The Other Sides View – Price Discrimination from the perspective of small business

Introduction

The literature review by Davis JP (2014; 131 @ 711 – 716) and the critique offered especially with regards to the Nationwide Poles V Sasol case is deserving of further comment. In particular, it seems to me that small business has very little voice on the subject of price discrimination. This is surprising, as small business is arguably the most affected part of our economy faced with this practice. The lack of organisation of small business as well as the high degree of knowledge and skills required prohibits most from active participation in the debate.

There exists a paucity of skills and experience regarding price discrimination cases, not only within the context of small business. The presence of only one decided case regarding S9 of the Competition Act suggests that this is virgin territory and that all involved are learning as they go along. In this regard, I refer to all players in the game, the prosecution, defence, economic analysts and in of those sitting in judgement. I would suggest that there are very few small businesses with both the resources and abilities necessary to prosecute a S9 matter.

The absence of a continued series of cases concerning price discrimination is a particular concern. We must believe either that price discrimination has been abolished in commerce, or that other issues are present which lessen or prevent the active prosecution of price discrimination cases. The literature review as noted above suggests the latter.

My purpose in writing this contribution is my hope to move the debate forward and to raise the other side of the coin, namely the perspective of small business. Nationwide Poles recognise that our active participation in the debate disappeared along with the demise of the company in 2006, and any opportunity to appeal the CAC judgement has long prescribed. In the light of this and with nothing to gain, our commentary as follows can and should be considered reliable. In some way we hope that our views can be considered as definitive, given the now completely impartial perspective which we now enjoy.

Davis JP raises four important issues in his review and critique of the price discrimination literature. Before commencing commentary, it will be plain that our views and those of the CAC are unlikely to coincide in all respects. Concerning one issue, we absolutely agree. Both the JP and the author are absolutely certain that the interests of small business need to be promoted in the execution of the will of the Act. Indeed so strongly does the Davis JP feel on this aspect that he prays for another case so as to interpret S9 with a view toward promoting the small business sector. Regrettably, the evidentiary burden placed on small business or its proxy, the Commission, suggest the unlikeliness of this event.

In the *Nationwide Poles V Sasol* case, NWP long pondered the meaning of what was likely to substantially lessen or prevent of competition could be. Even more difficult was attempting to envisage the type or format of evidence required to prove this essential aspect of S9. Our greatest difficulty revolved around the word “likely”. In our view, this word invited a forward looking assessment of the effects on the business as a result of the actions concerning the complaint. It also suggested a probabilistic approach to the analysis.

So difficult was this particular aspect concerning the likely effects on competition, that NWP requested specific guidance from the CAC in its judgement as to what precise proofs would be necessary to prove this aspect. NWP did so at the time so that those that were to follow could better understand what was meant by this requirement. In any event, this request was not traversed in the NWP v Sasol CAC judgement. The critique that the CAC has not provided direction as to the type of evidence would meet these test must be considered fair, in light of this knowledge.

The evidentiary burden placed upon a complainant concerning a price discrimination claim is most extensive. At very least all the tests regarding equivalence of transactions and market domination need to be crossed. In the latter case, it is necessary to conduct a market analysis and determine the upstream market in question. Only then can the question of domination be considered. The NWP experience suggests that within this market analysis, many points of debate will arise and require answer, amongst others the questions of substitutability of product etc. In addition to this onerous proof of upstream market load, is a second market analysis of the downstream market necessary?

Based on the CAC decision in the Medicross case, it seems that in order to prove a likely lessening of competition, a full downstream market analysis is in fact required. We must then ask why does lessening of competition necessitate a market analysis, when viewed against the predictive word “likely” as contained in S9? Historical market data cannot be considered to be reliable indicators of future outcomes, especially with regards to the survival of small business in a market. The effect of a single small business entry or exit in a large market will pass un-noticed in overall market statistics.

Fortunately the CAC has now provided some direction as to the kind of evidence that would assist in proving a likely prevention of competition. It appears to relate to how the act of pricing differentially causes obstacles of access to the relevant market or sustainability in that market. In other words as noted in *Medicross*, it concerns impediments or hindrances which retard or keep back that which might otherwise have happened. It is necessary to understand business in order to appreciate what this means.

Small businesses have a general commonality. The actions of the business feed the family of the owner and that of the staff involved. In essence the business operates in order to make money, not to lose it. It seems almost unnecessary to raise this essential point, but it is necessary so as to understand that which follows:

Decision making for small business, as indeed is the case for all business, involves daily assessment of actions that will either promote cash availability and those actions which will diminish cash resources. Any small businessman will tell you that cash is king. Absent sufficient cash resources, the business must shrink, due to a reduction in working capital. Any impost or cost to a business not carried by ones competitors has the effect of reducing available cash resources relative to that of the competitor. Higher input costs are thus a bad thing if selling into a competitive market.

However, in the presence of surplus cash options as to how to spend that cash arise. Leaving aside profit distribution, the rational businessman looks at the potential for reinvestment into the business, either through expansion or productivity improvements or a reduction in borrowings. These applications of cash enable additional cash reserves to be generated.

The critical matter at issue here is that these decisions are made in context. These decisions do not stand independent of competitive positioning of the market. By way of example, the reinvestment decision when faced with known price discrimination relative to one’s competitor becomes far less likely. Simply put, if the economic motive is adequate in the context of all known information, then reinvestment is more likely. Absent economic motive, it makes more sense to either hold on to the cash until a suitable opportunity arises, or exit the business.

Not only is there an advantage in having excess cash available for spend, a second and crucial outcome occurs. This outcome relates to the nature of the options presented. In the presence of surplus cash, the mere fact that options exist, creates a value of itself. The decision to reinvest could be delayed or made immediate, the nature of the reinvestment changed or saved for some future event. Essentially proper returns permit flexibility. When adequate cash is available, the business can change and adapt to market circumstances. These circumstances permit a build-up of resources to enable the business to survive in adverse economic climates. None of these advantages are made available to the cash strapped business.

In the case of the cash strapped business, the owner is generally faced with financial stress, and their enthusiasm to reinvest diminishes. The options then become one of survival or exit. The former can only be contemplated when realistic opportunity for profit is foreseen, The latter becomes reality when economic incentive disappears.

It is clear that small business generally fades the brunt of price discrimination. In the case of NWP a 4% effect on the bottom line equating to 50% of its profit, simply put the reinvestment decision into the unsustainable box. The business was forced to close its doors. It could not sustain its purpose, the generation of cash.

To avoid all doubt then, anything that sucks cash out from a business is bad for competitive positioning in the long run (including price discrimination), and anything that adds to available cash is good for long term competitive positioning. Surplus cash enables better competitive positioning and the survival of the business in bad times. This is to us a self-evident truth, and it needs no expert testimony to prove its existence. This is where the test of substantiality may come in.

The third issue that needs to be addressed relates to the apparent absence of evidence to support public interest considerations as contained in the preamble to the Act. It is hardly surprising that we disagree with the CAC on this issue. We note that generally the preamble is not taken into account when interpreting an Act.

In argument at the CAC, NWP did point out the detail contained in Hansard at the second reading of the Competition Bill. In response to criticism of the preamble from Dr Botha (NP), the Minister of Trade had this to say. “If he were to look at the preamble in its entirety, he would see that this is an important part of the new legislation. The purpose of the preamble is to indicate to those who will subsequently interpret the law the main thrust and spirit of the law.”…

In the view of NWP, and I would imagine that of small business generally, the preamble invites a purposive interpretation of the Act. This invitation is significantly bolstered by the direction apparent and given by Parliament during the reading of the Bill. Additional support is gained in the many mentions of the societal outcomes anticipated in the new Act. It is worthwhile to note that the bill was passed unanimously and all parties subscribed to the general aims of the new Act.

In order to promote the interests of small business it seems to us that a purposive interpretation of the Act will be required. Should this happen, we would commend the outcome.

Recently, the work of Jean Tirol came to my notice, and in particular his explanation of asymmetries of information. Generally, large corporations possess large and detailed volumes of information. Much of this information is classified as secret or business critical. In general, a great deal of information exists which is bot within the public domain. As a result, information available to larger businesses is generally more perfect than that available to smaller business or indeed the Commission when reviewing a complaint. This in Mr Tirol’s view causes significant disparities in the bargaining power of the parties. I offer this only to make the point about the costliness of a price discrimination case, and the great lengths required to obtain relevant factual information. NWP had personal experience of these costs. Perhaps these disparities in information contributed to the letter of non-referral. I personally have little doubt about this.

I must also touch on another issue. It seems to me that a dogmatic or prescribed approach in analysis may not be ideal. They certainly affected our thinking and not in a positive sense either. By way of example, as stated by the various authorities, there exists a dogma to the effect that : competition law is there to protect the competitive process and not competitors themselves… The following is an extract from my notes at the time of *NWP v Sasol* and it may be useful:  
  
*Absent any potential and beneficial effect on the ultimate competitive position of a complainant, there would be strong economic disincentive for an aggrieved firm to complain or pursue cases of competitive abuse. Without potential reward by way of improved competitiveness, it would be better for the prospective complainant to merely to exit the business or concede to the abuse.   
   
We can not ignore the fact that in competitive matters, the Authority must find either for or against a Complainant, thereby reinforcing the competitive position of one or other of the litigants. If the executive arm of the Act is to be effective in protecting competitive processes and implementing the will of the Act, it must therefore ultimately protect the interests of the individual competitor. Failure to do so would frustrate the intentions and objectives of the Act and nullify or reduce to a moot point, the very competitive equity and fairness that Parliament seeks to entrench.*

Or as stated by Mr Lewis, in the absence of competitors there can be no competition. In both cases, I feel that no matter their attractiveness, dogmatic generalisations serve little real purpose and they should where possible be avoided.

The point of this note shown above reverts to how this article started. Small business needs to be in business and it needs fair playing fields. It is the seed bed for potential future giants. To grow and thrive, small business needs little more than some good soil and a touch of sunlight. If planted in the shade, do not be surprised if its competitors overwhelm its presence because of faster growth. You see, sunlight is the cash of photosynthesis, less of it is detrimental, and more advantageous. Like small business, if the seedling is to survive it needs more in than that which goes out. Oh yes, and time to grow.

Given the costs of prosecution, we have often been asked as to why we chose to proceed with the matter. Surely, it is argued, economic rationality would have dictated exit the process and simply close shop. And with this I agree. We, however, had a different end in mind and one to which my conscience subscribes. It boils down to this:

* Meaningful economic participation and hence the welfare of the family is founded on fair and equitable commercial opportunity.
  + If true,
* Then economic emancipation of small business is a necessary prerequisite to the greater goal of societal fairness and equity

Sounds a bit like the preamble, perhaps.

JN Foot

*Ex owner of Nationwide Poles*

*No Credentials – University of Hard Knocks*