a way as to restrict its effects, as far as possible, to the claimant. The restraint we have placed on the respondent only extends to its relationship with the claimant. As such, the only impact that the order may have on the other shareholders is indirect, via its possible effect on the financial position of the company, and even that impact should be small. It is noteworthy that the respondent failed to bring to our attention any authority for the proposition that a shareholder instituting legal action against the company concerned must join all the other shareholders.

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[1] At paragraph 18 of the majority decision in the Cancun Trading case. For the analysis that led the panel to this conclusion refer to paragraphs 11 to 18 of the majority decision.

[2] See for instance Paterson: Eckard's Principles of Civil Procedure in the Magistrates' Courts (3rd Edition) at p. 182.

[3] See paragraph 20 of the majority decision in the Cancun Trading case, and *Pillay v Harry & Others* 1966 (1) SA 801 (D) at 804C-E.

24. In the alternative, the respondent contended that joinder of the other shareholder in this case rested on the constitutional principle of just administration, which encompasses, among others, the principle of *audi alteram partem*. It argued that the Tribunal, by virtue of its status as an administrative tribunal in the mould of the former Industrial Court, was constitutionally enjoined to apply the rules of natural justice.

25. The panel of the Tribunal in the *Cancun Trading* case accepted that the Tribunal must comply with the rules of natural justice, but pointed out, in our view correctly, that "it requires a logical leap of faith to infer a common law rule on joinder from the principles of natural justice" for which the respondent in that case had provided no authority. The panel proceeded to point out that natural justice and the doctrine of joinder deal with two distinct situations. Natural justice is about fairness to the parties who are already participating in the proceedings, while the High Court doctrine of joinder is about who should be joined.

26. Moreover, the authorities cited by the respondent in support of its contention that joinder of the other shareholders is required by virtue of the principle of *audi alteram partem* do not assist its argument. They do no more than confirm the approach of the panel in the *Cancun Trading* case[4].

27. We have accordingly concluded that this *in limine* objection is without merit.

Section (3)(1)(d)

28. The respondent's final point *in limine* relied on the recent judgment of Ngoepe JP in *SAD Holdings Ltd and Another v South African Raisins (Pty) Ltd* [2000] 2 ALL SA 326 (T) in the Transvaal Provincial Division of the High Court. The court in that case set aside the Tribunal's interim relief order in *South African Raisins (Pty) Ltd v SAD Holdings Ltd* 04/IR/Oct00 (unreported) on the basis that Section 3(1)(d) of the Competition Act had excluded the subject matter of the claimant's interim relief application from the jurisdiction of the Tribunal. Section 3(1)(d) excludes from the ambit of the Competition Act all "acts subject to or authorized by public regulation". The court found that the Marketing of Agricultural Products Act 47 of 1996 created a separate regulatory regime for certain agricultural products, including grapes and raisins, which, in terms of section 3(1)(d), placed the activities of SAD beyond the jurisdiction of the Competition Act.

29. The respondent argued that the High Court's judgment in the *South African Raisins* case applied directly to the facts in this case. It argued that the 'acts' complained of in the present application related to citrus products, which form part of the category of products that fall within the regulatory scope of the Marketing of Agricultural Products Act, and are therefore not actionable before us under the Competition Act.

30. The claimant presented us with a convincing counter argument on this point. His counsel argued that Ngoepe JP's decision in the *South African Raisins* case does not establish a precedent which binds us in

[4] *South African Technical Officials Association v President of the Industrial Court and Others* (1985 (1) SA 597(A)) merely confirms the status of the erstwhile Industrial Court as an administrative tribunal; *Morali v President of the Industrial Court and Others* (1987 (1) SA 130 (C)) did no more than confirm the principle that an administrative tribunal has a discretion to permit **a party** before it to be represented if representation is reasonably required to afford the party a fair opportunity of presenting its case.

this case. We agree with this argument. Ngoepe JP's decision[5] does not represent the current law on this point in the eastern Cape where the parties to this dispute and the subject matter of this dispute are located. This is because the local division of the High Court in that area (South-Eastern Cape Local Division) has ruled on this issue subsequent to judgment in the South African Raisins case and has not followed the judgment in that case. In Patensie Sitrus's application in the High Court to enforce its articles of association against the present claimant, Mr Bezuidenhout (Case no. 682/2000 – unreported), the court considered Ngoepe JP's decision in the *South African Raisins* case, but nevertheless decided to refer the matter to the Competition Tribunal, thus indicating that the Competition Act was indeed relevant to the dispute between the parties. The law on this point in the eastern Cape is thus at variance with that in Gauteng.

31. At any rate, we do not agree with the argument that Section 3(1)(d) excludes our jurisdiction in this case. The 'act' that we have found to be a prohibited practice in this case is Patensie Sitrus's enforcement of those provisions of its articles of association that compel the claimant to deliver his citrus produce to the company in perpetuity unless the directors of the company permit him to sell his shares in the company, a decision in respect of which they have an unfettered discretion. The regulatory regime established by the Marketing of Agricultural Products Act does not regulate this 'act'. It is consequently not an "act subject to or authorized by public regulation" as contemplated in Section 3(1)(d) of the Act.

Interim Relief

32. Having dismissed the respondent's points *in limine* for the reasons set out above, we will now deal with the merits of the application for interim relief.

33. The Tribunal may grant an interim relief order after considering the parties' representations if it is satisfied that the following three requirements have been met: that a restrictive practice exists; that, if the order is not granted, the claimant will incur irreparable harm or the purposes of the Act will be frustrated; and that the balance of convenience favours the granting of the order.

34. For ease of exposition, we first deal with the second and third requirements before proceeding with the assessment of whether a restrictive practice exists in this case.

<u>The order is reasonably necessary to prevent serious irreparable damage:</u>

35. The claimant asserted that he would suffer irreparable damage if we did not grant the order. He claimed that the damage he would suffer as a result would arise from his having to breach existing contracts for the supply of citrus that he had entered into and from the lower prices he would realise if he were compelled to deliver to the respondent.

36. We are satisfied that the order we have made is necessary to prevent the claimant from suffering irreparable damage. As in the *South African Raisins* case referred to above, we do not base this conclusion on only the direct financial losses that the claimant stands to incur as a result of breaching his forward contracts or the lower prices that he will realise from the respondent, as these losses can, in our

[5] Incidentally, this decision is being appealed to the Supreme Court of Appeal and has already been criticised in *obiter* remarks by that court in both the majority and minority judgments in *Standard Bank Investment Corporation Limited v Nedcor Limited* (Case no. 44/2000 – unreported).

assessment, be recovered without too much difficulty in a subsequent action for damages. Rather, the irreparable damages we envisage the claimant will suffer relate to the harm that the breach of his forward contracts will cause to his reputation.

Alternatively, the order is reasonably necessary to prevent the purposes of the Act being frustrated:

37. Perhaps more importantly in this case, we are of the view that the claimant's failure to successfully challenge the dominant pack house will discourage other farmers in the community from taking a stand against the respondent. These farmers/shareholders are vulnerable to severe penalties if they fail to meet their commitments in terms of Patensie Sitrus's articles of association and the claimant's failure, even if only at interim, would have them scuttling back into line thus reducing the possibility of these practices ever being subjected to full scrutiny by the competition authorities. We accordingly conclude that the order we have made in this application is reasonably necessary to prevent the purposes of the Act being frustrated.

The balance of convenience favours the granting of the order:

38. Given the fact that we have restricted our order to the claimant alone, we are convinced that the balance of convenience favours it being granted. Our granting the order clearly assists the claimant, who would otherwise stand to suffer extensive damages, while its effect on the respondent, we expect, will not be severe at all; it will only affect its supply arrangement with one of its many shareholders.

Restrictive Practices:

39. The substance of the claimant's case is that certain of the provisions of the respondent's articles of association contravene Section 5(1) and Section 8(d)(i) of the Competition Act.

40. Section 5(1) prohibits an agreement between parties in a vertical relationship if the agreement has the effect of substantially preventing or lessening competition in a market, unless a party to the agreement can prove technological, efficiency and other pro-competitive gains resulting from that agreement that outweigh the anti-competitive effect.

41. Section 8(d)(i) prohibits a dominant firm from requiring or inducing a supplier or customer to not deal with a competitor, unless the firm concerned can show technological, efficiency or other pro-competitive, gains which outweigh the anti-competitive effects of the act.

42. The claimant's contention is that it is the interplay between a number of provisions in the respondent's articles of association that gives rise to the reduction of competition and to the exclusionary practices that he complains about. The key provisions in this regard are Articles 7, 30, 109, 110, 112, 114.3.1, 114.3.2 and 114.3.5.

43. In terms of Article 112, each shareholder of the respondent company grants the respondent a first right and option to annually purchase the member's whole citrus crop, or such part of the crop that the respondent may choose. The shareholders are obliged to submit a crop estimate on the respondent's request, normally a few months before the fruit is ready for picking. The respondent then annually prescribes a delivery schedule according to which the shareholders must deliver their fruit to its packing facility. The respondent may fine shareholders who do not comply with these obligations in accordance

with a defined formula in terms of Article 112.6. Article 30 provides that if a shareholder wishes to 'resign' as a producer, he remains liable for a *pro rata* portion of the company's financial commitments. In addition, Article 114.3.1 entitles the respondent to apply for an urgent interdict to prevent a shareholder from delivering his fruit to anyone other than the respondent, while Article 114.3.2 entitles the respondent to issue summons for specific compliance by shareholders and to recover fines imposed on shareholders. Over and above this, Article 114.3.5 allows the respondent to set off any fines that it may have imposed on a shareholder against any amount owing by the respondent to the shareholder.

44. The claimant argues that the interplay between these exclusive supply provisions and certain other provisions that restrict the sale of the farmer's shares in the respondent (Articles 7, 109 and 110) exacerbates the restrictive effects of the exclusive supply aspect of the arrangement. For instance, Article 7 subjects the transferability of shares to the unfettered discretion of the directors of the respondent – if they refuse permission the shares may not be sold.

The Relevant Market

39. As always, the first step in an inquiry into an alleged restrictive practice, is determining the relevant market. As pointed out by a panel of this Tribunal in the *South African Raisins* case (Case no. 04/IR/Oct99), the relevant market is the narrowest market at a given stage of the supply chain in which a hypothetical monopolist operating at that level could exert a significant degree of market power.

40. The parties in the present application disagree about the stage of the supply chain in which the relevant market is situated in this matter. On the one hand, the claimant contends that the relevant market is situated at that stage of the supply chain in which the claimant and other farmers/shareholders sell their produce to pack houses for packing and distribution to the next stage of the supply chain. On the other hand, the respondent insists that the market is situated further downstream – in its view the relevant market must be defined with reference to the end user. In this regard the respondent made much of the fact that the price paid by the respondent to farmers/shareholders for their fruit is a function of the price that the respondent obtains for the fruit further down the supply chain.

41. In our view, there is no basis for the respondent's contention that the relevant market be defined with reference to the final consumers of the product. It is not in this downstream market that the alleged anti-competitive practices are being committed. Moreover, the respondent's lack of market power in the downstream market has no bearing on its ability to exert market power in the upstream market in which it purchases fruit from farmers for packing and distribution. This upstream market is clearly a distinct market for purposes of our inquiry.

42. The discord between the parties on the appropriate location of the relevant market within the supply chain necessarily impacts on their assessment of the geographic dimensions of the relevant market. In this regard the claimant asserts that the market is limited to the Gamtoos River Valley, but provides no evidence to support his assertion. He merely states that the market is localised – i.e. the Gamtoos River Valley – because the claimant sells his produce in the valley and the respondent, whose packing and other facilities are located in the valley, purchases produce from local suppliers. But this cannot be the basis on which the geographic boundaries of the relevant market are determined. The geographic market must be determined with reference to the choices that farmers in the Gamtoos River Valley have in respect of the packing and distribution of their fruit. The relevant market would be the Gamtoos River Valley only if a hypothetical monopsonist packing facility located in the valley could exert a significant

degree of market power over citrus farmers in the valley. And this would only be the case if farmers in the valley did not have the choice of supplying their produce to other packing facilities outside the valley, due to, for instance, prohibitive transport costs. If they were able to deliver to pack houses outside the valley, they would not be a captive market and the hypothetical monopsonist in the valley would not be able to exert any market power over them. The claimant failed to provide any evidence on this point.

43. The claimant's assertion in this regard was, however, confirmed by the respondent, albeit inadvertently. In protesting the claimant's narrow market delimitation, the respondent stated in its answering affidavit that there is no reason why a farmer in Patensie or in the Gamtoos River Valley cannot deliver his fruit to a packing facility outside the valley, **except for economic considerations such as transport costs**. The respondent made this submission in support of a broader market – the whole of South Africa – but in qualifying the statement it in effect admitted that the cost of transporting fruit to alternative packers is a localising factor. In fact transport costs are precisely what delimits one geographic market from another. We accept the respondent's contention that, under exceptional circumstances, it may purchase fruit from producers outside the Gamtoos River Valley. A local drought was cited as one such exceptional circumstance. However, this does not weaken our conclusion – indeed it serves to confirm it. Under these exceptional circumstances, local output cannot satisfy the respondent's requirements. It is then threatened with the prospect of operating its facilities at sub-optimal scale and it faces the prospect of not being able to meet its contractual obligations to its own customers. In these circumstances the relative significance of the transport costs decline. However, under normal circumstances they are clearly of sufficient commercial significance to localise the geographic market for citrus.

44. Based on the above, we accept the relevant market to be **the market for the purchasing of citrus fruit in the Gamtoos River Valley for packing and onward distribution**. By accepting this to be the market, we are not saying that the geographic boundaries of the market have been crisply delineated; we cannot rule out that some of the farmers on the fringe of this area may be able to supply to packing facilities outside the market as we have delineated it, either on a sustained basis or intermittently as circumstances allow. But, we are prepared to accept this geographic market to be a reasonable approximation of the relevant market in this matter.

<u>Prohibited practice in terms of Section 5(1)</u>

45. To find for the claimant under Section 5(1) of the Act, we must be satisfied that –

    (a) an agreement exists between the parties;
    (b) the parties are in a vertical relationship;
    (c) the agreement between them substantially prevents or lessens competition in the relevant market we have defined above.

46. The first element is not in dispute. It is common cause that the respondent's articles of association constitute an agreement between the claimant and respondent.

47. The respondent disputes that the second element is present in this case. It argues that nothing in the articles of association is indicative of a vertical relationship between the parties as the articles merely provide for the performance of certain contractual obligations by both parties – i.e. "respondent agrees and undertakes to re-sell citrus provided to it by its members and the members undertake to effect such

delivery as may be indicated" (Paragraph 13.3.2 of the respondent's heads of argument). In addition, the respondent submits that all the shareholders are parties to the articles of association, which means that the articles constitute a contract between the members, and can therefore not establish a vertical relationship.

48. We find these arguments to be wholly unconvincing. It is clear that the respondent purchases fruit from the claimant and other shareholders in terms of its articles of association and that it then packs and distributes and onward-sells the fruit downstream. This is sufficient to establish that a vertical relationship exists between the parties.

49. This brings us to the final element: do the articles of association substantially prevent or lessen competition in the relevant market? We believe they do. The provisions of the articles of association highlighted above have the effect of 'locking in' farmers who are shareholders of the respondent in an exclusive supply agreement. They make it very difficult, if not impossible, for the claimant or any of the other shareholders, to supply to any other competing packing facility. This results in the respondent being able to exert market power in the relevant market. The respondent denies this, citing the fact that it does not control the price it pays to its shareholders for their citrus, as this price is determined with reference to the price that it is able to realise in the downstream market.

50. The fact that the price which the respondent pays the claimant and other shareholders for its key input, fruit, is a function of the ultimate price obtained by the respondent further down the supply chain is of no moment in this regard. This mode of doing business does not mean that the respondent is not able to behave appreciably independently of competitors and/or control prices (i.e. exert market power) in the market in which it purchases fruit from its shareholders. It simply means that one factor in setting the price at which it purchases fruit, namely the price it obtains downstream, is beyond its control. Other factors such as input costs and the company's level of productivity are still very much under its control. That it chooses to mechanistically set the price of its key input, namely fruit, as a proportion of the price it must take in the separate downstream market simply reflects a business choice. It is precisely because the price of fruit as an input is determined by a formula devised by the purchaser of the input rather than by the process of competition that we hold that the respondent has market power.

51. This arrangement also has efficiency consequences insofar as the absence of competition in the market for the critical input lowers the incentive on the respondent to keep its other production costs low. That is, were it obliged through the process of competition to offer a higher price for this input than it desired and it found, in consequence, that its profit margins were being squeezed, its rational response would be to increase efficiency. This incentive is absent in the present arrangement.

52. The respondent would have us believe that the arrangement between itself and its shareholder/producers merely constitutes a type of forward contract between them in terms of which the shareholder/producers undertake to deliver their produce to the company at a later date. It submitted that forward contracts are a commonly accepted, and indeed necessary, risk-hedging instrument in commodity markets that should clearly not be considered anticompetitive. Indeed, the expert report (an affidavit by agricultural economist, Dr CJ Auret) submitted in support of the respondent's opposition to this application, described forward contracts as "the backbone of transactions in the agricultural commodity markets".

53. Of course, forward contracts are not *per se* anticompetitive. They are an important mechanism for producers to hedge themselves against future adverse movements in price by selling their next harvest at

current prices. For the pack house/processor/distributor, the benefit of entering into a forward contract with producers is that it assures the pack house of delivery of the agreed volumes of produce at the agreed price, which allows it in turn to conclude back-to-back forward contracts with parties further down the supply chain. However, the price-hedging benefit of a forward contract is denied to the farmers/shareholders by the present arrangement in which the price they receive is a function of the final price further downstream and other input costs. Moreover, the articles of association bind the farmers in perpetuity. Indeed, they permanently entrench the benefits of a forward contract to the respondent, without the concomitant benefits for producers normally contained in forward contracts. It is thus clear that the arrangement between the respondent and its shareholders cannot simply be equated with a forward contract. Had the arrangement between the claimant and respondent been a regular forward contract, we would not have taken issue with it. It is noteworthy in this regard that the claimant made his intentions not to deliver his crop to the respondent known at an early stage – at the time when the respondent would have entered into negotiations in respect of forward contracts with downstream parties – so that his actions cannot be dismissed as an attempt to avoid his commitments under a normal forward contract. He simply exercised his competitive choice not to enter into a forward contract with the respondent in respect of the forthcoming season.

54. Consequently, as the respondent made no attempt to justify its business practices by showing technological, efficiency or other pro-competitive gains, we conclude that its articles of association establish a prohibited practice in terms of Section 5(1).

Restrictive Practice in terms of Section 8(d)(i)

55. A Section 8 violation can only be established if the respondent is dominant in the relevant market. In terms of Section 7, the respondent is deemed to be dominant if it has at least 45% of the market. It is also deemed to be dominant if it has less than 45% of the market, but at least 35%, unless it can show that it does not have market power, as defined in Section 1. If the respondent has less than 35% of the market, it must be proved that it indeed has market power.

56. The claimant alleges in his founding papers that the respondent controls the purchase, packing and sale of approximately 50% of the citrus produced in the Gamtoos River Valley, which we have accepted to be the relevant market in this matter. But again, the claimant provides no substantiation for this claim. He is nevertheless fortunate in that the respondent does not dispute it. In fact, the respondent goes so far as to admit that it "without doubt" packs and markets more than 50% of the citrus produce in the Gamtoos River Valley. This puts the respondent's share of the market well above the 45% threshold, above which we can accept its dominance.

57. Next we must determine whether the respondent is engaging in an exclusionary act in that it requires or induces its suppliers to not deal with a competitor. 'Exclusionary act' is defined in Section 1 of the Act as "an act that impedes or prevents a firm entering into, or expanding within, a market". The provisions in the respondent's articles of association which we highlighted above without doubt serve to induce farmers, who are shareholders in the respondent, not to deal with the respondent's competitors – in fact they go even further than that as they require exclusivity from these producers. Moreover, we are convinced that this arrangement would make it more difficult for new entrants to enter the market, as well as for existing packing sheds to expand in the market, as they would not easily, or at all, be able to woo producers away from the respondent by offering higher prices for their produce.

58. We consequently find that the respondent has contravened Section 8(1)(d).

Costs

59. Since we have granted the claimant's application, we are justified in making a costs order in his favour.

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D.H. Lewis **Date:**

Concurring: D.R. Terblanche and P.E. Maponya