

ECONOMIC DEVELOPMENT DEPARTMENT

NO. 1424

21 DECEMBER 2018

REQUEST FOR PUBLIC COMMENT ON THE FIRST DRAFT SET OF BUYER POWER REGULATIONS IN TERMS OF THE COMPETITION ACT, 1998 (ACT NO. 89 OF 1998) AND THE COMPETITION AMENDMENT BILL, 2018 [B 23B-2018]**Background**

In my address to the National Assembly at the Second Reading Debate on the Competition Amendment Bill, 2018 [B 23B-2018] (the “Bill”) on 23 October 2018, I announced the establishment of a Panel which would draft regulations to give effect to the Bill once it has been passed by Parliament. It was further announced that these regulations would be the subject of consultation with the public and the Competition Commission (the “Commission”), in line with the proposed amendments to section 78 of the Competition Act (Act. 89 of 1998) (the “Act”).

Following the approval of the Bill by the National Council of Provinces on 4 December 2018, the Panel has concluded its preliminary work on a first draft set of regulations to give effect to the amendments in section 8 of the Act, regarding Buyer power.

Clause 5 of the Bill has introduced a new subsection 8(4) to the Act, which states it is prohibited for a dominant firm in a sector designated by the Minister in terms of paragraph 8(4)(d) to directly or indirectly, require from or impose on a supplier that is a small and medium business or a firm controlled or owned by historically disadvantaged persons, unfair—

- (i) prices; or
- (ii) other trading conditions.

Clause 5 of the Bill has further provided for regulations made by the Minister in terms of section 78 of the Act—

- (i) The factors and benchmarks for determining whether prices and other trading conditions imposed are unfair;
- (ii) The sectors to which subsection 8(4) will apply; and
- (iii) In respect of firms owned or controlled by historically disadvantaged persons, the benchmarks for determining the firms to which subsection 8(4) will apply.

The attached first draft set of regulations provides the initial thinking by the Panel on the general approach to determining the appropriate factors and benchmarks to give effect to the amendments to subsection 8(4).

Call for public comment

I hereby call on interested parties to provide representation and comment on these first draft set of regulations, including comment on (i) the general approach to the regulations; (ii) the specific wording used in the regulations; and (iii) any preferences for the options which have been presented in the regulations.

Specifically, comment is sought (i) from large firms as to whether the first draft set of regulations provides sufficient guidance regarding the practices which the Commission may investigate as a prohibited practice under subsection 8(4); (ii) from small and medium firms as to whether the first draft set of regulations sufficiently captures the range of abuses which small and medium firms may suffer as a result of abuse of buyer power; and (iii) from interested parties as to whether the first draft set of regulations sufficiently addresses the changes in industries as a result of technological shifts, in particular those relating to the Fourth Industrial Revolution.

Process to be followed

In making the proposed Buyer Power Regulations, I intend to follow the following process:

Step 1 (this step): A first draft set of regulations is hereby published in order to begin an initial consultation on the proposed Buyer Power Regulations prior to the President's assent to the Bill and its subsequent proclamation. Representation and comment should be made by 31 January 2019 in fulfilment of this step of the process.

Step 2: Following the conclusion of the public comment period, the Ministry intends to host a set of forums with firms, including large firms and small and medium firms, which may be impacted by the proposed amendments to subsection 8(4) of the Act. Any firm who wishes to be considered for participation in these forums should write to the Minister by 15 January 2019 to advise of its interest.

Step 3: Following assent of the Bill by the President; promulgation of the relevant sections; and conclusion of the Steps 1 and 2 above, a further second draft set of regulations will be published for public comment.

Step 4: Once this Step 3 has been completed it is expected that a final set of Buyer Power Regulations will be published, taking into account the public comments, accompanied by promulgation of the amendments to subsection 8(4) of Act.

The process outlined above is thus intended to allow for a collaborative and open process regarding the publication of the final regulations to enable the maximum participation by affected parties.

Representation and comments, and requests to be considered for participation in any forums on the regulations, should be made by 31 January 2019 and should be addressed to the Minister of Economic Development, for the attention of Ms MT Mushi, Email: ministry@economic.gov.za, Economic Development Department, Private Bag X149, Pretoria, 0001 or hand delivered at 77 Meintjies Street, Block A, Utangamari Building, 3rd Floor, Sunnyside, 0132.

**Enquiries: Ms MT Mushi
Tel: 012 394 3458**

Closing date: 31 January 2019



**EBRAHIM PATEL
MINISTER OF ECONOMIC DEVELOPMENT**

BUYER POWER REGULATIONS

FIRST DRAFT SET FOR PUBLIC COMMENT NOTE: Reference to the Competition Act in these draft Regulations refers to the version of the Act passed by the National Council of Provinces on 4 December 2018.

1. Short Title

1.1. These Regulations may be cited as the *Buyer Power Regulations*.

2. Interpretation

2.1. A word or expression that is defined in a chapter of the Act bears the same meaning in these Regulation as in the Act.

2.2. In these Regulations,

2.2.1. a reference to a section by number refers to the corresponding section of the Act;

2.2.2. a reference to a Regulation by number refers to the corresponding item of these Regulations; and

2.2.3. a reference to a sub-rule or paragraph by number refers to the corresponding item of the Regulations in which the reference appears.

2.3. In these Regulations unless the context indicates otherwise, "Act" means the Competition Act, 1998 (Act No. 89 of 1998), as amended from time to time.

3. Purpose

3.1. In terms of subsection 8(4)(a) of the Act, it is prohibited for a dominant firm in a sector designated by the Minister in terms of paragraph (d) to directly or indirectly, require from or impose on a supplier that is a small and medium business or a firm controlled or owned by historically disadvantaged persons, unfair—

3.1.1. prices; or

3.1.2. other trading conditions.

3.2. In terms of subsection 8(4)(d) of the Act, the *Minister* must, in terms of section 78, make regulations to address the following—

- 3.2.1. The factors and benchmarks for determining whether prices and other trading conditions imposed are unfair;
- 3.2.2. The sectors to which subsection 8(4) will apply; and
- 3.2.3. In respect of firms owned or controlled by historically disadvantaged persons, the benchmarks for determining the firms to which subsection 8(4) will apply.

4. Legislative Context to the Buyer Power Regulations

4.1. The legislative intent of s8(4)(a) is to protect the public interest by making it an offence for a firm with buyer power to unfairly exploit suppliers that are small and medium business or firms controlled or owned by historically disadvantaged persons (collectively the “designated class of suppliers”) in specific sectors of the economy. In so doing, the purpose is not to protect firms in the designated class from competing to supply large customers on the merits, but rather to ensure that they are equitably treated in gaining access to customers and markets.

4.1.1. Such unfair exploitation includes imposing inferior prices or trading terms on the designated class of suppliers simply because of their inferior bargaining position, smaller quantities supplied or ownership structure.

4.1.2. As such, unfairness may be determined in and of itself, or relative to other suppliers of the same or similar goods or services as the designated class of suppliers.

4.2. Furthermore, as the legislature structured this provision as an exploitative abuse focused on the public interest, the wording and intent of section 8(4)(a) is such that to establish an offence there is no requirement to:

4.2.1. demonstrate the conduct has an adverse effect on competition in any market;
or

4.2.2. weigh up the impact of the conduct as against the impact on consumers or customers of the buyer firm.

4.3. The plain wording of section 8(4)(a) sets out a number of elements that must each be satisfied in order to establish an offence. These elements are:

4.3.1. The purchasing firm and the transaction with the supplier must lie within a sector designated by the Minister in terms of s8(4)(d)(i);

- 4.3.2. The buyer firm must be dominant or shown to have market power within the meaning of s7 of the Act;
 - 4.3.3. The supplier must be a small and medium business within the meaning of the Act and any regulations gazetted by the Minister or alternatively a firm controlled or owned by historically disadvantaged persons within the meaning of the Act and within the benchmarks determined by the Minister as per s8(4)(d)(i);
 - 4.3.4. The price or trading condition must be required from or imposed on the supplier by the buyer firm;
 - 4.3.5. The price or trading condition must be unfair, either in itself or relative to other suppliers.
- 4.4. For the purposes of s8(4)(a), the assessment of market power is conducted in relation to buyer power in respect of the firms within the designated class of suppliers which form the subject of this section. Factors that are relevant to the consideration of buyer power in relation to a class of suppliers include, but are not limited to:
- 4.4.1. The dependency of the suppliers on the particular buyer;
 - 4.4.2. The importance of the buyer in specific distribution channels for the supplied good or service;
 - 4.4.3. The realistic alternatives available to such suppliers, including within a specific distribution channel for the supplier good or service;
 - 4.4.4. The alternative suppliers available to the buyer;
 - 4.4.5. The nature of supply negotiations between the buyer and suppliers;
 - 4.4.6. The outcome of supply negotiations relative to other buyers in the market.

5. Buyer Power Regulations

- 5.1. Reference to a price within these regulations includes discounts, rebates, commissions, allowances or credit. The mere fact a price is contractually agreed does not immunise it from this provision in the Act.

- 5.2. A price may be deemed unfair if it inhibits an efficient firm within the designated class of suppliers to sustainably operate and grow their business, and/or otherwise found to be unconscionable. Factors and benchmarks that may be relevant to this consideration include, but are not limited to:
- 5.2.1. The average total costs or long run average incremental costs of the firm for the specific product or service;
 - 5.2.2. Any additional relationship-specific costs to supply the particular buyer;
 - 5.2.3. Reductions imposed on the purchase price absent changes in costs or market conditions;
 - 5.2.4. The performance of the firm, including trends in sales, profits and investment, with the specific buyer and with other buyers; and
 - 5.2.5. The performance of other firms in the designated class of suppliers subject to the same prices by the same buyer, including patterns of entry and exit.
- 5.3. Alternatively, a price may be deemed unfair if it is inferior relative to other suppliers outside the designated class and there is no reasonable rationale for the difference. A rationale that is essentially related to the quantity of goods or services supplied or the ownership structure of the supplier is impermissible. Factors and benchmarks that may be relevant to this consideration include, but are not limited to:
- 5.3.1. The prices paid for the same or similar goods and services by the buyer to suppliers outside of the designated class of suppliers;
 - 5.3.2. Any differences in, amongst others, the quality, product characteristics and brand value of the goods or services supplied;
 - 5.3.3. Whether the difference in price is reasonably related and/or proportionate to the identified differences.
- 5.4. Trading conditions include any explicit terms contained in contractual arrangements as well as any implied or actual trading terms implemented by the buyer outside of the supply contract. The mere fact a trading condition is contractually agreed does not immunise it from this provision in the Act. Factors that may be relevant to the consideration of whether a trading condition may be deemed unfair in and of itself it, include but are not limited to:

- 5.4.1. It unreasonably transfers risks and/or costs onto the firm in the designated class of suppliers;
 - 5.4.2. It is one-sided, onerous and/or not proportionate to the objective of the clause;
 - 5.4.3. It bears no reasonable relation to the objective of the supply agreement.
- 5.5. Trading conditions that have been found to be unfair in other jurisdictions and which may be given due consideration by the Commission, include, but are not necessarily limited to:
- 5.5.1. Trading without a contract, which imposes uncertainty and risk on the supplier, whilst at the same time denying them standard contractual rights and protections;
 - 5.5.2. Imposing costs or risks onto the supplier that are not spelt out in a clear and unambiguous manner or quantified within the supply contract;
 - 5.5.3. Unilateral changes in the supply terms that are detrimental to the supplier;
 - 5.5.4. Retrospectively changing supply terms of a material nature to the detriment of the supplier;
 - 5.5.5. Excessively long payment terms;
 - 5.5.6. An unreasonable transfer of the buyer's costs of promotion and marketing onto the supplier;
 - 5.5.7. Transfer of the buyer's risks of wastage or shrinkage onto the supplier where it is not due to the supplier's negligence or fault;
- 5.6. Alternatively, a trading condition may be deemed unfair if it is inferior relative to other suppliers outside the designated class and there is no reasonable rationale for the difference. A rationale that is essentially related to the quantity of goods or services supplied or the ownership structure of the supplier is impermissible. Factors and benchmarks that may be relevant to this consideration include, but are not limited to:
- 5.6.1. The trading conditions in contracts with suppliers outside of the designated class for the purchase of the same or similar goods and services by the buyer;

5.6.2. Any objective rationale for such differences; and

5.6.3. Whether the difference in trading term is reasonably related and/or proportionate to the identified rationale.

6. Designated Sectors to which s8(4)(a) will apply

6.1. The concern in respect of the exploitation of buyer power over the designated class of suppliers typically occurs where there is greater downstream concentration relative to upstream supply, and the designated class of suppliers are active or have the potential to be active in the upstream supply.

6.2. In the context where there are frequently multiple stages to a supply chain, section 8(4) of the Act will apply to:

6.2.1. as purchasers, all firms with buyer power which are customers at any stage in the supply chain of the sectors as set out in the subsection below; and

6.2.2. as suppliers, small and medium businesses or, subject to sub-section 7 of these regulations, firms controlled or owned by historically disadvantaged persons, that are suppliers at any stage in the supply chain of the sectors as set out in the subsection below.

6.3. Sectors identified in other jurisdictions or raised in the course of debates on the need for a buyer power provision in the Act, and which may fulfil such criteria, include:

6.3.1. The food and grocery wholesale and retail supply chain (identified in the EU and where large numbers of SMEs exist upstream);

6.3.2. The apparel retail supply chain (where upstream supply has become increasingly fragmented domestically);

6.3.3. Online trading platforms (identified increasingly in global debates on competition law in respect of large tech companies);

6.3.4. The construction supply chain (where sub-contracting relationships with smaller firms are common);

6.3.5. The financial and insurance supply chain (for instance, in relation to small motor vehicle repair shops or intermediaries) ; and

6.3.6. The private healthcare supply chain (for instance, in relation to the supply of consumables and even categories of healthcare providers themselves).

Note to section 6 of the *Buyer Power Regulations*: The Ministry has taken no view on the appropriate sectors to be set out in the Regulations, though there is advantage in limiting the number of sectors to enable the Commission to focus its efforts to the most egregious examples of buyer power abuses, and to develop significant expertise in the sectors concerned. Public comments is invited as to whether these sectors identified in 6.3 above do indeed fulfil the criteria cited in 6.1 above such that a risk of buyer power exploitation exists or can be anticipated to arise in future; and whether there are other sectors that also fulfil such criteria and what is the optimal scope of sectors for the initial implementation of the buyer power provision.

7. Application to firms controlled or owned by historically disadvantaged persons

7.1. The wording of s8(4)(a) makes clear that the legislature intended the section to apply to firms controlled or owned by historically disadvantaged persons that also fell outside the category of small and medium enterprises. However, the legislature also intended to limit its application to such firms, given that customers that did not necessarily suffer from an inferior bargaining position may not require public interest protection.

7.2. In this context, section 8(4)(a) should not apply to firms controlled and owned by historically disadvantaged persons that sell a material and significant share of the input to the dominant seller, such that this provides them with countervailing seller power.

Note to section 7 of these Regulations: Public comment is invited as to whether a presumptive threshold specified as a percentage of sales to the dominant buyer (or the market as a whole) should also be set, (For example, 10% or less of the purchases of the relevant input by the dominant buyer are supplied by a firm that is controlled or owned by historically disadvantaged persons), outside of which the onus would shift to either demonstrating countervailing power or the lack thereof, and if so the level of such a threshold.