

## CHAPTER 7: PRICE-FIXING AND ITS IMPACT ON COMMUNITIES

### 7.1 INTRODUCTION:

The media has recently highlighted price-fixing and other types of collusion between certain business entities in South Africa. This includes allegations of price-fixing on basic foods as well as certain medicines. In the light of world-wide concerns about the high prices of food it raises serious concerns in the South African context where there is a large constituency of economically disadvantaged people. Certain social partners have expressed their disquiet about these issues. The Summit therefore explored this issue from a business perspective and obtained business responses, but more specifically, responses from the point of view of local communities who are hardest hit by such price increases. This session was in the form of a panel discussion with presentations made by the following:

- Dr Janette Minnaar, Business Unity South Africa;
- Ms Nandi Mokoena, Competition Commission;
- Mr Sidumo Dlamini, President, Congress of South African Trade Unions; and
- Mr Nkosikhulule Nyembezi, Black Sash;

**CHAIRPERSON: MS V HARBHAJAN, Business Unity South Africa (BUSA)**

### 7.2 PRESENTATION BY DR J MINNAAR, Business Unity South Africa (BUSA)

The Batho Pele principle proposes: "A better life for all South Africans by putting people first". The act of corruption, or price-fixing, as we are discussing in this session, serves self-interest above the interests of others.

Not only is price fixing and cartel-forming criminalised by the Competition Act, but the damage done and the detrimental impact on communities are significant. Price-fixing and corruption slows much needed economic development by stifling free and fair competition. When companies form cartels, market dominance is achieved and often maintained for lengthy periods resulting in the smaller businessman being eliminated. Entrance into the market by new role players is therefore more difficult because of the monopoly held by the cartel. Consumers do not have access to and cannot freely select the quality and variety of goods and services they desire<sup>25</sup>. Local communities have to pay more for products and services because the price is artificially manipulated. The fixing of a price of a product causes prejudice or harm to broader society and sadly, it is most often the poorest of the poor who suffer most.

These practices are immoral and unethical. It is not good, right or responsible behaviour and compromises the universal values of integrity, honesty, transparency and fairness. Price-fixing is in direct opposition to the principles of corporate social responsibility and good corporate citizenship as promoted in the well-known King II report on corporate governance.

Doing business in an ethical way pays in the long run. Ethical companies attract and retain better talent, protect their reputation more easily, build trust in the community and are more profitable and sustainable.

Our hands are not tied against price fixing and there are many existing structures and initiatives in the

<sup>25</sup> As stated in the preamble of the Competition Act 89 of 1998.

market which we can utilise to curb corruption. Examples are:

1. The United Nations Global Compact which is a framework for businesses that are committed to aligning their operations and strategies with ten universally accepted principles in the areas of human rights, labour, the environment and anti-corruption. The initiative was started because it was felt that business should play a greater role in making corruption unacceptable.

Principle 10 of the Global Compact states: "Businesses should work against corruption in all its forms, including extortion and bribery". Companies are challenged to join governments, UN agencies and civil society to realise a more transparent global economy.

2. The Integrity Pact (IP) developed by Transparency International. The IP is a tool aimed at preventing corruption in public procurement. It contains rights and obligations to the effect that neither side will pay, offer, demand or accept bribes, or collude with competitors to obtain a contract or engage in such abuses while carrying it out.

The IP (Integrity Pact) provides companies with a level playing field where all competitors are bound by the same rules, thereby discouraging bribes.

3. The World Economic Forum initiated the Partnership Against Corruption Initiative (PACI) which began as a sector specific project for the engineering and construction industry, as a practical step towards the implementation of anti-corruption measures. Many companies in South Africa have signed the PACI.
4. The International Business Leaders Forum and the China Business Leaders Forum are two forums where companies partner to promote transparency.
5. The US Federal Sentencing Guidelines, first published in 1991 and updated in 2004, encourage ethical conduct in US corporations. Businesses have to:

- Ensure that they have an effective compliance and ethics programme;
- evaluate periodically the effectiveness of the organisation's compliance and ethics programme; and
- periodically assess the risk of criminal conduct and ... take appropriate steps to design, implement, or modify each requirement ... to reduce the risk of criminal conduct identified through this process.

The Federal Sentencing Guidelines have been incorporated into the South African King 2 report on corporate governance as part of corporate-ethics management recommendations and they will be strengthened in the King 3 report (to be published early 2009).

Organisations can take internal steps to combat corrupt practices. For example:

1. Adopt a code of ethics with a set of chosen values and incorporate it into the strategy and daily operations of the organisation.
2. Follow up the adoption of the code by training and ongoing awareness. Continuous efforts need to be made to ensure that principles and codes are integrated into other management systems.
3. Implement a reporting facility or a "hotline" where employees and stakeholders can safely report crime and irregularities.

In conclusion, Business Unity South Africa and its members support free and fair competition and we

will continue to endorse the efforts of the Competition Commission and to take part in collaborative anti-corruption initiatives such as this Summit and the National Anti-corruption Forum. We applaud the valuable work done by the Competition Commission and we trust that the recent successes of this watchdog body will serve as a stern warning to potential transgressors.

### 7.3 PRESENTATION BY MS NANDI MOKOENA: Competition Commission

*"...on both a moral and practical level, there is not a great deal of difference between price fixing and theft..."*  
Richard Whish, 2001.

What is price-fixing? The Act says that it is an agreement not to compete on price. This has the effect of increasing prices and / or reducing output with the purpose to maximize profits. Price-fixing frequently includes a policing mechanism where businesses have a code of practice and will actually monitor each other. The impact is that consumers cannot 'shop around' to obtain the best prices.

International studies find a median price mark-up from cartels of approximately 15%.

Businesses also agree to divide markets among themselves which has the same effect as price fixing. In such schemes, competitors:

- allocate specific customers or suppliers;
- allocate territories; and / or
- allocate goods or services.

Collusive tendering includes firms that agree in advance as to who will submit the winning bid or tender. Other forms include bid suppression, complementary bidding and bid rotation and are often accompanied by sub-contracting. Such an approach is often found in the engineering and construction sectors where State tenders and other very large contracts are on offer.

The Commission's mandate recognizes that combating cartels is one of the most important tasks that it undertakes, "Combating cartels should be among the top priorities of any competition law enforcement agency."<sup>26</sup>

The Commission has implemented the Corporate Leniency Policy (CLP), 2004, which was revised in 2008. It is a pro-active tool which is integral to the detection and eradication of cartels. It operates on the basis of indemnity being given to firms that provide information of a cartel to the Commission. The "First through the door" method is applied, meaning that the first company that provides the Commission with information and subsequently fully cooperates with and assists the Commission receives a conditional immunity followed by a full immunity. This has proved to be a very successful tool as cartels are very secretive and are very difficult to penetrate.

Major cartels uncovered by the Commission include the bread price fixing cartel and the pharmaceutical cartel, among others. The theme of this session is the impact that price fixing has on communities: it does have a very severe effect on the poorer communities.

The Commission uncovered the bread cartel after the cartel had been implemented just before Christmas 2006 and found that Premier (Blue Ribbon) Tiger Brands (Albany) and Pioneer (Sasko) had agreed:

- to increase the price of bread to customers;
- to fix their prices to distributors; and
- not to poach each others independent distributors.

<sup>26</sup> International Competition Network, 2005

The effect was that:

- Prices of basic bread increased by +/- R0.30c;
- Distributors discounts were slashed from R0.90c to R0.75c; and
- Distributors were refused alternatives

This was implemented one week before Christmas (2006). There is an ongoing investigation into the milling industry.

“The bread case is a living example of how an unjust economy can further impoverish poor consumers, and destroy opportunities for small businesses (especially those that serve the poor) to help citizens to regain full and free participation in the economy.”<sup>27</sup>

The pharmaceutical cartel investigation was initiated by the Commission. The cartel included Adcock Ingram, Fresenius, Kabi, Dismed and Thusanong, all of whom they had agreed to act collusively when tendering for State tenders. For example, all acted collusively for a contract, namely Contract RT299, a state tender for intravenous solutions and they also agreed to divide the private hospital market amongst themselves.

The effects resemble the usual outcomes of collusion:

- State paid 10% - 15% more for IV fluids, estimates range from R20 million p.a to R60 million p.a
- Private hospitals paid up to 33% more for IV fluids
- Barriers to entry were increased<sup>28</sup>

The milk cartel investigation was also initiated by the Commission and the respondents were Clover, Parmalat, Ladismith Cheese, Woodlands Dairy, Lancewood, Nestle and Milkwood. It was Clover that has received leniency in part, with the hearings set for September 2008.

From the side of the Commission the allegations are that Clover, Woodlands and Parmalat fixed prices indirectly by co-ordinating the removal of surplus milk from the market, while Woodlands and Milkwood fixed the price of UHT milk and allocated geographic areas in which they would not compete in selling UHT milk.

The Commission further found that Clover, Parmalat, Ladismith, Woodlands, Lancewood and Nestle had exchanged sensitive information on procurement prices of raw milk in various ways.

### **Conclusion**

All of these cartels have had severe impacts on poorer communities, as bread and milk are both staple necessities.

## **7.4 PRESENTATION BY MR N NYEMBEZI: National Advocacy Programme, Manager of the Black Sash.**

As the Black Sash we believe that the greatest deterrent to cartels should be the likelihood that offenders at company and individual level will be apprehended, penalized and even punished through heavy fines, loss of future state tenders and tax incentives. There is no dispute that cartels destroy competition and are causing serious harm to the economy and consumers. This unscrupulous practice clearly

<sup>27</sup> National Consumer Forum, 2007

<sup>28</sup> The total expenditure on pharmaceuticals in the public sector is about R 5 billion

pushed up the price of basic food items and medicinal items to the detriment of consumers, but more disconcerting is the fact that these practices extended across the country for over 12 years.

It is important to remember that price-fixing and cartel activity takes place in an environment of high levels of unemployment, low wages, the sharp decline in purchasing power, rising fuel prices, rising energy prices, high interest rates and chronic poverty. It takes place in an environment where food security in poor households is declining. The significant increase in the price of basic food stuff particularly affects those at the lower end of the socio-economic scale for whom these food items are a staple.

The artificially high prices imposed on consumers through price-fixing have hurt ordinary people in our communities, especially those in the Living Standards Measure (LSM) 1-5, and increasingly the middle-income earners. So serious is the impact on poor communities that government has recognised the close link between social security and the price of food. Finance Minister Trevor Manuel's medium-term budget policy statement in 2007 set aside about R4,3 billion to compensate pensioners and social grant beneficiaries for rising food prices and other cost of living increases. This is based on the government's recognition that social grants are significantly and positively associated with a greater share of household expenditure on food.

We continue to ask ourselves, how many loaves of bread has this cartel activity taken away from the mouths of school children who are dependent on the school feeding scheme for a daily meal? How many households had to go hungry for days because there was not enough money to afford basic foodstuffs as a result of this activity? Price-fixing has affected the health of ordinary people as it has been noted in various studies that poor people with HIV/AIDS or TB benefit more from their treatment if they have the necessary nutrition to support the medication they receive. The high levels of poverty in South Africa are linked to structural unemployment and perpetuate the inequalities of the past. Cartels undermine the efforts of government to provide comprehensive social security and employment opportunities.

We call on this Summit to support legislative and other measures to ensure that companies guilty of collusion, particularly where this affects state resources and essential services, be excluded from state tenders for a determined period as a matter of principle. We also call on this summit to support legislative and other measures to ensure that government awards corporate tax relief only to those companies that practice good corporate governance by excluding companies guilty of collusion from this benefit.

The Black Sash calls for strong legislative measures to ensure that government departments, including the State Tender Board, involved in issuing and adjudicating of state tenders are better equipped to prevent corruption and deal with companies involved in collusion. In an environment where government is involved in the procurement of goods and services, and where the possibility for collusion and uncompetitive behaviour by companies applying for tenders is high, it is important that strong institutional checks and balances are in place.

Referring back to the strong legislative measures and the checks and balances we are calling for, companies and other stakeholders should not merely seek to promote compliance with certain guidelines or some pieces of legislation, but should promote a human rights culture through good corporate governance practice.

## 7.5 PANEL DISCUSSION

A panel discussion ensued after the presentations and the input/comments on the presentations are contained in Table 2.

TABLE 2: COMMENTS ON PRESENTATIONS

Discussion points	Inputs from conference delegates	Response by panel members
<p>Competition Commission</p>	<ul style="list-style-type: none"> <li>The Competition Commission should not depend on cartel members' confessions. The investigative agencies also should be involved.</li> </ul>	<ul style="list-style-type: none"> <li>The experience is that no company will come forward until the Commission has started an investigation, at that stage they come forward and the investigation is thus not compromised.</li> <li>The Competition Commission uses the Company Leniency Policy (CLP) as a tool to detect cartels. The Commission has been in existence since 1999; the CLP was only introduced in 2004. From 1999 – 2004 the Commission did not see much progress as cartels are highly secretive. But since 2004 there has been increased awareness and increased achievements. Furthermore, immunity is 'conditional' and only becomes 'full immunity' at the end of the process.</li> <li>The CLP is a trade off that the Commission needs to use to make progress as the commission can only act in terms of the Companies Act. However, the Department of Trade and Industry (DTI) has made proposals to criminalize certain aspects such as collusion, price fixing, and tender fraud etc. Also the Commission has already made submissions to Parliament on these issues.</li> <li>The Commission does not have criminal jurisdiction but there is cooperation with other organizations to see how this can be addressed.</li> </ul>

Discussion points	Inputs from conference delegates	Response by panel members
<p>Competition Commission</p>	<ul style="list-style-type: none"> <li>The CLP calls for full disclosure, yet Adcock Ingram and the bread price-fixing company belong to the Tiger Brands Group, thus indicating that there was not full disclosure. Furthermore, soon after being found guilty of price collusion, Adcock Ingram won a tender from the Department of Health. Further, there was no benefit for consumers after the bread price-fixing scandal and the whistleblower was victimized.</li> </ul>	<ul style="list-style-type: none"> <li>The Department of Health will be claiming damages from Adcock Ingram. Further, the Act also says that anybody can take matters to court in order to claim what they think their damages are. Naturally the individual damages are too small for individuals to go to court as such. As for the price of bread not being reduced; the Competition Commission does not have such a mandate and is not a price regulator.</li> <li>The Whistleblowers Act provides for protection for those that give information to the Commission. The Act says that such persons do not have to give their names and details. Regarding the bread price fixing and the case of Mr Mukkadam; he was not the original complainant - it was another person had informed the commission. The Commission thereafter went to the Cape to interview bread distributors, which included Mr Mukkadam. They were informed that they did not have to provide their names. However, two days later Mr Mukkadam filed a formal complaint against the bread companies and in so doing provided his name and details. The Commission has tried to assist Mr Mukkadam with his present difficulties although this is not in the Commission's mandate to do so.</li> </ul>
<p>Competition Commission</p>	<ul style="list-style-type: none"> <li>The Harvard Study Group that was appointed by National Treasury Commission "waits for persons to complain". The recommendation from the Harvard Study Group is that legislation must change to enable it to work proactively.</li> </ul>	<ul style="list-style-type: none"> <li>As a result of the bread and milk cases the Commission has commenced a study of the food industry to determine if there is further anti-competitive behaviour as it has had a huge impact on the poor. It is not an investigation and I am unable to reveal what has already been uncovered. Regarding the Harvard Study Group's report about the Commission being reactive; the Act provides that the Commission can act proactively and it has done so in many cases. The Commission also has a policy and research division so that it can generate important information. One of the submissions to Parliament recommends that this aspect needs to be enhanced. The Commission is using its powers with regard to the steel cartel which has huge implications for South Africa. This work has come from the Commission and thus shows that we are doing work on a proactive basis.</li> </ul>
<p>BUSA</p>	<ul style="list-style-type: none"> <li>What is Business Unity South Africa (BUSA) doing to sanction its members?</li> </ul>	<ul style="list-style-type: none"> <li>The members of BUSA participate on a voluntary basis and many of them are in other chambers and professional bodies such as the insurance industry. BUSA does not operate in terms of legislation and thus it does not have the mandate to apply sanctions against its members. Senior members of BUSA have taken part in the Summit and participate in the NACF and BUSA has called for the strengthening of the Boards of Directors as well as participating in the King III report. BUSA is developing programmes for future awareness and capacity building to prevent corruption in organisations. The comments made however have been noted and will be referred to BUSA.</li> </ul>

Discussion points	Inputs from conference delegates	Response by panel members
<p>BUSA</p>	<ul style="list-style-type: none"> <li>● Legislation needs to be tightened as a R2000 penalty for a CEO is too low. Also, the legislation is very good on paper but it needs to be implemented. Price-fixing is no less than robbing the consumer. The British Office of Fair Trade found that businessmen dread going to jail and also fear not being able to tender for government business. The voluntary membership of BUSA should require the adherence to codes of conduct. Can BUSA allow corrupt companies to continue to be members? There should be a message from BUSA that corrupt businesses should face the full wrath of the law.</li> <li>● There seems to be an inability of business to regulate itself and hence such issues as price fixing. Also there are issues around medical schemes and bank fees among others that results in the calls for and by government to improve regulation.</li> </ul>	<ul style="list-style-type: none"> <li>● BUSA does not have direct membership; its members belong to business organisations, for example Business Leadership South Africa which has some of the top JSE companies as members. Further, BUSA is not a watchdog organisation and can only react to allegations of price-fixing and has on a number of occasions stated via the media that it does not condone price-fixing and that it is against corruption.</li> <li>● Regarding codes of conduct – BUSA cannot prescribe to companies and industries as to what their codes of conduct should contain. Hence the codes of conduct of banks would be different to the codes of conduct of other sets of business.</li> </ul>
<p>BUSA</p>	<ul style="list-style-type: none"> <li>● Can BUSA clearly state that they support the principle of CEOs being criminally charged and sent to jail for price-fixing and corruption?</li> </ul>	<ul style="list-style-type: none"> <li>● BUSA supports very strict punishment for directors and member companies that are involved in corrupt activities such as price-fixing. BUSA is a representative body, and we will take these suggestions back to be discussed at management level.</li> </ul>