IN THE COMPETITION TRIBUNAL SOUTH AFRICA

Case NO: 110/CR/Dec06

In the matter between:

Competition Commission of South Africa	Applicant
And	
Senwes Limited	Respondent

Panel	: N Manoim (Presiding Member); Y Carrim (Tribunal Member) and M Holden (Tribunal Member)
Heard on	: 12 November-23 November 2007; 28 and 29 January 2008; 21-23 April 2008; 3, 6, 9, 17 and 18 June 2008 with argument heard on 10 and 11 July 2008
Delivered on	: 03 February 2009

REASONS FOR DECISION [NON-CONFIDENTIAL]

Introduction

[1] In this case we are asked to determine whether a vertically integrated firm that is dominant in the grain storage market, through its ownership of concrete silos, has abused that position, through its storage tariff practices to exclude rival firms in the downstream market for the trading of grain.

[2] The case against the respondent, Senwes Limited ("Senwes") was referred to the tribunal by the Competition Commission ("Commission") on 20 December 2006, following a complaint lodged by another trader, CTH Trading (Pty) Ltd ("CTH") on 2 December 2004.[1]

[1] CTH also had other complaints against Senwes' practices, these related, to its administrative charges and production loans to producers. The Commission elected not to refer these aspects of the complaint. Another firm, Unigrain, applied to intervene in these proceedings, to include in these proceedings, other complaints it had against Senwes. We dismissed the application.

[3] It is necessary to have an appreciation of the history of the silo market and the evolution of the tariffs charged for storage in order to consider the complaint.

Background

[4] Senwes is a public company that operates in the agricultural sector. It provides numerous services, but for our purposes we are interested in the business it operates as a silo owner, storing grain for itself, as well as third parties, and as a marketer and trader of grain. Senwes has existed for almost a century. For most of its existence it was a co-operative, but was converted to a public company in April 1997.[2]

[5] Senwes' silos are located mainly in the Free State province and to a lesser extent in the North West, Gauteng and the Northern Cape provinces.[3] The Commission alleges that each silo constitutes a local grain storage market for a radius of 60 kilometers surrounding it. Taken cumulatively these local markets make up what is termed the 'Senwes area', a concept not in dispute in this matter.[4]

[6] The large concrete silos that characterise Senwes' silo assets are a product of an age of regulated agriculture. Built mostly in the years between the mid 60's and the mid 80's, these silos are near monopolies in their own areas.[5] Senwes owns 56 of the 80 silos in the Senwes area. It has 90% of the storage capacity in 45 of these silos areas.[6]

[7] Senwes and similar co-operatives in other parts of the country acquired this position in the economy as a result of state regulation. In terms of the Co-operatives Act, co-operatives were forbidden to go into competition with one another.[7] This led to there usually being only one silo in a local region, typically owned by a co-operative. Grain production was also the product of a centralised system of planning. Farmers were obliged to sell their product to the

[2] See extract from Senwes annual report of 2004, pleadings file page 137.
[3] Complaint referral paragraph 16.1.
[4] Senwes itself refers to the 'Senwes area'. See transcript page 1637.
[5] See Pleadings file page 94. Paper by Brendan Bayley, of the Land and Agriculture Policy Centre, entitled "The Market for Bulk Storage and Handling in South Africa, October 1997. This paper is an annexure to the complaint of CTH, which itself is annexed to the Commission's referral.
[6] According to the Commission's expert agricultural witness, Professor Vink. See transcript page 34.
[7] See testimony of Johannes Davel a former general manager of Senwes.See ttranscript page 158.

Maize Boards, who in turn were obliged to buy it from them at a regulated price. Maize boards then sold the product to millers who processed the grain for the final consumer.[8]

[8] All this was to change in the mid to late 1990's when following the new dispensation, the government embarked on a policy of de-regulating agricultural markets. In 1995 the marketing boards were abolished and the trading of grain was no longer regulated by statute.[9] The effect was dramatic. Since farmers were no longer guaranteed a fixed price for their grain, usually calculated on some cost plus formula, based on the costs of the most inefficient farmers, certain farmers were no longer viable, and so the grain farming area shifted to those geographic areas most conducive to the growing of the crop - from the south west to the north east.[10] Less of the country was now devoted to grain farming, but the yields improved in those areas where farmers continued with these crops.

[9] Whilst the choice of land to devote to planting could shift, silos could not. Some silos established in areas that lost out, now found themselves in the neighbourhood of game farms not maize fields.[11]

[10] Senwes was fortunate in that its silos retained their central location in the grain planting areas.[12] But whereas farming was now the subject of market forces, silos were not. Silo ownership was however to change. Once owned co-operatively by farmers in their catchment area, they are now public companies owned by shareholders many of them institutions. Silos, like Senwes, are now run for the benefit of these shareholders, not, as once was, the community of farmers that surrounded them. Yet what market forces did not disturb was the near monopoly silos enjoyed in their respective areas. Silos are enormously expensive structures to construct and given the fact that they appear in general not to be at full capacity outside the initial harvest season, an imprudent investment for anyone else.[13]

[11] The most significant changes brought about by liberalisation came to the way grain was traded. With the abolition of the control boards, grain was now traded as a commodity and

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[8] See Van Tonder transcript 805-7. As a note on nomenclature in this case farmers are sometimes referred to as producers and millers as processors.

[9] CTH complaint affidavit paragraph 14.1, pleadings file page 38.

[10] See testimony of Professor Nick Vink, the Commission's agricultural economist, transcript page 27 onwards.

[11] See evidence of Remy Burdairon, a trader with Dreyfus, who testified that this had happened in Limpopo. Transcript page 625

[12] Vink testimony, see transcript page 29.

[13] Vink testimony, see transcript page 51.

subject to market forces. In 1995 grain started to be traded on the South African Futures Exchange ("Safex"). In 2001 Safex was purchased by the Johannesburg Securities Exchange, and now forms part of its Agricultural Products division ("APD").[14] In 2007, the APD recorded 2.4 million contracts had traded.

[12] Safex has had a profound effect on the grain market. The price of grain is now determined by the Safex price, and, all are agreed on this, is the subject of competitive market forces. Safex not only trades grain as a spot market but crucially as a futures market as well offering for most grain types a series of futures contracts that get traded daily as well. In order for grain to trade on Safex it must be traded by way of a negotiable instrument that can be traded multiple times. Liquidity differs depending on the type of grain. Safex states that white maize is the most liquid, followed by wheat, yellow maize, sunflower seeds and soya. This instrument is referred to as a silo certificate and is issued by silos registered with Safex, such as Senwes. Silo certificates represent the holder's entitlement to a fixed quantity of grain stored at a particular silo. In the case of maize, each certificate represents 100 tons of maize. The certificate as we noted can be traded many times. Ultimately a holder is entitled to collect the quantity specified in the receipt, from the silo issuing it, free on truck. The holder is liable for any outstanding storage and handling fees. The certificate will record any storage and handling fees paid up to the date endorsed by the silo owner on the certificate. Typically, this would be the costs incurred as of the date the certificate is issued. The holder will thus be in a position to calculate the outstanding costs of storage payable on collection date.[15]

[13] Typically, South African grain prices are someway between import and export parity prices, and whilst graphs show they do not track them perfectly in the short term, the observation is correct for the medium to longer term.[16]

[14] The advent of de-regulation also meant that the market was becoming more complex, and with Safex becoming the primary place where trades take place, the way was set for private intermediaries, in the form of trading firms, to replace control boards as the interface between farmers and millers. Traders buy up grain from farmers throughout the season and then sell grain to millers. Traders however are not only involved in the trading of physical grain. Indeed

[14] Website of Safex, document entitled Exchange traded agricultural derivatives in South Africa.

[15] See Exhibit F, a blank certificate that sets out the conditions and states *"for delivery in terms of a Safex futures contract and in terms of the rules of the JSE*." See also evidence of Van Tonder, transcript page 826-8.

[16] See figure 2 in the Genesis report a graph comparing the Safex price with the import and export parity price from May 2005 to October 2007, Witness statement file page 63.

some of them never are. The amount of grain traded on Safex exceeds the amount of physical grain traded by a factor of eight. One Senwes witness testified that a silo certificate could be traded as many as 25 times.[17] Many traders are only involved in trading grain contracts and not what is termed the physical grain market. Trading firms vary in nature from large international traders who are also present in the local market, financial institutions, to small firms comprising of not much more than a few traders and their fax machines.

[15] But what is relevant for this case is that silo owners, Senwes amongst them, are major players in the trading market as well. The Commission's case is that trading has become such an important component of its business that its trading strategy has informed its storage policy, with the trading tail wagging the storage dog.

[16] The significance of silo owners playing in the trading market becomes apparent when we examine how prices are formed on Safex. Although, as we noted, what is termed the Safex price is the product of competitive market forces, the prices that traders pay to farmers to buy grain and to sell it to processors is not the Safex price, but a price derived from it. In order for grain to trade as a commodity on Safex it is necessary, or so we are told, for Safex to set tariffs for storage and transport inputs- so that the market trades the commodity with the assumption that these post production and pre-milling inputs are standard. Committees within Safex recommend, inter alia, annual tariffs for handling charges at silos, daily storage rates, transport rates from silos, and costs for the issue of silo certificates. Whilst these rates are not binding, we are told that in practice they are followed by all the silo owners. The rates are not administrative prices set by a body tasked by public regulation to do so, yet de facto, they are treated as if they were. [18]

[17] Witnesses during the hearing suggested that the rates are the subject of a diktat from the silo owners of the grain silo association, who recommend them to Safex which then accepts them.[19] Senwes contends that the rates are the subject of negotiation between players in the industry represented on the relevant sub-committees of Safex. We are not in a position to take a view on this, as whether Safex rates are the product of robust negotiation or collusion, is not the

[17] See Booyens, transcript page 1725.

[18] See Senwes joint witness statement where it is stated, *"As a rule of thumb, silo owners charge Safex rates."* See paragraph 2.3.3 page 5 of Senwes joint witness statement.

[19] See for instance the testimony of Burdairon from Louis Dreyfus, who says this is not the way things work in other markets he is familiar with such as Chicago. See transcript page 618-9 and 658.

case before us presently. Nevertheless given what some of the traders have said about this during our hearing, the Commission should give this matter urgent attention.

[18] When traders purchase grain from farmers they use the Safex price for that day as the basis. From that price they make deductions based on the Safex tariffs for transport, storage, and handling. Typically, they will also make a deduction for their commission expressed as a percentage per ton. The Safex transport tariff is a notional tariff. It is calculated on the basis of the rail costs from that particular silo to a base destination Randfontein.[20] Randfontein serves as a base destination as historically it was where many of the major processors were located.

[19] However for various reasons the Safex transport tariff does not reflect the actual transport costs of a particular transaction between a farmer and a trader and hence we refer to it as a notional tariff. In many instances a trader's actual transport costs are lower than those provided for by the tariff, either because the distance is shorter (the mill is not situated at Randfontein but at a destination closer to the particular silo) or the trader uses transport alternatives that are cheaper than rail.[21] Konrad Keyser, one of the trader witnesses called by the Commission, points out that some silos are closer to Randfontein than the rail network, because sometimes trains do not run directly, but pass through another point, before going to Randfontein. In such cases traders offer some of this saving to the farmer in order to induce the sale. The difference between the actual cost and the notional cost is referred to as the Safex premium.[22] As Christo Booyens of Senwes, who confirmed this fact put it, if he knew that the transport differential for delivering from a silo to a mill in Kroonstad was favourable, and he knew he could sell grain to a miller there, he would be willing to pay a farmer more for the grain.[23]

[20] The more efficient a trader the more of the premium it can pass on to a producer to procure a sale. There is no complaint from industry about this aspect of competition between traders who own silos and traders who do not.

[21] Safex also sets rates for handling and storage. The storage is set at a daily rate which is reviewed annually.

[20] Keyser evidence see transcript 225.
[21] Keyser suggests that whereas several years ago it was 90-10 in favor of rail that figure has come down close to 50 – 50. See transcript page 224.
[22] See explanation by Theron, transcript page 906
[23] See transcript page 1210

[22] The grain market comprises several products that have different seasons. The products are white and yellow maize, wheat, soya and sunflower seeds.

[23] The largest crop is maize, comprising 80 % the grain crop and hence its season is the one that has occupied most of the attention during this hearing.[24] Typically a season starts with planting from October to December (sometimes late January) and the bulk of the crop is then harvested from June to August (again a very small amount in September) –of the following year.[25]

[24] By harvest time most farmers are financially strapped. They have borrowed heavily to finance their crop and need to recoup these costs.[26] Farmers thus have the dilemma as to whether to sell all or some of their crop at harvest time to pay off their debts and to realise some income. Prices are however lowest at harvest time and rise during the course of a season.[27] This is because supply is at its greatest at the beginning of a season and reduces thereafter. But there have been seasons where prices have dropped over time and so farmers knowing this cannot be certain that prices will always be better in the future.

[25] As a rule of thumb we are told that farmers typically sell 30% of their crop before harvest, 30% at harvest and the balance is carried for a longer term to sell later in the season.[28] In this way famers ensure cash flow and can speculate on improved prices.

[26] Traders for their part seek grain from the beginning of the harvest season. Some traders, Senwes amongst them, arrange deals for farmers prior to the harvest to sell grain to them and in variations of this arrangement may grant them a share of the upside in prices later in the season.[29]

[27] Other farmers cut out the middleman and sell some of their crop directly to millers. However, this does not account for much of the crop. There are reasons for this. Millers prefer

[24] See evidence of Theron, transcript page 962 and her witness statement, and Econex report, Commission witness statement file, page 273.
[25] See transcript page 1184-5 evidence of Booyens.
[26] Transcript page 316, evidence of Keyser.
[27] See Vink transcript page 31 and Keyser transcript page 316.
[28] See evidence of Keyser, transcript page 295. Also Senwes witness statement, witness statement file page 15 paragraph 5.1
[29] Senwes offers such a hybrid it is referred to as the plaaslaai. See transcript 1194 -5

to buy grain from silos because of quality control exercised by silo owners, and secondly, storage capacity at mills is limited. Vink suggests that millers have capacity for storage for four months at most, but they need grain throughout the season.[30] Others suggest the storage capacity of miller is typically only one month.[31] Thus even a farmer located next to a miller would need to make use of storage. Mills also want to take advantage of price movements during the course of a year.

[28] Thus the bulk of farmers' crops not required immediately by processors must be stored and must be stored at someone's expense - either the farmer or a trader.[32]

[29] When the farmer brings the grain to a silo it is graded and then stored in a silo according to its grade e.g. white maize number 1. The grain now loses its identity as being the property of a particular farmer.[33] When a farmer delivers grain to the silo he will get a receipt for the quantity of grain delivered and specifying its quality. This receipt known as the silo owner's receipt is not to be confused with the one tradable on Safex. It is a matter between the farmer and silo owner. Typically farmers do not deliver grain in quantities of 100 tons. Rather they deliver gradually in varying amounts. Only however once a farmer had delivered 100 tons could that farmer apply for a silo certificate to enable that grain to trade on Safex.[34]

[30] Historically Senwes' policy towards storage has been to offer a daily rate for storage at the Safex tariff, and then after a period, to set a ceiling on that rate for the remainder of the season. Thus at the moment Senwes charges farmers a daily rate for any period of storage up to 100 days, and thereafter it caps this rate at the cost of 100 days of storage and thereafter the farmer can store for free until the end of that season. Once the new season begins the storage is charged again on a daily rate. This is referred to as the 'capped tariff' as the tariff is capped at 100 days of storage. Thus to illustrate this point, a farmer who stores for 99 days will be charged 99 x the daily cost of storage, a farmer who stores for 199 days (assuming this is still in the same season) will pay the capped rate viz. the equivalent of 100 x the daily cost of storage- the storage for the last 99 days will be for free.

[30] See transcript page 73.
[31] Booyens transcript page 1195
[32] According to Booyens a large farmer will produce somewhere between 20 to 30 thousand tons per annum, whilst the smallest produce between 200 to 400. See transcript page 1194
[33] Booyens, see transcript page 1210. Van Tonder, transcript page 847.
[34] See transcript page 243, evidence of Konrad Keyser and Safex website.

[31] Up until May 2003, the capped tariff was a feature of all silo owners rates, and was offered to storage customers regardless of whether they were farmers or traders. In 2001 an option for farmers to defer the decision as to whether they wanted to opt for daily storage or annual storage was offered.[35]

[32] In May 2003 Senwes removed the capped tariff from traders and offered it only to farmers.[36] This new tariff has been referred to in this case as the 'differential tariff' as the tariff is differentiated on the basis of whether the customer is a trader or a farmer. Where farmers who stored under the capped tariff sold to traders, the stated policy was that they could still benefit from the capped tariff and the trader would pay storage from the date of sale at the daily rate. If a farmer had not yet selected which option he preferred, he was, if still storing after 31 December, assumed to be on annual tariff and was billed accordingly.[37] The accounts were sent out on 31 December and had to be paid within 60 days of invoice.[38] A trader however who stored longer than 100 days continued to pay the daily tariff. If a farmer applied for a silo certificate then that farmer would be regarded as a trader and would be put on to daily tariff from the day of the request for the silo certificate. The reason for this is that a farmer who applied for a certificate, a pre-requisite to trading grain on Safex, was assumed to be ready to trade his grain and hence should be treated as if he was trader.

[33] There are factual disputes between the parties about the reason for this change and whether Senwes has represented its policy to farmers in direct negotiations as being different from its stated policy. To be more specific, as we shall see, the Commission suggests that around this time farmers were told that if they sold to a third party, as opposed to Senwes, they would receive a less favourable price, because Senwes would not charge them for storage or would offer a discount on storage charges, whilst traders would deduct from their offer price the full costs of storage at a daily rate.

[34] It would appear that other silo owners followed the same course of action, and denied traders the cap storage benefit, although it is not clear from the record when they did so, and whether it was done in consultation. Remi Burdairon from the trading firm Dreyfus is the clearest on this point. In his witness statement he says they did, but after the Commission commenced

[35] See transcript page 1212 evidence of Booyens. Counsel for Senwes suggested later in the proceedings that deferred tariff was available for everyone including traders. (See transcript page 1228)
[36] See transcript page 1212 evidence of Booyens.
[37] See transcript page 1213, evidence of Booyens.
[38] Booyens, see transcript page 1213.

its investigations, at least two of the silo owners, Afgri and Northwest informed him that they would be changing the structure of their charges and that the capped tariff would be available to traders as well as farmers.[39]

[35] Senwes has chosen not to alter its policy and for this reason the proceedings against them continued.[40]

[36] The trading practices of millers were also not immune from the market forces sweeping the industry since liberalisation. With control boards out of the way millers realised that they could achieve economies by using their buying power against traders. According to Nicola Theron of Econex, the Commission's economic expert, the four largest millers process 73 % of the maize and 87% of the wheat produced in the country.[41] They introduced what are called mill door contracts.[42] In terms of this contract millers invite traders to tender to supply them at a price quoted for delivery of the grain to the mill door. In other words traders have to deliver grain physically to the mill and incur the transport cost of doing so. Booyens of Senwes, suggests that the reason mills like the mill door contracts is because Safex contracts are in quantities of 100 tons, mills wanted to get grain delivered in the same quantities that they are traded i.e. units of 100 tons. However trains deliver in carts carrying a maximum of 44 tons. This lead to situations where the balance required needs to be delivered in small quantities by road at higher cost. By imposing the transport cost on to the traders, mills avoid making this their problem.[43]

[37] Although millers have storage capacity in their own silos they usually accommodate no more than they can mill in a month.[44] Typically these contracts arranged for the delivery of grain over a period of time, Keyser suggests 9 months.[45] While grain may be produced over a limited season that is less than half the year in duration there is a demand from milling companies for grain over 12 months of the year.[46] Traders, in order to win these contracts, needed to be able to supply grain over a season and not at just a specific moment in time. Accordingly the practice was to quote the mill a price as the delivery month's Safex price on the date of delivery, less or

[39] See Burdairon, witness statement file page 202, paragraph 33.
[40] Cross examination of Booyens transcript page 1401-2.
[41] See Econex report Commission witness statement file, page 261.Theron relies here on the work of Cutts and Kirsten.
[42] Booyens suggests the initiative for this came from some of the international traders ,see transcript page 1191
[43] See transcript 1190.
[44] See transcript page 1195 evidence of Booyens.
[45] See transcript 258-9
[46] See transcript page 1190 evidence of Booyens.

plus a certain amount. The amount that the trader could afford to deduct from the relevant Safex figure determined the competitiveness of the bid. In order to tender a trader needed to ensure that it had a supply of grain throughout the season – in order to ensure a competitive bid, the trader had to be in a position to lower its costs of supply. This meant that the trader needed to have grain stored at a silo as close as possible to the mill that was offering the contract. Thus, as with the Safex premium, favourable transport economics influenced where it was best to supply from.

[38] For traders who did not get the benefit of a capped storage rate this posed a dilemma for trading in the post 100 days period. Because they were paying for storage when they previously did not, their costs had increased if they had to bid against Senwes for a mill supplied from a silo located in the Senwes area. If they chose to supply that mill from a silo that was not owned by Senwes, but gave them the cap, then, unless the mill was on the fringe of the Senwes area, the traders transport costs to the mill would put them at a disadvantage again. The Senwes area is unusually well located to supply millers. Booyens suggested that 60-80% of the amount required by mills is supplied out of the Senwes area.[47]

[39] As he put it:

> *"Meaning certain areas are much better situated for certain mills and the Senwes area is one of those. Practically all the mills can be supplied … some of the best locations would be Senwes mills, not 100% but we are well situated for each and every area in South Africa."*[48]

[40] Why can traders not pass on the costs of storage post cap to the millers? This is an important question to answer and depends on the complex economics of the Safex trading market. We go on to examine this later in the decision.

[41] With this background we can now consider the claims against Senwes and the evidence against it.

Claims against Senwes

[47] See transcript 1762.
[48] See transcript 1762.

[42] Distilled to its essence the Commission's case against Senwes comprises two forms of abuse; an 'inducement' abuse and a 'margin squeeze' abuse.

[43] The Commission alleges that the inducement abuse comes about because Senwes has induced farmers not to trade with trader rivals by making representations concerning storage costs. The inducement itself took different forms. In the first place it was alleged that the annual cap was only available to farmers if they sold to Senwes. If they sold to a third party after the period when the annual cap became operative, essentially after grain had been stored more than 100 days, the farmer would have to pay storage at the daily tariff for the full period. Thus if on day 150 a farmer elected to sell his grain to a trader other than Senwes, that farmer would pay 150 days storage costs, because by not selling to Senwes he would forfeit the entitlement to the annual cap. If, on the other hand, the farmer chose instead on day 150, to sell to Senwes he would be entitled to the annual cap and hence only be liable to pay for 100 days storage. In addition the Commission alleges, even before the 100 day period, farmers were told that if they sold to Senwes in they would receive a reduced storage charge and hence that Senwes could make them a more competitive offer for their grain even pre –cap if they sold to Senwes.

[44] The Commission alleged that the inducement abuse constituted a contravention of section 8(d) (i) of the Act, alternatively 8(d) (iii), alternatively 8(c). The Commission also alleged that by charging farmers and traders a different price for the same service, namely long term storage, Senwes was guilty of price discrimination in terms of section 9(1) of the Act.

[45] In the course of the case the Commission alleged that the differential tariff constituted a margin squeeze by an integrated firm dominant in the upstream market for grain storage, so as to exclude non integrated rivals in the downstream market for trading.

[46] In all these allegations where dominance is an essential element of the contravention, the Commission alleges that Senwes is dominant in the storage market and leverages this dominance into the downstream market for trading, a market where it concedes that Senwes whilst a significant player is not a dominant player. The margin squeeze case is based again on 8(d) alternatively 8(c).

Relevant markets:

[47] In order to prove a contravention under section 8 or 9 it is necessary that the respondent firm is a dominant firm. It is not necessary for the firm to be dominant in the market in which the abuse has effects however, sometimes referred to in the literature as an adjacent market.

[48] The Commission alleges that Senwes is a dominant firm because it is dominant in the upstream market for the storage of grain in the so-called Senwes area. It alleges that it has abused that dominance in an adjacent downstream market for the trading of grain. Whilst Senwes is alleged to be a significant player in the downstream market it is not alleged to be dominant there.

[49] The market definition for the upstream market is common cause, not so for the downstream market as we go on to discuss.

Upstream market for grain storage

[50] As we noted in the background section, silo ownership was a function historically given to co-operatives and in accordance with state policy co-ops did not compete in each others areas. As a result the ownership of co-operatives became monopolies in their areas as a function of public policy at the time. When markets liberalised there was no significant private investment in silos, nor were silos once belonging to the co-operatives sold off piecemeal. Thus the virtual monopoly of the co-operative was inherited by subsequent owners, including Senwes. This is not to suggest that they are complete monopolies. In the Senwes area, a concept we shall get to later, there are privately owned silos. They are however not perfect substitutes for Senwes silos. Grain is only tradable on Safex by means of silo certificates, which are the equivalent of negotiable instruments, as the silos that issue them guarantee that on collection, the owner of the certificate will receive grain of that amount in the silo specified; e.g. 100 tons of grade 1 white maize at Mirage. In order to be able to issue the certificate the silo must be registered with Safex, and because most of the private silos in the Senwes area are not, they constitute an imperfect substitute for a Senwes silo.[49]

[49] There is one private silo that is registered with Safex in the Senwes area and that is owned by Allem Brothers. See witness statement of Shane Bird, witness statement file page 204 paragraph 4. This is confirmed by CTH who state that there are only 2 listed private silos one being Allem Brothers and the other a silo in North West.

[51] The other substitute for the concrete silo is the silo bag. Silo bags are a recent development and enable farmers to store grain on their farms in bags that have been developed for this purpose. Whilst some farmers make use of them they are by no means ubiquitous. In the first place silo bags again suffer from the limitation that private silos have - that there is no silo certificate issued in respect of the grain stored in them. Thus silo bags are only a solution to farmers who have a ready buyer who does not require the comfort of the certificate.

[52] Whilst some traders have invested in silo bags, Dreyfus being one, even it sees limitations to this as a viable strategy.[50] Shane Bird of Cargill stated that hedging stock in a silo bag would not be possible as the value of the stock in the bag would diverge from the value of the same quantity since the silo bag could not be tendered on to the exchange. The pricing distortion this creates prevents the use of a hedging strategy that is a vital component of the trading business.[51] Bird also mentions another disadvantage – because silo bags are not stored at places that are connected to millers by rail links, those utilising them cannot optimise transport costs by utilising the cheapest mode of transport to a mill.

[53] Secondly, although opinion on this subject varies, the quality of grain from silo bags is seen to be more suspect than grain stored in concrete silos, due to its exposure to the elements and rodents. They are also not a cheap option for many farmers. For this reason all agreed that despite the existence of some substitutes, the Senwes silos are not constrained by them.[52]

[54] Therefore the only constraint on Senwes, silos pricing is when another registered silo is located equidistant or nearly equidistant to some producers, who then have a choice of silo to patronise, assuming transport costs to each location are roughly equal. This constraint is not considered sufficiently ubiquitous to affect Senwes' storage prices, which remain at the level of the storage tariffs recommended by Safex.

[55] Moreover as certain witnesses have pointed out, Senwes' pricing decisions for its storage do not reflect those of a firm responding to market forces. If Senwes was facing a competitive market for storage we would expect its tariffs to be completely different.

[50] See transcript 623. Burdairon testified that there was nothing better than concrete silos.
[51] See witness statement of Shane Bird, witness statement file page 204 paragraph 4.
[52] Senwes to its credit concedes this point. See transcript page 623.

[56] Vink quotes from the research of Bayley, a policy consultant to government at the time the implementation of the liberalisation of agricultural markets, who argues that storage charges should reflect the demand at a particular place at a particular time of the season. Thus one would expect a higher tariff immediately after harvest when the demand for storage is greatest, and for this to decline as the season extends, regardless of who the customer is seeking storage be it trader or farmer. One would also expect silos which are in low demand areas to lower tariffs so as to attract customers at the margin to travel further than their nearest silo so that storage costs compensate for the transport disadvantage. Vink therefore concludes that the storage market is not competitive.[53] Keyser one of the traders familiar with overseas practice, suggested that this is how markets work in the US for silos, but that in South Africa the opposite happens.[54]

[57] Such was the concern over the market power that co-operatives could exercise over storage tariffs that at one stage following the liberalisation of agricultural markets in the 1990's the then Minister Derrick Hanekom was advised to consider either nationalising silos or regulating them; after representations from the industry that they would not abuse their dominance, no steps were taken to do so.[55]

[58] Thus it would seem that Senwes has market power over the pricing of its storage regardless of its share of the market. As it happens its market share is over 80% in the Senwes area and in this respect alone it is deemed to have market power by virtue of section 7(a) of the Act.[56]

[59] We find that the Commission is correct to argue that Senwes is dominant in the storage in areas surrounding its silos. Whether the area extends to 20km or 50 km was a matter on which witnesses had different opinions, but, it is common cause, is not material to the outcome of the case.[57] The areas surrounding the silo are contiguous as the map of the area shows. For this reason the geographic market that both parties agree comprises the Senwes area is the

[53] See transcript page 37. See also Bayley report op cit.
[54] Testimony of Konrad Keyser of Brisen transcript page 247.
[55] Evidence of Johannes Davel a former general manager of Senwes who testified for the Commission. Transcript page 158-60.
[56] That this is common cause see testimony of Booyens transcript page 1420. Senwes we are told owns 45 out 56 out of the 80 silos in the Senwes area. As per Vink T 34. There was some uncertainty as to the number of silos Senwes had. Theron testified that on its website Senwes stated it had 69 silos although in information given to the Commission it was suggested this number was 57. Transcript page 924
[57] Van Tonder suggested a 20km radius T 799, Vink thought it should be less than 50km

aggregation of all these areas surrounding the approximately 56 Senwes silos; this area is mainly located in the Free State province but extends to part of the Northern Cape, Gauteng and the Northwest province.[58]

[60] Senwes has not disputed its dominance in the storage market and indeed made this concession in its answer.[59] Nevertheless despite this concession, for reasons never really clear to us, various witnesses were cross examined about storage bags as alternatives and other possibilities for storage in the Senwes area. However at the end of the case Senwes maintained its position in the pleadings and conceded its dominance in the grain trading market in the so-called Senwes area.

[61] We thus find that Senwes is a dominant firm in respect of the storage of grain in the area referred to as the Senwes area.

Downstream market for trading

[62] Broadly speaking the downstream market in this case is the market where traders interact with farmers on the one hand and processors on the other. Here the parties are not in agreement over the market definition.

[63] The Commission has contended that the downstream market is for the physical trading of grain, and that this is a national market.[60] By emphasising the "physical" trading of grain the Commission seeks to distinguish transactions where traders purchase grain from producers and at a later stage sell to processors, as opposed to the derivative trading market where traders are speculators and arbitrageurs.

[64] Senwes argues that there are two downstream markets – one in which traders purchase grain from farmers, the so-called procurement market, and the other, where traders on-sell grain to other traders or processors. Both these markets are national contends Senwes and it is dominant in neither.[61]

[58] Complaint referral paragraph 16.1 page 13 of pleadings file. This allegation is not denied by Senwes in its answer.
[59] See answer paragraph 8, pleadings file page 242.
[60] See paragraphs 15.2 read with 16.4 of the complaint referral, pleadings file pages 12 and 14.
[61] See Senwes answering affidavit paragraphs 10- 12, pleadings file page 242.

[65] The Commission has attacked this bifurcation of the trading market into two segments, suggesting that Senwes is only doing so as a contrivance to avoid making traders compete with farmers so that the differential treatment of tariffs is not seen as price discrimination. We discuss later the subtleties of this attempted evasion in the section on price discrimination.

[66] For the moment we need to decide where the effects of the alleged abuses are felt. It is alleged that these are not experienced in the storage market itself, where the dominance exists, but in the market downstream of it where traders operate. For the Commission the bifurcation of trading into buying and selling is artificial as trading comprises both functions.

[67] The matter is complicated by the fact that not all traders function in the same way. Some operate in what is loosely termed the physical market. That is they procure grain from producers to ultimately sell it to processors, who are the next line in the vertical chain from farmer to ultimate consumer. However not all traders operate in the physical market. Some operate as pure speculators and trade futures and hedges and other exotic instruments that an organised agricultural market can offer. These traders may have never sullied their hands with a ton of grain, interacting more as stockbrokers buying and selling from other intermediaries and making their money out of the shrewdness of their trade. It is well known that a single ton of grain particularly on the white maize market is traded many multiples of the underlying grain that is represented by it, the figures vary but it can be as much as 6 to 10 times the underlying volume represented by those trades.[62] This means that most trades are not in physical grain and that the trading market as such needs to be more carefully defined to understand the nature of the alleged abuse, because the alleged abuse relates to traders exclusion from the physical trading market where they buy from producers with the view of selling to processors.

[68] Traders who do not operate in the physical market are not a constraint on the activities of those who are, because the formers' activities have no impact on the two crucial areas of concern here – the price at which traders buy from farmers and the price at which they sell to millers. Traders who operate in this physical market are clearly conscious that they do so. Keyser for instance spoke repeatedly of being in the physical market and stated that 90% of his firm's business was in the physical market.[63]

[62] As per Theron see transcript page 1133.
[63] See transcript page 322.

[69] We agree with the Commission's conclusion that the downstream market is the market for the trading of physical grain. We also agree that the market cannot be bifurcated in the manner suggested by Senwes. Traders do not buy merely to hold and they cannot trade without buying. We further agree, and this point is less contentious, that this market is national, but we have a caveat. It is clear from the evidence that in the market for physical grain a trader must source grain and then sell it to a processor. This means that the trader must incur the costs of delivering the grain from its location either on a farm or in a silo to the processor's mill.

[70] It follows that if the trader is to win a contract to supply a mill in a particular locale that whilst theoretically that trader can source supply from any location nationally, the transport cost of moving the grain to the processor may make the transaction unviable. From this perspective it is erroneous to think of the market as being national in that from the point of view of the trader in relation to the particular transaction not all sources of supply of grain are substitutable. This is a point well appreciated by Senwes and which has informed its approach to trading and storage.

[71] Booyens testified that if you tender for a mill door contract, you have to take a view on exactly where you are going to buy the grain, how many tons are close to the mill, how big is the *plaaslaai* and how much grain is already sold.[64] He went on to state that when Senwes buys grain from a farmer it already has a clear idea to which tender it will go so that it can offer the farmer a price that takes into account an appropriate transport premium.[65]

[72] Thus in the market for the physical supply of grain there is a competitive advantage to having the best location for storage. This is a relative, not absolute advantage, as in a given situation, the nearest silo to a processor may have run out of grain at the time the processor needs it, and so the next best location enjoys, relative to everyone else, the best comparative advantage. Thus while the trading market may be national, in the sense that competitors are located nationally and compete for supplying processors nationally, geography cannot thereafter, be dispensed with. Geography is relevant to comparative advantage of supplying a mill from the silo most optimally located to it, and to the extent Senwes is able to influence this to its advantage, it can create barriers to entry to rivals competing to supply processors in the Senwes area from Senwes silos. Thus whilst the downstream market is national, to the extent

[64] See transcript, page 1201.
[65] See transcript, page 1304-5.

that geography plays a role in creating a competitive advantage, Senwes is able to use this in the Senwes area, although in no other area, and to that extent competitive advantage is local not national.

[73] It is common cause that Senwes is not dominant in the downstream market. However it is not a bit player in the trading market. As Theron, the Commission's economist, noted in her report:

> *"This is confirmed by data provided by Senwes… which show that Senwes has a market share of 16% in the white maize trading market, 9% in …yellow maize.., 24 % in sunflower…and 13% in wheat. ... This data indicates that Senwes, though not meeting the benchmarks for dominance, is not an insignificant player in the trading markets. In the white maize trading market it is the largest player, in the yellow maize market it is the 3rd largest (after Cargill and Afgri), in the sunflower seed trading market it is by far the largest (the next player has 14%) and Senwes is also the largest player in the wheat trading market."* [66]

[74] During her cross examination it was suggested to her by Senwes' counsel that Senwes had only a 6.1% share based on Safex figures. Theron responded, correctly in our view, that the Safex market is a larger market than the physical market as it includes the trades of those not engaged in the physical market. The correct approach then is to calculate Senwes' share of the physical trading market as she has done.

[75] Notwithstanding this debate on the correct calculation the important point to bear in mind is that the Commission is not required to show that Senwes is dominant in the trading market. What Senwes is doing is to leverage its dominance in the storage market to perfect an exclusionary strategy in a downstream trading market. We have previously held that:

> *"There is nothing in our Act that suggests that an abuse of dominance cannot be perpetrated in one market and the effect thereof be experienced in another related market. Any contrary interpretation would mean that a dominant firm could leverage its market power from one market to another with impunity."* [67]

[76] This is also the position in European law. As Whish has observed:

[66] See witness statement file page 280.
[67] See *Competition Commission v SAA* case number 18/CR/Mar01 paragraph 36.

"It is not necessary for the dominance, the abuse and the effects of the abuse all to be in the same market." [68]

[77] In argument Senwes accepts this legal proposition, but suggests that leveraging be applied with caution and that in a leveraging case the Commission would have to show: i) the storage and trading markets are closely associated, ii) the conduct of Senwes is likely to reinforce its dominant position in the storage market iii) that Senwes enjoys some market power in the trading market.[69]

[78] We do not need to comment on the correctness of this test, because as we shall see when we examine the theory of margin squeezing, both economic theory and case law are well aligned on this point, which would suggest that propositions (ii) and (iii) above are overly restrictive.

<u>The abuses</u>

[79] We will now consider two alleged abuses in this case, the inducement abuse and secondly, the margin squeeze abuse.

Inducement abuse

[80] The case concerning this abuse dominated the proceedings, and at times, had all the drama of a criminal trial with evidence of secretly taped conversations, an admission of perjury by one Senwes witness who was then renounced by his own side.

[81] Because of a finding we will come to later concerning this abuse, we will not treat it with the same detail that the parties have.

[82] What we term the inducement abuse arose in the complaint referral as an allegation that Senwes induced farmers not to trade with rival traders by denying the benefit of the capped

[68] See Whish, Competition Law, 6th edition, page 203. Whish cites several European decisions in support of this proposition.
[69] Senwes heads of argument paragraphs 171 to176.

storage to any farmer who sold his grain to a third party trader. In other words the Commission alleged Senwes only offered the annual cap to farmers who sold to it.[70]

[83] This, the Commission alleged, constituted an act by Senwes as a dominant firm to induce its customers not to deal with a rival in contravention of section 8(d) (i). Section 8(d) (i) provides that it is an abuse of dominance for a dominant firm to engage in an exclusionary act the effect of which is to require or induce a supplier or customer not to deal with a competitor.

[84] In the alternative the Commission also alleged that the same facts gave rise to a case in terms of 8(d) (iii). Section 8(d) (iii) provides that it is prohibited for a dominant firm to sell goods or services on condition that the buyer purchases separate goods or services unrelated to the object of a contract, or forcing a buyer to accept a condition unrelated to the object of a contract.

[85] This case was premised on the fact that Senwes forces farmers who are the buyers of its storage services to sell to it as a trader in order to benefit from the capped storage.[71]

[86] In the course of the evidence at the hearing certain of the Commission's witness alleged that Senwes had made representations to farmers that if they sold to Senwes they would not have to pay storage charges at all, in contradistinction to when they sold to a third party in which case they would. Thus although in the pleaded case it was alleged that the inducement operated only after 100 days, the so called post cap period, in the hearing, some witnesses alleged that it operated throughout the season.

[87] Senwes denies that it ever made the annual cap contingent on farmers selling to it. It states that farmers are charged daily storage pre -100 days regardless of who they sell to at the daily tariff. Post 100 days all farmers are entitled to the annual cap regardless of whether they sell to Senwes or a third party trader.

[88] Senwes relies on its circulars to farmers as evidence of this policy and claims that its financial records do not show what the Commission alleges.

[70] See Complaint referral paragraph 24.
[71] See Complaint referral paragraph 29.

[89] Senwes' position is less clear in relation to discounts offered in the pre-100 day period. In a letter to the Commission, Senwes' attorneys stated that there were about 10 to 15 instances that they could find, where discounts had been given to farmers who had sold to Senwes. In its heads of argument Senwes concedes that discounting for farmers who sell to it, has sometimes taken place, but when it has, this does not constitute an abuse of dominance, but legitimate price competition.[72]

[90] Whist one might have expected that these issues could be definitively resolved by reference to the accounts of Senwes, this has not proved to be the case, largely because of the manner in which Senwes accounts for storage fees in its books. For this reason the Commission has relied on anecdotal evidence from witnesses who had interaction with Senwes trading staff to prove the existence of these inducement representations.

[91] Jac " Nan" Keyser, who was at the relevant time a farmer and a trader with CTH, testified that in October 2003 he had a conversation with Arnold Wessels, a senior grain procurer with Senwes, which he tape recorded. He also had a conversation with Alida Williams, a credit controller with Senwes, and the conversation was again recorded. Keyser alleges that the upshot of the two conversations was that he was told that if as a farmer he sold to Senwes prior to 31 December he would pay no storage charges.[73] If he sold to Senwes after 100 days he would pay the annual cap fee. On the other hand if he requested a silo certificate, something he must do to sell to a third party trader, he would be charged storage from date of delivery to the Senwes silo, and hence, it was suggested to him, a third party would need to offer him R 40 – R50 more per ton, to match the Senwes offer.[74]

[92] In the course of the conversations, Wessels suggests: *"so by implication regarding storage for a producer delivering to me and selling to me ... there will be no net effect on his price."* Keyser asks, *"so in net effect I do not pay for it"* The answer from Wessels is, *"that is correct it is an advantage"* [75]

[72] See for instance Senwes Heads of Argument paragraph 180. *"Rather, Senwes, in certain instances may choose to offer a higher selling price through the waiver of storage and handling fees."*
[73] See witness statement file page 15 paragraph 5. See transcript page 488. (Note Jac Keyser is not to be confused with Konrad Keyser the witness from Brisen.
[74] See transcript 489-90.
[75] The transcript of the call in English translation appears in the pleadings file page 256 -60.

[93] In cross examination by Senwes' counsel it was put to Keyser that when in the transcript of the conversation, Wessels uses the word *"betaal"* (pay), he meant not that there would be no payment by the farmer, but no cash payment. Keyser refutes this.[76]

[94] In his conversation with Alida Willams in October 2003, again there is a similar enquiry about the manner in which costs are levied and in the course of the conversation Keyser enquires *"…so it is better to sell to Senwes"*, and the answer from Williams is *"If you sell outside Senwes they have to give you a much better price than Senwes"* [77] In the course of the same conversation Williams seems to suggest that if he sold grain to Senwes before the end of December there would be no handling or storage charge involved.[78] She testified that when Senwes purchases grain from a farmer prior to 31 December no debit is raised in the farmer's ledger in respect of storage and handling costs.[79]

[95] Williams did not, unlike Wessels and Pretorius, who we deal with later, seek to explain the conversation by reinterpreting the ordinary language of the text. Indeed we found her to be the most reliable of all the Senwes witnesses, precisely because she was not there to defend a version. Senwes sought in argument as a result, to suggest her knowledge of events was limited, because she performed a largely clerical role. She would not be aware, it was contended that when Senwes quoted a net price, it was inclusive of the costs of storage.[80]

[96] Under cross examination, Jac Keyser conceded that he could not recall having been charged more than the annual cap when he sold to a third party.[81] It was also put to Keyser in cross examination that the fact that he might not have received an invoice for trades before 100 days did not mean that he was not charged for storage. Nevertheless, Keyser responded that this was how the tariff was understood in the market.[82]

[97] Burdairon, from Louis Dreyfus and Bird from Cargill both testified that they were under the impression that the annual cap was not available to farmers who sell to third parties. This perception seems to be based on discussions with farmers, and not from any representations

[76] Transcript 497.
[77] The transcript of the call in English translation appears in the pleadings file page 261 -63.
[78] See Pleadings file page 262.
[79] See transcript 2249 – 2250.
[80] Replying Heads paragraph 14.1
[81] See transcript 525-6
[82] See transcript 546.

they have had from Senwes directly.[83] Van Tonder another trader, from the firm Kernel Maize, had the same impression. He testified that when he quotes a farmer for grain that has been stored beyond 100 days, he includes in his quote (again a net quote) a price which takes into account the full daily cost of storage at 100 days plus. To this, cross examining counsel retorted that it was small wonder he was losing business because his perception of the true position was erroneous.[84]

[98] Petrus Kirstein a farmer from the Bothaville district testified of a conversation that he had had with Bertus Pretorius a junior grain procurer in the employ of Senwes. He had been told in the past by Senwes representatives that he had been throwing his money away by dealing with third party traders and not Senwes.[85] Kirstein had maize stored in a Senwes silo at Mirage. Sometime in November 2005 he was at Senwes in conversation with other farmers about prices. Whilst there, he met Pretorius, who had explained to him how the net price is derived from the Safex price. Pretorius suggested that *"the other guys* (meaning other traders) *were just conning*" him.[86] As a result he had asked Pretorius to prepare him a quote of what he would realise if he sold his maize to Senwes instead of another trader. Pretorius then prepared him a memorandum which became part of the record.[87] The memorandum purports to compare two scenarios of what would be realised from the sale of maize, after various deductions had been made. Under both scenarios the basic starting Safex price is the same and thereafter deductions are made for transport, storage and handling. Under scenario one which is headed *'Senwes'* the net price is R31,71 more favourable than under scenario two, which is headed '*buite'*. The difference would appear to come about because the *'buite'* was more expensive in terms of storage, the charging of commission, which Senwes under its scenario does not charge, and the cost of a silo certificate. The latter again a charge Senwes does not charge but *'buite'* (i.e. the third party trader) would have to.

[99] The Commission relied on this memorandum as proof of Senwes' inducement strategy. What it demonstrated is Senwes, under the hand of one of its own, showing a potential customer why it would not pay to sell to a trader unless they wanted to receive less money per ton.[88]

[83] See transcript 584 for Bird and 669-70 for Burdairon.
[84] See transcript 872-3.
[85] Witness statement file page 11 paragraph 5.
[86] See transcript page 713.
[87] Witness statement file page 13. Annexure PK1
[88] Interestingly this seems to be the only time a quote from Senwes could be pinned down. Booyens testified that when they were investigating the CTH complaint all the procurement officers were asked if they had given quotations

[100] In cross examination Senwes alleged that the memorandum was prepared on the basis that Kirstein had wanted to know what he would realise if he sold his maize after 150 days. Under the Senwes scenario it was postulated that he would only pay storage at the daily rate for up to 100 days after which the annual cap would apply. Thus under this scenario the final 50 days of storage were free.[89] Under the *'buite'* scenario the proposition was that a silo certificate had been issued at the outset, and the grain had therefore been stored on daily tariff for the full 150 days. Kirstein vigorously disputed that he had suggested anything about days to Pretorius. The only thing he was interested in was which trader would pay him the most.[90]

[101] There is nothing in PK1 which refers to 150 days, the capped tariff, and the fact that the '*buite'* was being quoted on the basis of a silo certificate being issued on the first day of storage. The content of the document is more consistent with Kirstein's version of the events than Senwes' propositions in cross examination. It seems highly unlikely that the farmer would want to compare two wholly different scenarios; one for storage with Senwes under cap, and the other storage with an outsider when a silo certificate had already been issued from day one. Surely a farmer asking advice after 150 days would not have applied already for a silo certificate? Surely Pretorius who had gone to the trouble of preparing his memorandum including details of the breakdown of silo certificates cost would not have neglected to note the small matter of 150 days and the fact that a silo certificate had been issued on day one, on the so called '*buite'* scenario?

[102] What is more likely is that someone has, post facto, concocted a version to support the figures that is consistent with Senwes' official version that the annual cap applies to farmers irrespective to whom they sell to. The only way to do this and to make the numbers on the memorandum work was to suggest that the '*buite'* option was costed on the assumption that the silo certificate having been applied for on day one. Given that other witnesses suggest that farmers typically only apply for a silo certificate when they are ready to sell to an independent trader, it seem unlikely that Kirstein was on the date in question (24November which would have been about 100 days, plus minus, after harvesting) asking for a comparison of this nature, if he

to anyone in writing and the answer was no. He was told that it was not the practice to give written quotations. See transcript page 1341.

[89] Cross examining counsel puts the scenario for Senwes twice the first time in a confusing manner which suggested 50 were under the cap and 100 days under annual storage. We have used his second clearer formulation which accords with what Senwes alleges its policy is. See transcript 722 and 723

[90] See transcript page 722

had already asked for a silo certificate. If he had not, why compare the situation as if he had a silo certificate from day one?

[103] Pretorius' version, put under cross examination to Kirstein, of course preceded his own entry into the witness box, since the Commission had presented its case first. This version seemed improbable even before Pretorius appeared to defend it. It crashed completely when he testified. Pretorius started off supporting the version discussed above. Mid-way during his cross examination, the Commission produced yet another tape recording. This time not the recording of a rival trader furtively tapping the conversations of Senwes, but a recording that Senwes made of its own calls. The Commission had called for discovery of all these transcripts at an earlier stage of the case. It had then had some transcribed, but they were not put into the discovered hard copy part of the record. Ambushed by the unexpected transcript, Senwes' legal team demanded that the evidence be excluded or that they be given an adjournment to allow them to deal with the new evidence. We allowed the adjournment, which because it coincided with end of our dates set down for hearings meant Pretorius was only ready to testify again some weeks later on 3 June 2008. In the meantime, Senwes lawyers were provided with the transcript of two conversations both of which featured Pretorius, one is a conversation with another farmer the other with a fellow Senwes employee.

[104] When we resumed the hearing, the once confident Pretorius was much chastened in his demeanour. Faced with the transcripts of two further conversations with himself as Senwes' interlocutor, Pretorius confessed to perjury.[91] He had, he said, misled the Tribunal. The truth was, or so he now maintained, was that he had given incorrect information to farmers and suggested that it was cheaper for them to sell to Senwes rather than to third party traders. However his confession came with caveats. His misstatements were limited to only those instances we were now aware of, and that he had done so without authorisation from anyone in Senwes.

[105] The Commission has vigorously contested the version that Pretorius was acting on his own or the probabilities that his now confessed misrepresentations, only extended to the limited cases we have been made aware of. Rather, they suggest, the probabilities are that Pretorius did this in many other conversations and that the management of Senwes were well aware of

[91] See transcript page 2400.

the representations and either encouraged them or did little to disabuse enthusiastic subordinates from doing so.

[106] The Commission was particularly critical of Booyens professed lack of knowledge of Pretorius real role, and argued, in our view convincingly, why his version was inherently improbable. Also less than satisfactory in Booyens testimony is his explanation for the manner in which Senwes dealt with the problem of the inducement complaint once it had been brought to Senwes' attention by the Commissions' investigation. Booyens claimed to have sent an email out to warn his trading desk about not misrepresenting Senwes policy to farmers, but despite the threat of a pending case against them this very important and no doubt exculpatory email has disappeared. The Commission suggests it never existed.

[107] The broad question for us is whether there was a practice by Senwes employees of making representations to farmers that storage with Senwes was cheaper because Senwes could absorb storage costs to the farmers advantage, something rivals which did not own silos, could not do. On the probabilities representations were made. The tape recordings and memo from Pretorius, which Senwes so tenaciously sought to exculpate itself from by ingenious readings until the confession of perjury, now look very implausible indeed. We draw an adverse inference from the manner in which it conducted this defence with such vigour and then when cracks appeared in their defence inconsistent with the official version suggested that this was the doings of an aberrant employee.

[108] The more probable version, is that the company at a reasonably senior level was aware of the representations, but at the same time appreciated their damaging implications for them in competition law, and sought to deny them for as long as was reasonably plausible, and when it was no longer, very late in the day, let one individual take the fall.

[109] The probabilities are that Senwes traders made representations to traders to sell to their employer in preference to third party traders, significantly at a time when Senwes had introduced the differential tariff to raise the costs of rival traders after the 100 day period had elapsed. By inducing farmers to sell to Senwes and not to deal with rivals, they facilitated that strategy. What is less clear is the content of the inducements. Were they limited to suggesting that the cap only applied to sales to Senwes and not sales to third party traders, or were there suggestions that even in the pre-cap period farmers would pay less by selling to Senwes because storage would either be not charged or discounted?

[110] The evidence of the memo and the taped conversations we have, and the understanding of traders suggests both types of representations were made.

[111] On the other hand there is no evidence that any farmer was denied the cap because he sold to a third party trader, and not to Senwes, nor is there evidence of Senwes systematically waiving the daily fee when farmers sold to them. The latter piece of evidence will be impossible to establish because of the way Senwes accounts for storage fees in its books. When farmers store beyond the 31st December it is assumed that they are on the annual cap rate and they receive an invoice within 30 days. However if a farmer sells before that to Senwes, there is no charge for storage in the farmers ledger account. The evidence of Booyens is that farmers are quoted a net price the so called "*boer prys*" by Senwes procurement officers. This price is the Safex price, net of storage, handling, commission, the transport differential and takes into account as well any transport premium.[92] The farmer however is not aware of what these deductions are, only the net price he will be receiving – seemingly because what he gets in his pocket is all he is interested in. At best farmers will compare one trader's net price with one another without any knowledge of its composition. This allows Senwes to grant greater discounts for storage than actual costs and it seems in an extraordinary frank passage during Booyens cross examination [**CONFIDENTIAL**].[93]

[112] The Commission's case on inducements therefore turns on oral representations, which in turn fed into perceptions which spread throughout the community of farmers and traders in the Senwes area. Given that this community is small and interact with one another regularly, it is probable that representations even if made only to a small group of people (we don't indeed know how widespread they were) would have spread throughout the community rapidly.

[113] Senwes was doubtless aware of this and did nothing to correct it, and on the contrary, seemed to have discretely encouraged, through the Pretorius' and Wessels' in its employ, the making of such representations. The incidence of the differential tariff would have bolstered the credibility of this perception. After all if Senwes had taken the cap away from traders, that everyone was aware had previously been offered to them, it was small wonder that market

[92] Booyens transcript page 1302.
[93] Booyens transcript page1309.

participants would believe, even erroneously, that the cap was only available to farmers who sold to Senwes.

[114] Despite the controversy this must have had in a small market, despite the complaint to the Commission from CTH, Senwes did little to disabuse the market of its misperception. It has hung tenuously on to its opaquely worded circulars to farmers as if they were the panacea to this widely held misperception. As opaque as its communications to farmers is its accounting system. It seems clear that farmers have no idea of storage costs they incur in the pre cap period because of the manner in which Senwes accounts for storage.

[115] We thus find that on the balance of probabilities Senwes had a practice of through its traders of making farmers and other traders believe that farmers would have an advantage by selling to Senwes because it could make them a better offer because it did not apply its storage policy to own trading division as it did to third parties. This practice seems to have existed independently of the issue of the cap. Indeed it is more probable that it operated before farmers were sent their annual cap invoice – the only invoice they seem to get for storage except when they apply for a silo certificate in which case they are selling to a third party and storage would be charged on the daily tariff from the date of delivery of the grain to the silo. Thus the inducement representations on the probabilities were at their most effective in the pre-cap period when farmers who had enquired about wanting to sell grain were induced to sell to Senwes on the basis of representations accompanying the "*boer prys*" offer, which appeared to be and more than likely probably was more favourable than the price offered by rival traders for an equivalent period.

[116] These representations, by their very nature, had an exclusionary effect. By inducing customers through representations that storage would be cheaper with Senwes, customers were induced not to deal with rival traders, who did not own storage silos. Later we examine whether this practice had a cognisable anti-competitive effect on traders in the downstream market.

Margin Squeeze abuse

[117] The concept of a margin squeeze is something relatively new in the literature and case law of abuse of dominance. One of the reasons for its new found utility is that margin squeeze

cases frequently arise in the context of recently liberalised markets. As we noted in the introduction this is a feature we see in the grain industry as well. A useful definition of a margin squeeze is to be found in the work of O'Donoghue and Padilla:

> *"In basic terms a margin squeeze involves situations in which a vertically integrated dominant firm not only engages in self-supply of an input used on a downstream market, but also supplies independent third parties active on the downstream market, which are in competition with its own business."*[94]

They go on to describe that the squeeze occurs when:

> *"..a vertically integrated firm with a dominant position in an upstream market prevents its non-vertically integrated downstream rivals from achieving an economically viable price- cost margin"*[95]

[118] The Commission's case is that Senwes is a vertically integrated firm that supplies an essential input (storage), in a market in which it is dominant, to its downstream rivals (traders who trade in the physical market for grain) at price that prevents them earning a viable price cost margin in the market for long term storage (post 100 days) in the Senwes area.

[119] In order to appreciate the Commission's case on this aspect it is necessary to have some knowledge of how the futures market for grain operates, because it is the mechanics of that market which according to the Commission have facilitated the manner in which Senwes has purportedly exercised its margin squeeze, by denying traders the benefit of the annual cap.

[120] In the grain industry as we have noted, futures contracts are traded on Safex. Safex provides for different contract months for future contracts to be traded. For white maize for instance this is March, May, July, September and December. Safex will also quote the current month, also sometimes referred to as the spot, physical or cash market, which is the price that would be obtained if the grain was sold at the moment. All other calendar months are introduced

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[94] *"The Law and Economics of Article 82 EC"*, Robert O'Donoghue and A. Jorge Padilla, Hart Publishing 2006 page 303.
[95] O'Donoghue and Padilla, op cit, page 304.

20 business days prior to the new month. Once the new month is introduced it is traded in the same manner as the five hedging months.[96]

[121] Thus on the 4th November 2008 the newspaper reflected prices for white maize for the following months:

Nov 2008	1782
Dec 008	1803
March 2009	1882
May 2009	1926
July 2009	1975.[97]

[122] The reader will note from this extract that the prices for the contracts increase over time.

[123] The price quoted for white maize in November 2008 is R1782, whilst for July 2009, it is R1975. The increase in price is explained by the market building in the costs of interest in holding the maize, as well as the costs of storage. However the price of maize as a commodity is driven by a variety of factors both local and international. It is thus correct that on any given day the market reflects an increase in prices as a function of time, but it is not correct that over time prices always rise. By way of example, on Sept 30 2008, the July 2009 future had been quoted at R2099. Thus between September 30th and 4th November the price of the July future has declined by R124.[98]

[124] This minor example illustrates the volatility in grain prices and hence the risk for buyers and sellers. What Safex does is to make pricing transparent and to offer mechanisms for players to reduce their exposure to risk.

[125] How do farmers or millers use Safex in their interactions in the market? Safex on its website gives two examples. A farmer, for instance in November 2008, may be concerned that maize prices for delivery in July 2009 will be even lower when we reach 2009, than the present quoted July 2009 price. The farmer may wish to lock in that price by selling a future in July maize at the currently prevailing price i.e. the price quoted for a July 2009 future on 4th

[96] See Safex website http://www.safex.co.za/ap/docs/products/Eng_2009.pdf last visited on 29 January 2009.

[97] Quoted in Business Report on 5 November 2008

[98] According to the press report where this price was quoted the reason for the decline on the particular day was because prices had slid in the United States. (See Business Report November 5 2008, article entitled Agricultural futures and sourced from Bloomberg.)

November 2008, R1973. Let us assume in July 2009, the time when the farmer must deliver the grain on the contract, the price has, as per the farmer's pessimistic assumption, fallen from its level in Nov 2008, and is now R200 lower, at R1773. What Safex enables the farmer to do, is to 'buy back' the future at R1773 per ton, before the last trading day on that month's contract, resulting in a gain of R200 per ton. The farmer can then sell his grain on the spot market and he will realise the price of R1773. The reason that the farmer might want to go to the additional trouble of buying back the future is that the grain has to be physically delivered and delivering on a futures contract may not be to an optimal mill. Indeed he could choose to deliver to a mill located much closer to the silo where his grain is stored. Since futures contracts are dependant on delivery to the exchange the farmer might prefer to deliver locally. [99]

[126] The relevance of futures trading to this case is the effect of storage costs on Safex prices. The evidence of Konrad Keyser from Brisen is that when a trader buys grain and holds it the trader faces two costs. Firstly the interest incurred in financing the cost of purchasing the grain and secondly the costs of storage. The longer grain is held the more these costs accumulate per day. To some extent the costs of holding grain is reflected in the Safex price and hence we see that futures prices later in a season are higher than prices earlier in a season. The reason for this is the so called spread reflected in the price. The market reflects the spread between the costs of storage as it increases over the season in these increasing prices. (We should not confuse the daily price movements with this concept of spread. As the example we set out above of the November white maize prices where there had been an overall price decline from the previous day's prices, the spread on that day between the respective future contracts remained. Thus overall the prices had declined but relative to one another on the day the prices still reflect a spread across future contract prices for the season.)

[127] However according the Keyser and this is not refuted by Senwes, the market does not fully reflect these carrying costs. According to him at best the market spread is about 60 – 80% of the real carrying costs. Asked if this shows that the market is inefficient Keyser says no. The reason is that the market factors into its prices the fact that not all traders and not all areas are subject to the daily storage costs and hence the market discounts this spread.

[128] Keyser says that for this reason the spread is sufficient for trading in areas where traders still get the annual cap, but it is not in the Senwes area (unless you are Senwes) since the cap

[99] This example has been adapted from ones on the Safex website and the United States' Commodity Futures exchange website. http://www.safex.co.za/ap/education_option_strat.asp

has been denied to them. To illustrate his point he compared two scenarios; a trader who stored on daily tariff and a trader who stored with the benefit of the annual cap.[100]

[129] The assumptions were that the grain was bought in July and stored from the 1 August 2006, until the 7 March the following year. This is a period of 212 days. He assumes that other than storage costs, all other costs are equal i.e. transport financing and the Safex charge. The trader who benefits from the annual cap, pays R38 in storage, (calculated at R0.38 per day for a maximum of 100 days) whilst the trader paying the daily rate, pays R 80.56 (212 x R0.38). This makes the daily storage scenario R42.56 per ton more expensive. The net effect of both transactions, were that both were loss making, but whereas the trader with the annual cap benefit losses represent 0.46% of the costs, the trader without this benefit experiences greater losses.[101] Keyser makes the point that the trader paying storage has costs 3.3 % more expensive than the trader on annual cap. Whilst that might not seem significant, he cautions that given that margins on trades are razor thin – the average net profit seldom exceeds 1% - the transaction would not be viable on the daily storage charge. In his example Keyser has been very conservative. He examined the annual spread throughout that period between the Jul 06 and March 07 periods and found that at their greatest (and thus the figure least beneficial to his example) the spread was R82. On average during that period however the spread was R68.50 and at its lowest it was R52.

[130] Note that this example as well compares the situations of third party traders not a Senwes. Senwes would in fact have lower storage costs, based on its marginal cost of storage for that period, as Senwes does not internally transfer storage costs to its internal trading wing, and it would not pay the costs of a certificate.

[131] It thus serves to illustrate the raising of rivals costs for third party traders comparing what the world was like before the introduction of the differential tariff and the world after its adoption. To test his thesis Keyser did the same exercise for the following year and the result was the same tendency was shown.[102]

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[100] Keyser's evidence on this point is contained in Exhibit E. In the transcript he deals with this evidence from page 271 onwards.

[101] Keyser says that even though the annual cap deal still shows a loss, the deal would still be profitable, if one had a good location, as one could make up for the loss by the difference between the notional transport costs of the Safex tariff and the actual cost. Thus on his example the transport cost per Safex was R 90 per ton and the loss on annual cap was R 5.75. If the difference between the actual cost of transport and the notional cost was more than R 5.75 per ton, the transaction would be profitable.

[102] See transcript page 279-80.

[132] Although not as detailed as Keyser, other trader witnesses called by the Commission supported the thesis he advanced.[103]

[133] The importance of the Keyser thesis is that in its material terms it is corroborated by Booyens, the key witness for Senwes, on this aspect of the case. Perhaps he was at his most graphic when he explained why Senwes would not participate in mill door contracts one had to contract for a long period in advance. As he put it, if you participate in anything where there is no spread you are going to get ‘burned’ every time.[104] Later, he seems willing to concede in cross examination that traders who do not have the cap would be foreclosed in circumstances where the market did not cover the costs of the spread.[105]

[134] Booyens’ only point of difference with Keyser on this aspect is whether the Safex costs reflects storage costs for all products or only white maize. On this point Keyser was not challenged in cross examination, and so we only have Booyens’ version which we have to treat with caution, given the general unreliability of his evidence on other aspects of this case. Even on this aspect he is not wholly consistent. Having disavowed any other commodity other than white maize reflecting carrying costs, he later qualifies this to suggest there is a spread in yellow maize but that the spread is not a sufficient one to cover ones costs.[106]

[135] The Commission’s economic expert Dr Nicola Theron has supported Keyser’s testimony.

[136] Theron says that the literature suggests that there are three necessary conditions to establish the existence of a margin squeeze:

i) a dominant firm supplies an input to downstream rivals i.e. the rival is also its customer;

ii) the input must be essential in order to enable the downstream rival to compete;

iii) the input must form a substantial part of the downstream rival’s fixed expenditure.

[103] Bester, transcript page 470, Burdairon, 651, Van Tonder 830
[104] See Booyens transcript 1202.
[105] See transcript 1693-4
[106] See transcript page1691

[137] Once one has established the conditions for a margin squeeze one needs to test whether one exists. Theron testified that the literature suggests two tests. In the first test we ask whether the downstream operation of the dominant firm could trade profitably on the basis of the upstream price charged to competitors of the dominant firm. Theron says based on Keyser's evidence – the example we saw in Exhibit E being illustrative of this - they could not.[107] In the other test we ask whether the margin between the price that the dominant firm charges a competitor for access and the price that the downstream firm charges in the downstream market, allows a reasonably efficient firm operating in the downstream market to obtain a normal profit.[108]

[138] Theron says given that firms such as Brisen, Dreyfus and Cargill, who are efficient traders, cannot make a profit when they compete with the trading division of Senwes, we have a margin squeeze. She concludes that on either test, a margin squeeze in this case has been established.

[139] The literature suggests that to sustain a margin squeeze case, a number of pre-conditions have to exist. O'Donoghue and Padilla, in a useful chapter on the subject, set out these conditions as follows:

(1) The supplier of the input (or translated into our jurisprudence the dominant firm) is vertically integrated;
(2) The input in question is in some sense essential for downstream competition
(3) The vertically integrated dominant firm's prices would render the activities of an efficient rival uneconomic
(4) There is no objective justification for the dominant firm's pricing arrangements.[109]

[140] The literature on margin squeezes also suggests that foreclosure of the downstream rivals need not be total for a margin squeeze to have been established. O'Donoghue and Padillo, explain that foreclosure may be either complete, leading to the complete exclusion of

[107] See transcript page 929.
[108] See transcript page 930.
[109] See O'Donoghue and Padilla, op. cit. page 310. The authors have derived this test based on a notice of the European Commission on the application of competition rules to access agreements in the telecommunications sector.

downstream rivals, or partial, in which case the vertically integrated firm is content with restricting rivals output and obtaining a larger market share for itself.[110]

[141] Case law suggests that although the firm should be dominant in the upstream market it need not be dominant as well in the downstream market for a margin squeeze to be effective.

[142] In the Genzyme case the United Kingdom's Competition Appeal Tribunal held that:

> *"Contrary to Genzyme's assumptions, it does not seem to us an essential ingredient of such an abuse that the dominant undertaking should be dominant in both the upstream and downstream markets concerned, although that will often be the case."*[111]

[143] Whilst some economists, according to O'Donoghue and Padilla, believe that downstream market power is necessary, as the dominant firm must have some expectation of capturing the sales diverted from the foreclosed rivals, this use of the term 'market power' may be a matter of nomenclature. Under our statute, the term 'market power' has a defined meaning, and the ability to capture diverted sales is probably not a factor which in our law one could rely on to conclude a firm had market power. For the purposes of this case, it is clear that Senwes with its emptying silos in the latter part of a season does have the capacity to capture diverted sales opportunities in the latter part of the season when the foreclosure is alleged to manifest itself. Therefore to the extent that the ability to capture diverted sales is equated with market power in some of the European case law and literature, this factor is present in the present case, albeit it that we might not classify that potential in our law as market power.

[144] The literature also suggests that there is a relationship between price discrimination and margin squeezes. It is this feature that we see present in the current case. As O'Donoghue and Padilla express it:

> *"The essential point in a margin squeeze case is that a dominant firm's activities on two levels of trade offer scope for concealing what is in effect discrimination against downstream rivals that depend on it for essential inputs. The dominant firm can extract the profit at the upstream level or the downstream level or can adjust its prices either*

[110] See O'Donoghue and Padilla op. cit. pages 305-6.
[111] *Genzyme Limited v Office of Fair Trading* Case [2004] CAT4 at paragraph 534.

upstream or downstream to squeeze rivals margins. But it is also possible the discrimination is not implied but actual.

Actual discrimination by a vertically integrated dominant firm against non-integrated downstream rivals is also a form of exclusionary abuse. By charging non-integrated rivals a higher price than its own downstream business, offering them less favourable terms, or degrading the quality or speed of delivery of the input supplied a dominant firm can artificially raise rivals costs, which may, if the harm is serious enough and the rivals important to consumers, also harm consumer welfare….. The discrimination may be absolute, such as in case of an absolute refusal to deal, but it can also take the form of price and non-price regulation."[112]

[145] In analysing the European cases of discriminatory abuse, the authors make the point that the cases involve conclusions that the conduct is unlawful not merely because they involve implied discrimination, but because they involve exclusion. Later we apply this conclusion to our analysis of the Commission's price discrimination case, which involves a conclusion that the conduct is unlawful, merely because it discriminates between traders and farmers. The correct analysis to see whether the discrimination is exclusionary, because it excludes traders by raising their costs in the downstream market for trading in the post 100 day period in the Senwes area.

[146] Let us now apply the test suggested by O'Donoghue and Padilla earlier, to the facts of this case. The first requirement is uncontroversial. Senwes it is common cause is dominant in the grain storage market, is vertically integrated and also trades grain in the trading market. The second requirement is also not seriously contested. Storage in grain silos is an essential input to traders in the trading market. The third requirement is that the dominant firm's prices would render the activities of an equally efficient rival uncompetitive. Here the evidence is contested and we need to examine the issue more fully.

[147] In its answering affidavit, and in its line of cross examination to trader witnesses called by the Commission, Senwes alleged that the reason for the difficulties experienced by the non-integrated traders in the market is because they were inefficient. Senwes makes much of this in the witness statement of Booyens et al.[113] The Commission witnesses to whom this proposition

[112] O'Donoghue and Padilla op cit page 339.
[113] See Senwes witness statement file page 21 paragraph 8.

was put in cross examination, denied this, and asserted that in every respect, other than access to storage, they provided a service that was at least as efficient as that of Senwes and denied some of the factual allegations levelled by Senwes in cross examination to buttress its contentions of their inefficiencies.[114]

[148] We also heard in evidence allegations and counter allegations about whether Senwes or some of its rivals in the trading market had earned a bad reputation with traders. We need not decide this point as it is collateral to the main issues before us. On the probabilities, whilst some traders might not be as efficient in their operations as Senwes, given the number of firms that have made these allegations in common, the fact they are representative of different sizes of operations, not merely small firms, that some have been in the market for a long period, it is probable that at least some of them must be considered efficient. Given that two of the firms whose representatives testified, Cargill and Dreyfus, are amongst the largest trading firms in the world, and no suggestion was made that they were inefficient, had the same complaint about the margin squeeze created by the differential tariff, the probabilities are that an efficient trader would not be able to compete viably given the present tariff.[115] There is also evidence that these firms were responsible for new innovations in the market such as the mill door contract, - these are not the actions of inefficient firms.[116]

[149] The test could also be approached differently as Theron points out. We can ask whether Senwes trading could operate at its present downstream prices if its upstream grain division passed on the same input cost for storage that it does to rival traders. Despite the Commission asserting this in cross examination during the case, Senwes which is in the best position to present its own financial information, did nothing to refute this and appears to have conceded this. Indeed the Commission argued that Grobler, Senwes' financial witness, has conceded that Senwes treats its storage unit differently to the manner in which it treats other traders and that there is no internal storage cost recovery.[117] Absent such refutation which it was incumbent on Senwes to adduce, we can assume that these costs are not passed on to its trading arm. By extension we can infer that if the trading arm were faced with incurring the cost of paying for storage post cost it would as per Exhibit E, be constrained to offer the downstream prices it

[114] See for instance Keyser at 318-22 and Burdairon at 603, 607 and 612 of the transcript.
[115] This is a point well made by Dr Theron in her evidence, see page 930.
[116] Interestingly it is Booyens who points this out. See transcript page 1190-1.
[117] See Commission heads paragraphs 214-215. See also transcript pages 1923-1925. Although it is arguable if Grobler makes this concession directly, it is a fair inference, despite his evasive answers, that he has.

does presently and maintain a profitable margin. We therefore consider that this requirement has been satisfied as well.

[150] The requirement of objective justification, the final requirement suggested by O'Donoghue and Padilla, equates to our Act's so called 'efficiency defence'; a feature of both sub-sections 8(c) and 8(d). In accordance with our Act's schema we first have to determine whether an act has an exclusionary nature and only if it does do we consider the efficiency defence or translated into European law language, the defence of objective justification.

[151] We therefore find that the margin squeeze conduct amounts to an exclusionary act by a dominant firm, in that it has the effect of impeding or preventing rival traders downstream from Senwes' dominant grain storage arm, from competing with its own downstream trading arm.

[152] Recall the Commission has alleged that Senwes has contravened sections 8(d) (i) and (iii) of the Act alternatively 8(c). Because the onus of proving the efficiency defence varies depending on which section we make our finding under, it is appropriate that we make this finding first and then proceed to examine the efficiency defence raised by Senwes.[118]

Legal issues (section 8 claims)

[153] The Commission has prosecuted the case under 8(d)(i), in the alternative 8(d)(iii) and in the further alternative 8(c).

[154] Since we have identified the margin squeeze abuse as a separate and self standing abuse to the so called inducement abuse; we consider each one separately for the purpose of our finding.

[155] The relevance of the distinction between the two subsections is not academic. A finding under section 8(d) makes the respondent liable to a fine, and for the purpose of balancing pro and anticompetitive effects shifts the onus from the complainant to a respondent. Clearly, as we noted in <u>*SAA*</u>, the legislature considered there to be different consequences attaching to conduct that is listed in section 8(d) and that which might fall outside of that *numerus clausus,* and hence the distinction in treatment and evidential consequential consequences.

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[118] See *SAA* decision cited above, paragraphs 133-5.

[156] We have not previously had to consider the distinction between the two sections. In this case we need to consider more fully the dividing line between exclusionary behaviour that constitutes inducement, and therefore falls to be dealt with under section 8(d) (i), and conduct that falls short of inducement, despite being exclusionary in character, and would therefore fall under section 8(c).

[157] In theory, every act of exclusion perpetrated against a competitor could be said to induce customers or suppliers not to deal with a competitor, because one has made such dealings commercially unattractive, for instance by raising the costs of rivals. [119]

[158] However, if that was the case then the distinction the legislature sought to draw by its separate treatment of 8 (c) and 8(d) would be lost. There must therefore be a qualitative difference between an abuse constituting (d) (i) inducement and more general exclusionary acts.

[159] Comparative case law is not helpful to us because the schema of section 8, insofar it has provided for the separate classification, is not a feature of legislation in other jurisdictions that we know of. Section 2 of the Sherman Act which creates the monopolisation offence in US law does not specify particular conduct as constituting monopolistic conduct. Although Article 82 of the Treaty of the European Union, provides a list of conduct that might constitute an abuse, the list is neither exhaustive nor does it purport, unlike our law, to distinguish between the juristic consequences of specified and unspecified conduct. Nor for that matter is the language of section 8(d) (i) referring to inducement, replicated in Article 82.

[160] Black's Law Dictionary defines inducement as:

> "the *act or process of enticing or persuading another person to take a certain course of action..."*[120]

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[119] As we noted in *Mittall,* an earlier occasion in which we had to consider the ambit of section 8(d)(i) :
"After all, on the face of it, the practice of competition consists precisely in inducement. While we can envisage – as clearly does the Act – a species of anti-competitive inducement, the facts of this case are insufficiently clear to arrive at so far-reaching a conclusion." See *Harmony Gold Mining Company Ltd and Durban Roodepoort Deep Ltd vs Mittal Steel South Africa Ltd and Macsteel International Holdings BV* Tribunal Case No 13/CR/Feb04 at paragraph 204.
In *Mittall* we did not have to distinguish between conduct falling under 8(c) and 8(d) (i).

[120] See Black's Law Dictionary 7th Edition.

[161] Whilst interpreting competition legislation is not always a matter of dictionary interpretation, but rather appreciating the underlying economic mischief the statutory provision seeks to address, in this case the definition is instructive.

[162] It would seem that section 8(d)(i) requires that the exclusionary act complained of constitutes a process of enticing or persuading a customer or supplier not to deal with a competitor. Absence the features of persuasion or enticement to either a specific customer or supplier or a class of them, the requirements of this subsection would not be met.

[163] This case offers an opportunity to illustrate where that test has been met and where it has not.

[164] In the case of the so called inducement abuse the conduct of Pretorius and his colleagues sought to entice or persuade customers why they should deal with Senwes rather than another trader. From the language of their representations this is uncontroversial. They attempted to say to customers – deal with us, if you deal with our competitors they will pay you less for your grain because we can offer a better deal on storage costs. This is clear cut inducement to deal with Senwes and not with a rival. For this reason we find that the exclusionary act complained of in respect of the inducement abuse, does constitute inducement for the purpose of 8(d) (i).

[165] The same cannot be said of the margin squeeze. Raising rivals costs is one matter, but there is nothing in this conduct to suggest that it persuades or entices customers not to deal with Senwes' rivals. Indeed customers may not even be aware of what traders' terms with Senwes are. The mere fact that rivals costs are raised and that consequently they may have to make less competitive offerings to customers, does not constitute inducement for the purpose of 8(d)(i).

[166] Nor can we see how this conduct falls foul of section 8(d) (iii) which states:

"8. *It is a prohibited for a dominant firm to-*

…………

(d) engage in any of the following exclusionary acts, unless the firm concerned can show technological, efficiency or other pro-competitive gains which outweigh the anti-competitive effect of its act -

…………

> *(iii)selling goods or services on condition that the buyer purchases separate goods or services unrelated to the object of a contract,or forcing a buyer to accept a condition unrelated to the object of the contract;"*

[167] There was no evidence in the case that Senwes tied or bundled storage with trading. At best it can be stated that if the Commission had proved that the annual cap was only available if one sold to Senwes this might constitute partial bundling. However this was not established as a matter of fact, and to the extent misleading misrepresentations were made of this nature they are best captured as inducements under 8(d) (i).

[168] However we do find that the margin squeeze conduct is an exclusionary act and absent a pigeon hole to slot it into any other provision of 8(d), we find that the conduct falls to be considered in terms of section 8(c).

[169] Since we have found that one form of conduct falls to be considered under 8(c) and the other under 8(d) (i); we must consider how this affects the issue of the reverse onus created by section 8.

[170] In terms of section 8, if a dominant firm is found to have engaged in conduct that is exclusionary, it can only be found to have contravened the section, if the anti-competitive effect outweighs its *" technological, efficiency or other pro-competitive gain"* For efficiency of language we will refer to this phrase as the 'objective justification' for the practice. Once a justification is alleged the Tribunal must perform a balancing exercise to weigh up the anti-competitive effect versus the justification. Because in many cases this may be a difficult exercise to perform, the Act varies the onus in this respect depending on whether the case is brought under the general section 8(c) or the specific provisions of the various sub-paragraphs of section 8(d).

[171] Under section 8(c) the Act makes it clear that the onus is on the party bringing the complaint to demonstrate that the anti-competitive effect outweighs the gain from the objective

justification. Under 8(d) it is the reverse. However even under section 8(c) it would be necessary for the dominant firm to establish the existence of an objective justification for the balancing exercise to be invoked. If it does not do so, the complainant is not required to imagine all the justifications that might be invoked and then repudiate them. This is perfectly fair, as the existence of any objective justification is one best known to the firm concerned. The complainant is not expected to mind read the respondents' defence of justification and then debunk it. Thus where a firm does not raise a defence of objective justification it will be assumed that it does not have one, and the complainant will be deemed to have established that the anti-competitive effect has outweighed any pro-competitive gain.

[172] Case law in the EU supports this approach. In the *Microsoft v Commission* the Court of First Instance recently held:

> *"it is for the dominant position concerned, and not for the Commission, before the end of the administrative procedure, to raise any plea of objective justification and to support it with argument and evidence. It then falls to the Commission, where it proposes to make a finding of an abuse of a dominant position, to show that the arguments and evidence relied upon by the undertaking cannot prevail and, accordingly, that the justification cannot be accepted."* [121]

[173] But the interpretation must go further than this. Even if the respondent firm raises what purports to be an objective justification, unless that justification, objectively considered, and before balancing takes place, is a rational justification, the balancing exercise need not be embarked on, because a defence will not been properly held to have been raised. One can only balance considerations of anti-competitive effect versus pro-competitive gain once one has two weights to place on either side of the scale. If there is no objective justification there is no weight to be placed as a counterbalance on the scale. Recall that the language in our statute is that the act in question results in a "... *technological, efficiency or other pro-competitive gain".* In other words the act of justification must possess this quality, before it can be recognised as something to be weighed on the scale.

[174] We now examine whether Senwes has raised an objective justification. We first consider this in respect of the margin squeeze abuse.

[121] Case T-201/04 *Microsoft Corp v Commission* [2007] ECR II –OOO, 5 CMLR 846, paragraph 688.

Objective justification – margin squeeze

[175] The margin squeeze case, as we noted above, is premised on the implementation of the differential tariff in May 2003, when Senwes denied traders the right to store on the annual capped rate after 100 days of storage, and required them to pay daily storage, without any option of a lesser tariff or discount for long term storage. The annual cap appears to have been in existence throughout the industry since 1997 when the markets liberalised and was available to all.

[176] Whilst in its pleadings and throughout the case Senwes has not denied the existence of this tariff, less clear is its justification for doing so. No justification for the differential tariff is offered in the pleadings. We consider this point more fully later when we discuss the pleadings, but regardless of the fact that the theory of harm in relation to the margin squeeze was not pleaded by the Commission, the justification for the tariff would still have been important even to meet the case as it was then. In all dominance cases respondent's who have an objective justification for their conduct would be expected to plead this point as it is an essential feature of section 8(c) and (d) and arguably 9(1).

[177] The next opportunity that Senwes had to deal with the issue was when it came to the filing of witness statements. Unusually, Senwes chose to file as its primary witness statement, a joint statement from three people – Dr Lubbe, the erstwhile General Manager of the Grain Division, Christo Booyens and Wikus Grobler a financial manager in the grain division.

[178] In that statement the existence of the differential cap is explained as:

> *"..largely historical, reflects Senwes' estimation of the relative capacity of each to pay and is designed to maximize the exploitation of its silo storage capacity .It gives the producer whose financial liquidity is often tight, latitude in deciding when to place grain on the trading market. Approximately 15% of the producers make use of the capped tariff. "* [122]

[122] See Senwes witness statement file page 13 paragraph 4.9

[179] During the course of the hearing of the Commission's case, counsel for Senwes had suggested to a Commission witness that there were two reasons for the cap; one was based on paternalism towards farmers and the other on so called Ramsey pricing. What the cross examiner intended it seems was to introduce the notion that price discrimination is sometimes considered welfare enhancing if firms charge customers different prices depending on their different willingness to pay. In this case it seems the intuition was that traders could be expected to pay more than farmers and hence it would be profitable to charge the former more by denying them the cap.[123]

[180] Later in the case however, when one trader witness asked the reason for the introduction of the differential, counsel for Senwes suggested to him that he would make submissions on the matter in due course.[124] Whilst counsel obviously does not have to answer to the witness, this would have been a useful opportunity to put Senwes' version for the change in practice to the witness, as the justification ultimately relied on had to deal with countering the strategies of traders. Given the witness was an experienced trader his comments on the matter would have been important. The same stance is taken in cross examination of Keyser.[125]

[181] When Senwes lead Booyens he testified on the reason for the adoption of the differential tariff putting forward what was termed the '*selecting against*' problem. This problem, which we consider in more detail below, related to the behaviour of traders in withdrawing grain rapidly from silos in the Senwes area early in the season, and leaving the rest on annual cap, in an opportunistic manner, allegedly to the disadvantage of Senwes' storage income. When Booyens was being cross examined by counsel for the Commission it was suggested that this "*selecting against*" version, had never been put in either a Senwes witness statement or in cross examination to any Commission witness.[126] Counsel for Senwes objected and said that it had been put to Vink in his cross examination.[127]

[182] It is correct that Senwes' counsel used the term *selecting against* in cross examining Vink. However the context was entirely different. Counsel suggests that when Senwes passes on a transport premium they (meaning farmers) will select in favour of Senwes and when they

[123] See transcript page 116
[124] See transcript page 676, cross examination of Burdairon.
[125] See transcript page 396. Here counsel suggest there will be evidence on the point but does not state what it is.
[126] See transcript 1245
[127] See transcript 1255

do not, they will select against them.[128] No reference to traders and their preference for withdrawing grain too rapidly out of the Senwes area.

[183] Nevertheless Senwes maintains that even if it introduced this concept late into the case this is not evidence that the defence is a recent creation. Senwes points to an internal document that existed prior to the investigation of this case which uses the term *selecting against*.

[184] Booyens was led on this document in his evidence. The document is a 2003 Senwes strategy document which the Commission had sought in a supplementary discovery affidavit, and was discovered prior to the commencement of the case. The document, which is Exhibit I in these proceedings, states (as translated by Senwes):

> *"A change in the tariff structure was made last year in terms of which only the daily tariff would be made available to purchasers….*[129]

[185] After going on to discuss that producers will still be allowed the choice between the annual ceiling tariff, the daily tariff and the deferred tariff, the document goes on to state that:

> *Silo certificates are, at all times, issued on daily tariff. This prevents purchasers from selecting against Senwes."* (Our underlining)

[186] The reference to purchasers ('kopers' in the Afrikaans) is a reference to traders. What can be derived from this extract is that the term selecting against is being used contemporaneously with the decision to introduce the differential tariff, and in the context of a discussion of that tariff. Whether the language means what Booyens later says it does is hard to fathom – the problem and the solution are not explained in this brief, rather meaningless extract. Crucially, what is unclear is whether the complaint about traders, which is to be cured by denying them the cap, is their selection against the interests of the storage or the trading business of Senwes. If the complaint is about the storage business one would expect a response that was specific to the storage business and without regard to the trading business. If the selection against meant that traders were making storage decisions that prejudiced the

[128] See transcript page 112.
[129] See paragraph 7.2.3.3 of Exhibit I a document entitled "Senwes Graan Strategiese beplanning 2004/5. Despite its title the document is dated 18 December 2003 on its first page"

Senwes trading business then the solution would be a different one and might even mean disadvantaging the storage business, if this was compensated for in higher revenues in trading.

[187] It is appropriate now to turn to the explanation given by Booyens, which now stands as the case for objective justification offered by Senwes. The Ramsey pricing and the paternalism justifications, were not pursued as justifications in the later stages of the case.

[188] We must declare upfront that we have found this *selecting against* argument very difficult to follow. For that reason in fairness to Senwes we reflect Booyens' explanation in his own words in a passage that was relied on in its heads of argument as illustrative of what selecting against means:

> *"MR BOOYENS: I think Senwes is the prime producing area and has a good location for most mills in South Africa. That simply means that grain is withdrawn very quickly out of our silos, very very quickly it is some of the first grain that goes to the mills. And we had the experience where we had the cap people would try to get their grain as quickly as possible out of the Senwes area until they reached their cap and then they would leave the grain only on the cap. So they were selecting. We always had the short end of the stick in terms of storage, so we decided to remove the cap. In any case Safex is trading has a daily storage tariff and we simply decided to animate the trading market where Safex is active as our storage rate for traders."*[130]

[189] James Hodge of Genesis Analytics, Senwes' economic expert, in his evidence deals further with the mechanics of selecting against. Hodge perfectly fairly concedes in his evidence that this is difficult to follow:

> *" I think its certainly in some of the discussion quite difficult to understand how this could actually work out, this selecting against and what I have tried to do is reflect my understanding from talking to Senwes how selecting against actually works."*[131]

[190] Hodge also prepared a table (which is page 82(b) of his report) in which he seeks to show how before the differential tariff was introduced, traders could withdraw grain from the

[130] See transcript page 1240.
[131] See transcript 2689.

silos over the season in a manner that reduced Senwes' storage income and concomitantly reduced traders' storage expenses.

[191] The problem it would appear all relates to who decides what batch of grain held in the silo by a trader goes out, when a trader decides to sell – Senwes or the trader.

[192] Prior to the introduction of the differential tariff, regardless of whether you had a silo certificate issued or not in respect of your grain, whether you were farmer or trader, you were entitled to the benefit of the annual cap.

[193] If your grain was held under a silo certificate, which you needed in order to trade it on Safex, you as the trader could decide which quantity of your grain held under the certificate you wanted to trade. Assume that you have been buying up grain steadily throughout the period. You want to sell some grain in the short term and some in the long term. To minimise your storage costs Hodge suggests that you would hold on to the grain that you stored first and then sell it last. (First in last out) This is because you know you are going to sell late in the season (post 100 days) that you get the benefit of the cap if you store for more than 100 days and therefore you have no incentive to sell in a hurry what you put in storage earliest in the season. However you also want to sell grain in the short term. Since you are liable for the daily tariff for the first 100 days, you would want to sell this grain in a way that minimises your daily storage costs. The way to do this is to use the grain that you store at later dates as the grain to trade in the early part of the season. You thus operate by selling last in first out. Thus if I started storing in early July and delivered my grain purchases on a weekly basis throughout July and August, if I wanted to sell a quantity in August, I would withdraw from my August quantities not my July ones, to reduce the incidence of daily storage. Since I know I am doing business in the post cap period and I get the annual cap I may as well use my July quantities to sell in the post cap period, since by then my storage costs would have evened out – all are on the cap irrespective of when I delivered then. Hence by doing so in Senwes parlance I am selecting against.

[194] In the alternative scenario where no silo certificate exists (what Hodge calls for reasons not clear to us the deferred system) when you decide to sell, assuming again that you have been delivering to the silo throughout the season, Senwes, determines which of your quantities of grain should leave the system first. In so doing it applies what it calls the first in first out system. Here your earliest delivery gets sold first, your second next etc. Hodge has developed a

table in which he shows that the person using the silo certificate is able to minimise costs to the detriment of Senwes; whilst the person who does not have the silo certificate, the so called deferred system person, would pay more – on his example 26% for storage. This is because Senwes cannot apply FIFO to the former but can to the latter. Hence, because FIFO cannot be applied to traders, who are all holders of silo certificates, Senwes wishes to incentivise them to apply FIFO and not LIFO, and by making long term storage now subject to the daily tariff , traders would now have an incentive to sell on a FIFO basis, because the long term storage free ride is now over.[132] With everything on daily tariff the trader will be reluctant to leave the early July quantities waiting for the post cap period. Thus without the benefit of the annual cap all traders will be incentivised to apply FIFO to minimise their storage costs.

[195] Hodges' example was never put to any trader witness or to Dr Theron, and emerged, as we noted, for the first time during his oral testimony. It is filled with assumptions all of them questionable. Would traders always sell as rapidly as he concludes, early in the season? On his calculation they are selling these first quantities in the beginning of the season so as to not incur a single day's storage. On his silo certificate example all the early storage by the trader pre – 100 days is free. This seems highly unlikely and artificial. Recall that Burdairon stated that traders need to buy early and hold as long as possible.[133] His model seems to be designed to prove the assumption not how the market may really work. Not surprisingly the Commission produced a different model premised on different assumptions which came to the opposite conclusion. In exhibit X the Commission gives an example of a scenario where income from the silo certificate customer would exceed that earned on the so called deferred tariff even when the silo certificate customer gets the annual tariff. This illustrates that by tweaking the numbers of tons stored and the periods held before one sells the differences are significant. The

[132] Hodges testimony on this is to be found in the transcript from 2688 to 2693.

[133] What the example shows is that prior to the change in regime traders (classified as such once they took out a silo certificate) could place their first 200 tons of deliveries on the cap to be sold in the post cap period. Hence for these deliveries the example shows a charge of R8000 i.e. 40c x 100 days x 200.Then it is assumed that even under the old regime subsequent deliveries on which silo certificates are issued don't remain in the silo for very long hence the R0 charge levelled. This assumption is rather synthetic as the incentive under the old regime would surely have given traders greater flexibility to keep grain in the silo for longer periods. There is the assumption that both traders and farmers both want to sell 500 tons each at the same time and keep 200 tons for later for the period after the cap in January. What the example does show is that in the event of the traders losing the cap under the new regime instead of them paying R8000 storage for the 200 tons their storage costs would rise to R11720. This is calculated as follows:
They would presumably sell their earlier deliveries first (A through E) keeping F and G for the post cap period as before and paying the daily tariff. This amounts to R6000 for 100 tons for F (150 days @ 40c up to Jan2) and R5720 for G's 100 tons (143 days @ 40c up to Jan 2) amounting to a total of R11720.
Therefore compared to the old system their costs rise by R3720 which effectively closes them out of the post cap period. With the low margins that have been shown to exist in the trading market an increase of 46.5 per cent would be prohibitive. We have evidence to the effect that since the change in regime traders have failed to operate effectively in the post cap period. This is now corroborated in the example given in 82 (b).

Commission does not allege that its example is any more accurate of what does happen, rather it is designed to illustrate that selective use of assumptions can lead to diametrically opposite results. In Hodge's scenario adopting the differential tariff as a counter to the alleged selecting against strategy makes sense, but in the one by the Commission it does not.

[196] But even if Hodge's model works for Senwes in some instances, what is pro-competitive about it? That is after all the question we are concerned with. Not only why they did it but whether it is justifies the invocation of pro-competitive gain. What is fairly clear is that it is limiting consumer choice about optimising their grain storage, but it is not increasing the supply of storage and thus increasing welfare. Rather, as we see later, traders in the Senwes area have exited the post 100 day market – whether they have changed their storage strategies in the short term is not clear. Senwes has led no evidence on this point nor did it cross examine any of the trader witnesses as to whether they had changed their storage withdrawals from LIFO to FIFO. If the loss of traders storing long term is not compensated by improvements in short term storage income it is hard to see why this strategy has benefited even Senwes.[134]

[197] There are a number of further problems with this version. If the explanation for selecting against rendered by Booyens and expanded on by Hodge, was what was meant by the 2003 strategy document, why was the explanation not given from day one of the case in the pleadings? Why not in the witness statements and why was it not put to the trader witnesses, who could most usefully have confirmed that their behaviour had changed in the way intended.

[198] Nor if this was the problem why were other strategies not considered such as a sliding charge for storage weighted more in the beginning of the season. Booyens concedes that they could have done this but cannot explain why it was not considered.[135]

[199] Nor does Senwes have any internal documents in which this strategy is contemplated beyond the cryptic passage quoted earlier. Surely a financial exercise would have been done to test the proposition and so justify the strategy change which was bound to be controversial with traders as it was? Booyens alleges that a strategy session was held in Senwes internally and one Darjan Wheatley was tasked with making a presentation.[136] The Commission requested

[134] Booyens concedes in cross examination that the benefit of the differential tariff will be lost if there is no post cap grain in storage. Transcript page 1384
[135] See transcript 1393
[136] See transcript page1270

Booyens to get a copy of this document during an adjournment in the case. When it resumed it was clear that the document that had been supplied was not the one in question and the Commission was informed by Senwes' attorneys that the relevant one could not be located.[137] Since this would have been an important document for management to have as well as crucial to Senwes' defence in this case it is most surprising that it has disappeared.

[200] Next one would expect that even if the internal documentation was no longer in existence that post the adoption of the differential tariff Senwes would have financial information to prove that the strategy had worked – that storage income had improved.

[201] The key witness on this point was its financial manager Wikus Grobler. Under cross examination, he admitted that prior to the introduction of the differential tariff, Senwes' storage income was actually increasing.[138] After the introduction of the differential tariff, Grobler conceded that it dropped, but suggested that this may have been due to some other reason.

[202] Pressed to say what, he suggested this may have something to do with crop size.[139] When the Commission suggested in cross examination that his explanation was not borne out by the data and couldn't be the proper explanation, he then said the analysis would be more complicated, and he was not in a position to do this at that moment.[140] He conceded that Senwes had not done an analysis on this point.[141] He also conceded that Senwes had not analysed whether storage income had changed as a result of the differential tariff.[142] Although he qualified this answer by saying the analysis had not been performed for the purpose of this case, it is quite clear it had not been done at all – for if it had, Senwes would have an incentive to reveal it, and if not, a duty to discover it.

[203] This response of Grobler indicates even further how implausible it is that the differential tariff was introduced as a response to the selecting against problem. Not only does Senwes not appear to have done any assessment of this strategy, to see if it was working in relation to improving storage income, but on the contrary, storage income appears to have declined, consistent with the Commission's theory of harm. The obvious inference is that Senwes did not

[137] See transcript page1499
[138] See transcript page 2588.
[139] See transcript page 2589.
[140] See transcript page 2594
[141] See transcript page 2594
[142] See transcript page 2594.

need to do this analysis, because the compensating feature was the improvement in its storage income and in particular its share of the volumes under cap. This is because that is what the differential tariff was meant to achieve.

[204] The other curious feature never explained in this case is why all the other co-operatives had adopted the differential tariff. Did they all face the selecting against problem, and if they did, why did the others abandon it in the face of the Commission investigation, when they too could have raised the justification. More likely they all adopted the policy because it would assist their trading arms in competing with non integrated trader rivals for processors in their own respective areas. When Senwes uses the term selecting against in its 2003 document the selection against being complained of is traders' choices in competing with its trading arm by having the annual cap available to them to compete for mill door contracts in the post 100 day period. By eliminating this *selecting against* Senwes has raised rivals costs in the trading market, and not as it would have us accept, improved revenues in its storage division.

[205] Thus in summary we find that even if selecting against had in 2003 the meaning that Booyens contends it does, this is not a pro-competitive justification for the practice. Senwes' conduct throughout this litigation inspires little confidence that it had much belief in this defence for if it did it would no doubt have put the same diligence into establishing it as it has into other aspects of its defence. Secondly, we find in any event that this is not the likely explanation for the introduction of the differential tariff and the Commissions' margin squeeze theory is the more probable.

[206] Since we have found, as stated above, in relation to the margin squeeze abuse that Senwes has failed to establish the existence of a pro-competitive defence, it is not necessary for us to perform the balancing test required by section 8(c). Thus, even though ordinarily, because we found that the margin squeeze case conduct constituted a contravention of 8(c), the Commission would have borne the onus of the balancing between anti-competitive effect and pro-competitive gain, we do not need to do so in this case.

Objective justification – inducement abuse

[207] In relation to the inducement abuse, Senwes has not sought to offer a justification for the conduct as being pro-competitive. Here too, no balancing exercise therefore needs to take place

under 8(d) (i). A belated attempt to do so was made in the replying heads of argument, where Senwes argued that a dominant firm was not precluded from offering a discount. This was not advanced earlier in the case where its defence was a denial of any special treatment of farmers who dealt with it save for some exceptions. It is somewhat late in the case to advance this defence and even then the discounts offered, (we assume that this can only apply to pre-cap periods as Senwes still steadfastly maintains that all are equal after the cap) given only to farmers who sell to Senwes amounts, without better justification, to using its storage business to subsidise its trading business presumably because the profits forgone in storage will be recouped by the benefits of less intense competition in trading. This, in the context of a dominant firm, is not an unambiguously pro-competitive discount. Since Senwes has the onus of establishing its pro-competitive nature, it needed to have alleged this aspect of the case far earlier so that it could be properly tested. By closing off that possibility by the manner in which it litigated this case the ambiguity must be decided against Senwes and we find that its pro-competitive nature is insufficiently established to rebut its potential anti-competitive aspect.

[208] It remains for us to consider in respect of both the inducement conduct and the margin squeeze, if the effects are sufficient to give rise to an anticompetitive effect. This has been put in issue by Senwes and was where the burden of their defence in the economic evidence went to.

Effects

[209] Although we have dealt with the abuses separately, because the factual matrix that informed them, allowed us to do so, we find it difficult to apply the same approach to the effects. The evidence on the effects was agnostic as to its cause, the inducement or the differential tariff. For this reason we must examine the evidence of effects and decide whether:

- The effects can be unpacked and attributed variously to cause viz. either the inducement abuse or the margin squeeze or are equally consistent with either; or
- If we cannot, whether the effects are more probably the result of the one rather than the other.

[210] Recall that the test for effects set out in SAA was either actual harm to consumer welfare or if the exclusionary act is substantial or significant in terms of it foreclosing the market to rivals.[143]

[211] The Commission's case is that both types of harm are manifest in this case.

[212] We go on to apply this test in considering the evidence the Commission led.

Foreclosure

1) *Evidence from traders about how the denial of the cap to them led to a change in their trading patterns in the Senwes area*

[213] Several of the trader witnesses led by the Commission testified that the change in tariff, when the annual cap was denied to them, had had adverse effects on their trading business in the Senwes area.

[214] Konrad Keyser from Brisen testified that the change came about in May 2003. He says that prior to the change he and other traders could trade competitively in the area including in the post 100 day period. He said that since the change, Brisen no longer had trades in the post cap period in the Senwes area.[144] Its trades were confined to short term transactions where grain was held for a maximum of 3 months. To illustrate his point he prepared a table of his firm's trades in the Senwes area, before and after, the change in the cap policy in 2003. Prior to the practice being changed, 71% of his trades in the Senwes area were in the short term or pre 100 day period, and the balance, 29%, were in the post 100 day period or what he termed long term.[145] After the change in the cap policy, 100% of his firm's trades are in the short term period and it has no trades in the long term. Although his figures in the table show that since 2002 his business in the Senwes area has doubled, from [**CONFIDENTIAL**] tons to [**CONFIDENTIAL**] tons he has no trades in the long term. He says that his expectation would have been that his trades in the long term would similarly have doubled and hence if the trend in the growth of his short term business had applied to his long term business, he would have

[143] See SAA paragraph 132.
[144] See transcript page 252. Keyser in fact expressed it more categorically than we have put it. He says in his witness statement that Brisen as a result of Senwes' conduct was forced to *"restructure its business"*. See transcript 267.
[145] See transcript page 254 read with the table he handed in as exhibit E1.

expected to have traded [**CONFIDENTIAL**] in the long term – instead he now trades none, a factor which he attributes solely to the denial of the cap since 2003.[146]

[215] Keyser's evidence was that the change in tariff was an issue of concern for all traders in the industry and had come up as a topic of discussion at board meetings of the industry association (SACOTA), over the last 3-4 years on which a number of the major players in the industry, including Brisen represented by him, sit. The gist of these discussions was that everyone considered they had been affected as well, and his perception was this was not a complaint of a small number of traders such as CTH, but was an industry wide concern.[147]

[216] Keyser was referred to a portion of the Genesis report where it was suggested that although the number of traders in the Senwes area had declined from 135 in 2002, to 105 in 2005, the volume that they had traded in the area had increased and thus that volumes of some traders may have been lost to others.[148] He challenged the reliability of this data. Although he could not comment on the veracity of the data in respect of volumes traded, because Senwes regards this as confidential business information and was not willing to allow him access to it, he testified that there were traders on the list who were no longer in existence at the relevant time. By inference Keyser was suggesting that if the identity of traders was unreliable, the volumes attributed were probably as well. He also made the point that the data did not seem to distinguish between short and long term storage in the Senwes area, which is his key concern.[149]

[217] Gustavus Bester of Bester Feed and Grains, a smaller trading firm, testified that in 2002 his firm procured 25% of its grain in the Senwes area, but that this declined in 2003 to 13%, came down to 7% in 2004 and was 3% in 2005 . He says he was told by farmers at the time (2002) that they could get a better price from selling to Senwes. When he asked his traders to enquire further, they discovered that Senwes' ability to offer better prices to farmers was due to preferences it granted farmers in respect of storage costs. As a result his trades in the area declined and he was sometimes forced to buy grain not from farmers, but from Senwes.[150]

[146] See transcript 255 to 256 and in cross examination 424.
[147] See transcript 266-7.
[148] Genesis report witness statement file page 94 -95.
[149] See transcript 432-3
[150] See transcript page 444-5

[218] Bester in his oral testimony is less clear than Keyser as to what he attributes this decline to. He complains in his oral testimony mostly about representations that Senwes traders make to farmers to induce them to trade with them and not other traders. He does however in his witness statement remark that the higher storage and administration costs Senwes charged other traders, made them uncompetitive *"especially if the grain was stored for longer than 100 days"* [151] Under cross examination Senwes' counsel suggested that the figures put up by Bester were incorrect and not in accordance with its records. Bester vehemently denied this and stated that this data emanated from his records and he asked to see the Senwes record. He was not given an opportunity to do so by Senwes and counsel did not press the issue further. In the circumstances we are not persuaded to prefer Senwes' records to those of Bester's. If Senwes was confident of rebutting this point it no doubt would have taken the trouble to extract the relevant information from its records and put that to Bester for his comment, rather than relying on putting instructions to the witness.

[219] Shane Bird of Cargill, mentions in his witness statement that as a result of the introduction of the differential tariff, Cargill was forced to change the way it traded in the Senwes area. Cargill had to obtain grain from other traders and brokers. He states that the amount of grain Cargill stored with Senwes declined from 53 000 tons in 2002 to 1207 in 2006. In 2007 he says that Cargill sourced only 1.3% of its requirements from the Senwes area. He stated that because of the limited margins in trading even a few rand difference taken over a large volume becomes a critical factor when producers decide who to sell to.[152]

[220] In his oral testimony Bird says that the Senwes area produces about 25% of the grain in the country. He says as a result if you want to trade large volumes you must get your hands on some of the grain produced in the Senwes area. His firm is supplying 1.4 million tons and in order to continue doing so, it must have access to Senwes grain.

[221] Remi Burdairon of Louis Dreyfus, testified that from 2004 to 2007 his firm's turnover in South Africa doubled, but that in the Senwes area it diminished by two- thirds.[153] The amount that Dreyfus stores with Senwes does not represent the full amount it purchases in the Senwes area, as it makes use of silo bags and short term purchases which obviate the need to store in Senwes silos. He says of the amount purchased post 100 days, although he did not have the

[151] See transcript page 445 and witness statement file page 313 paragraphs 3-5.
[152] See witness statement file pages 206 to 207.
[153] See transcript 599.

exact numbers at hand it was probably close to zero.[154] Burdairon emphasises the importance to traders of having the ability to hold grain over time. According to his witness statement "*a trader stands to make more money and has more opportunity to generate profits if the period between when he purchases and sells is longer.*" In oral testimony he supplemented this observation by saying that in trading a commodity a trader adds no value in the short term. The value a trader can bring to a client is by holding the commodity over a long term and since storage is an integral part of the expenses it plays a very big role especially as a trader holds for a longer time. [155]

[222] Jannie Van Zyl from Free State Maize (FSM) a small trading firm said that as a result of the differential tariff his firm was forced to diversify out of the Senwes area. In his witness statement he states that FSM's purchases declined over the past six marketing seasons, from 348 000 in 2000/1, to 70 900 in the 2005/6 season.[156] Although its overall grain procurement in South Africa did not decrease, the reason for this was that it implemented an input finance program to replace the tonnages lost from normal procurement.

[223] Under cross examination, his version that the differential tariff was the reason for FSM's diversification was challenged. Senwes suggested that a letter that Van Zyl had written to the Commission during the course of its investigation, and which preceded his witness statement, appeared to attribute the diversification to FSM's desire to reduce its risk in any one area.

[224] Van Zyl responded that this was a selective reading of his letter to the Commission. He pointed out that what he said in the letter is that FSM do not store grain for long periods in the co-ops because of the costs involved. "*In 2002 almost all the grain Free State Maize purchased were delivered at the traditional co-ops silos, currently we are moving between 30 -50 000 metric tons directly from farms to millers in the Senwes area.*"[157]

[225] In other words Van Zyl has not been inconsistent on this point. The cost of storage has driven FSM from a long term storage firm to a short term one. When asked is this not what he wants to be, his answer is that he would keep grain for more than 100 days if the *"market allows*

[154] See transcript page 600.
[155] See witness statement file page 182 and transcript page 602.
[156] See witness statement file page 37. He sets out the exact figures which show a decline through out each year of this period.
[157]See transcript page 753.

us to carry it within the storage cost component." [158] He then gave an example of a co-op which does give him the annual cap and where he used the cap tariff to store 60 000 tons for over 2 years.[159]

[226] The risk that FSM was concerned about as its letter states, was the exposure to storage costs i.e. costs imposed by the silos, precisely the kind of risk it was exposed to by storing in the Senwes area as a result of the differential tariff. This, properly analysed, is diversification informed by exclusionary behaviour, not diversification for the sake of spreading the portfolio of risk to other areas in the country.

[227] Wilhelm Van Tonder of Kernel Maize, another small trading company, although having other complaints against Senwes not pertinent to the present case, also complained that if a trader did not get the cap it was not possible to compete after 100 days. In cross examination it was put to him that although its volumes in Senwes had declined over three years prior to 2002 they had increased subsequently after the cap was introduced.[160] He then exited the physical trading market to live in Hermanus so had no subsequent data to impart. In re-examination he was asked whether he knew whether his data was for the post 100 days period or a shorter period. Van Tonder said he could not remember.[161]

[228] Theron testified that one of the aspects of a margin squeeze is that it should be persistent and that it must have a long term impact on the downstream rivals. She stated reviewing the testimony of the traders that there was evidence of *"...rather drastic decline in volumes traded by other traders in the Senwes area ..."*[162]

[229] Her conclusion is that:

> *"..long term trading in the Senwes area paying daily storage tariffs, which are not reflected in the carrying cost or in the spread, would not make any sense..."* [163]

[158] See transcript page 754
[159] See transcript page 755
[160] See transcript page 875-6.
[161] See transcript page 896.
[162] See transcript page 936
[163] See transcript page 937

[230] In response to this evidence Senwes countered with the evidence of James Hodge. The thrust of his evidence was that if one examined figures prior to 2003 and figures for years in the interim for some of the firms, the pattern that Dr Theron seeks to infer from the numbers is less compelling and may be subject to other explanations.[164] He also relies upon FSM's letter to the Commission, discussed earlier, and suggests in its case, diversification was a reason for its decline in volumes in the Senwes area, and tries to attribute this as well to Dreyfus.

[231] When cross examined on these issues, Hodge was in difficulty. For instance Hodge suggests in his document on a page 91(b) that FSM, *"acknowledge a diversification program was in place"*. Beneath this on the same slide is a remark concerning Dreyfus, *"Dreyfus was over-exposed in the Senwes area historically"*

[232] The slide clearly conveys the impression that the declines evidenced by both FSM and Dreyfus are attributable to the fact that these firms were 'over exposed' in this area and had diversified as a response to that. When cross examined on this point Hodge is forced to concede:

ADV BHANA "And contrary to what you are now suggesting, you were not posing a question here, although cryptically you were making a statement and the statement was that the reason for the decline in the Dreyfus revenue is because it over-exposed in the area. That's what you were doing. Correct?
MR HODGE: No, with Free State Mealies I'm quite explicit. They have made the claim that they had a diversification program. I'm not making that claim in respect of Dreyfus.[165]

[233] He is then pressed by Mr Bhana from the Commission to state whether he will concede that what is stated in respect of Dreyfus in his report can be disregarded and after much pressing he states: *"I do not know if Dreyfus has a diversification program. Yes that's correct."*[166]

[234] Whilst Hodge has had regard to all the data supplied to the Commission by traders the same cannot be said to his approach to the explanations given by traders. He has had no regard to any explanations given in respect of this data by the traders in their witness

[164] Table 8 of his original report, witness file page 91, and new data he introduced at the time of his testimony, pages 91a and 91b.
[165] See transcript page 2824
[166] See transcript page 2826

statements and their testimony. However in the case of FSM who in the letter to the Commission might have been said to have offered the only explanation for their decline in the Senwes area that might suit his client's case he does take into account the explanation. But even in relation to that explanation, as we have seen, he reads the letter selectively and ignores Van Zyl's testimony about it. He then appears to attribute this risk spreading explanation to the declining figures of Dreyfus, who had never even hinted at diversification.

[235] Theron was willing to concede to Genesis that the trend in the data was not always consistent with a pattern of falling sales in the Senwes area post 2003. However she says this is not sufficient to reject the notion that the data demonstrates an adverse effect. Because the volumes by some traders are very low a downward trend can be reversed by just one or two transactions. This is not enough to negate the existence of the trend. More important is the fact that the figures for some traders such as FSM and Dreyfus show drastic results, and that large traders are trading such small volumes in the Senwes area, whilst Senwes is increasing its volumes. Looked at holistically she concludes that traders are trading less and Senwes is getting the benefits.[167]

[236] Whilst Theron has been willing to consider the evidence of the change in trading patterns in totality, including evidence inconsistent with the trend she is seeking to advance, the same cannot be said of Hodge, whose evidence on this point we find to be both selective and unreliable. In the result we prefer to accept Theron's evidence on this point and agree with her well motivated conclusion that the evidence shows that traders have been excluded from the Senwes area most notably in the post cap period and that Senwes has been the beneficiary of the volumes traders have lost.

2) *Evidence about the change in percentage holdings in grain under the cap indicating that Senwes' share of grain under cap in the Senwes area had as a percentage increased substantially at the expense of traders*

[237] Theron has, reworking Genesis' figures, come to the conclusion that of the post cap volumes more than 90% of them go to Senwes.[168] However on average, when one includes both pre and post cap volumes, Senwes purchases 70% of the grain in its silos. Theron argues

[167] See transcript page 975-6
[168] This reworking is part of a series of graphs and tables to be found in Exhibit G.

that this means that Senwes purchases proportionately higher in the post cap period than it does overall.

[238] She then goes on to examine trends in trading grain for which a silo certificate is issued in the post cap period, or what she refers to as the capped volumes. She makes the assumption that all capped volumes for which a silo certificate is issued go to traders as Senwes trading has no need to issues certificates to itself. This is an assumption shared by Hodge. Theron shows that the proportion of capped grain in the Senwes silos for which a silo certificate has been issued has declined dramatically in the period 2001/2 to 2006/7. The most dramatic decline occurs in 2002/3.[169]

[239] This would illustrate, she suggests, a trend in which less of the volume is being sold to traders in the post cap period and it follows that more must be being sold to Senwes. Thus over the period in the two key categories, Senwes' post cap share of white maize goes 79% to 85%. In yellow maize Senwes goes from 77.5% to 86%.[170]

[240] Theron goes on to show that Senwes' share of the crop traded in the Senwes area has gone up from 44,6% in 2001/2 to 75,8% in 2006/7.[171] While she says that the traders' declines might not be solid enough to show a pattern, because the volumes they trade are so low, the increase in Senwes' volumes indicates a trend that can be relied on. The fact that large traders such as Cargill and Dreyfus do such low volumes in the Senwes area, in comparison to their national figures, suggests the existence of an exclusionary effect.

[241] Hodge has countered this argument by suggesting that post cap volumes are *de minimus* and hence not sufficient to come to the conclusion that there is evidence of an anticompetitive effect. He suggested that the post cap volumes account for only 9% of the grain in the Senwes area and only about 2-3% of the national crop.[172]

[242] Theron has a number of responses to the de minimus argument. She points out that even if the Genesis methodology is correct, which she disputes, the average figure of 9% for all

[169] Page 2 of Exhibit G.
[170] Page 5 of Exhibit G.
[171] Page 10 of Exhibit G
[172] Genesis report witness statement file page 73.

grain disguises the fact that the two key maize crops (white and yellow) have volumes that exceed 9%.

[243] She says the methodological error by Genesis is to consider the amount under cap as a percentage of the total Senwes volume.[173] If one is to ascertain the amount foreclosed to other traders then one wants to have regard to the amount that is under cap in the Senwes silos. Reworking the figures this way on page 7 of Exhibit W, she comes to the conclusion that the amounts are higher than 9% and in some years range between 15 and 20%. Keyser of Brisen had suggested that this volume was about 20 to 25 % and Burdairon of Dreyfus estimated 20-30%.[174]

[244] The next thing she notes is that over the period there is an increase in post cap storage from 2003 onwards.[175] Although a decline is noted in 2006/7 she suggests that the explanation for this was it was a bad crop year in the Senwes area.

[245] The final point that Theron makes on the de minimus argument is that it is not simply a matter of the quantity of the grain under cap one holds, but also its value to the holder. Evidence of Professor Vink and Burdairon is that the post 100 day period is typically the most lucrative, because prices rise during that period of the season before the next harvest. Burdairon had explained that traders make more money the longer they can hold grain.[176] For all these reasons Theron concludes that the amounts under cap are not de minimus.

[246] We would agree with this approach. It is worth noting that the volumes stored under cap may also increase depending on price formation during a season, because if prices are thought to be low post harvest, traders may want to store pending the latter part of the season in case prices rise, as we observe from page 8 of Exhibit W, where in 2005/6 where such an occurrence took place; then the volumes under cap were several factors larger than in a season such as 2001/2. Given the volatility of agricultural markets to conclude on the basis of a small data set that the amounts are de minimus would be cavalier indeed. We find that the amount under cap

[173] See transcript page 962.
[174] See transcript page 963. See also the following Exhibits which were put to Hodge in cross examination i.e. at a time after Theron had testified, but which were based on her reworking of his figures. In Eexhibit Z, the Commission suggests that Senwes market shares in its own area exceed its national market share, for white and yellow maize, suggesting that the reason for the discrepancy is that other traders are excluded from the market in the Senwes area. See transcript page 3043. In exhibit Y the Commission suggests a huge amount of capped grain is sold to Senwes and a very small quantity sold to third parties. See transcript 3038.
[175] Exhibit G page 8
[176] See transcript page 963

is not de minimus and that the trends illustrated by the growth in Senwes' share of the capped storage against that lost to traders over the period is again consistent with the anticompetitive foreclosure effects alleged in the margin squeeze abuse allegation.

3) *Evidence of two tenders that Senwes won which the trader witness alleged could only have been done because of the effects of a margin squeeze on them*

[247] Konrad Keyser of Brisen testified that he had recently lost a tender for delivering maize to Tiger Brands a processor located in Randfontein as part of a so-called mill door contract.[177] His firm had tendered at the Safex price less R10.00 delivered. Quoting a price derived from the Safex price is apparently the manner in which these prices are quoted for mill door contracts. He was told by the procurement officer that part of the tender had been awarded to Senwes (the balance had gone to Unigrain) who had tendered at Safex minus 20.[178]

[248] Keyser testified that his firm could not have made a profit tendering at this amount. He excludes the possibility of Senwes being able to make a more competitive offer by taking advantage of the transport differentials.[179] His view was that 70% of the grain was delivered by rail from the Senwes area. He says there is no silo in the Senwes area where the transport differential to Randfontein would have been sufficient to account for a price that low. In other words he concluded that Senwes could only have made an offer this low, if the difference between Brisen's offer and Senwes' was attributable to another saving, that Senwes could make, but Brisen could not. He drew the inference that this must relate to savings on storage and handling, because these are costs which Senwes could avoid charging to its own trading division, whilst its rivals would have to pay them. The Senwes response to this in cross examination was to suggest that the tender had been made in error and was not profitable as it had miscalculated.[180]

[249] Booyens did not take the matter much further in his evidence. It is not clear whether he could recall the Kroonstad tender. His general explanation seemed to be that Senwes was a late entrant to the mill door business and so competed very aggressively in the beginning.[181]

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[177] He gives no date, but he is testifying in November 2007

[178] See transcript 299.

[179] Recall that as we explained earlier the Safex transport differential is often higher than the cost for which grain can be transported by a trader in particular circumstances.

[180] See transcript 429

[250] A similar event is described by Burdairon in his witness statement. Burdairon states that up until 2004 Dreyfus was the largest supplier of grain to the World Food Program (WFP). In the 2004/5 season the WFP put out a tender again, and although Dreyfus tendered it was unsuccessful with the award going to Senwes. He believed that this was due to the fact that Senwes knew exactly at what prices his firm would bid and where his grain was stored in its silos. Armed with this information he says Senwes was able to undercut his bid. Burdairon suggests that discriminatory costs in storage enabled Senwes to undercut rivals.[182]

[251] Theron relies on both instances as symptomatic of the effect of the margin squeeze on rivals' ability to compete with Senwes.[183]

4) *Evidence that Senwes was winning more post cap tenders than it had prior to the removal of the cap.*

[252] In its report Genesis argued that there was no evidence from mill door contracts that Senwes was able to charge higher prices to mills as a result of facing less competition. In order to prove this theory, Genesis took data from Senwes for its tenders to Premier's mill in Kroonstad. The reason for this selection was that Kroonstad lies in the heart of the Senwes area and thus mills in this area were less likely to source grain from other silo operators. Thus Kroonstad is selected as being in the heart of the area that Senwes could most easily monopolise. In table 11 of its report, Genesis seeks to show that:

> *"the general trend is a decline in the Safex premium for the particular Safex delivery month and physical delivery month for the Kroonstad mill. This indicates a more competitive trading market over time and the inability of Senwes to reduce competition in the period."*[184]

[253] At the same time in the report Genesis concedes that:

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181 See transcript page 1199, Booyens goes on to explain that in early mill door contracts during the *'plaas laai'* period they tendered very aggressively because they did not know this market yet and wanted to make sure they got in. This is in response to a question about the 2005 Kroonstad contract when they tendered lower than everyone else. Booyens doesn't appear to know that this was the contract in question because he says, *"I don't know which one you exactly you refer to, but we were very aggressive in the harvest period this because we had our learning curve and we participated in the market, Sir."*

182 Witness statement file statement of Remi Burdairon paragraph 32 and transcript pages 605 to 606.

183 See ttranscript pages 939-40.

184 See Genesis report, witness statement file pages 99-100.

"Specific tender prices at different points in time will still be subject to variation given that they will be influenced by specific market conditions prevailing at the time of the tender. As a result it is difficult to draw particular lessons from individual data points."[185]

[254] Yet notwithstanding its own caveat, Genesis still seeks to derive the general trend we quoted earlier. We have great reservations about whether this table can be relied on to negate the evidence to the contrary. The data has not been verified by anyone else for accuracy and, most importantly, was not put to trader witnesses to comment on given that they would have been in the best position to vouch for its accuracy. Doubtless Senwes would say that it is confidential information and hence could not be put to them. Whilst that may be true at the time of the tenders, the pricing is now historical. As a piece of evidence to confront traders with it would have been useful to show that pricing for mill door contracts was still keen, notwithstanding traders' contentions to the contrary. Most importantly we do not know what other traders were tendering at to make a meaningful comparison. Since evidence about pricing competitiveness is an exercise in comparison, without it, we cannot come to conclusions about trends.

[255] The Commission whilst not being in a position to verify this data nevertheless performed its own exercise using Genesis' figures to come to a different conclusion. It produced a table, Exhibit W, which used these figures to suggest that Senwes wins more tenders at Kroonstad in the post cap period than it does in the earlier periods. Exhibit W shows that in the pre-cap period from May to July, Senwes wins 46,67% of the tenders, this figure is 40% for the period September to December, but in the post cap period, between December and March of the following year, the figure doubles to 85%. This again is consistent with the evidence that traders find it more difficult to tender in the post cap period because of the effects of the margin squeeze created by the differential tariff.

[256] Whilst not wishing to overemphasise the importance of this data set, the Commission's use of it has greater utility than Senwes. The Commission demonstrates that this data set is consistent with its other evidence on effects and its overall theory of harm. It can make this point without that data needing the kind of additional analysis that is required to validate the Senwes point, as the Commission' s point is a less ambitious one. It seeks to use Senwes, data to make

[185] See Genesis report page 99.

observations about Senwes' itself and not about Senwes vis- a- vis other trader competitors whose data we do not have.

5) *Consumer welfare. Effect on farmers and effect on mill door contract prices.*

[257] The Commission's effects case is not confined to foreclosure. The Commission also led evidence of the harm that the margin squeeze practice was having on consumer welfare. The best evidence on this point was that of Shane Bird of Cargill. Bird explained in relation to Senwes' Wesselbron silo, that because traders were denied the annual cap they were not in a position to make as competitive an offer to farmers for Wesselbron maize.[186] As a result Senwes could always make the best (i.e. highest bid), but he argued that that bid was probably still lower than what it could be in a competitive market, because if traders were afforded the annual cap, their storage costs would be lower, and they could then compete in bidding with Senwes more competitively from a reduced cost base, which would mean higher prices for farmers. On the flip side he argued that once Senwes had secured the grain in the area, buyers for grain in that area (i.e. processors) had only Senwes to buy from, because other traders had not been able to secure grain in that area. This means that in relation to the competition Senwes has now a locational advantage in relation to the supply of that grain.

> *"All of a sudden the maize in that silo, the prices become distorted and it has become distorted because of these practices."*[187]

[258] Bird's evidence is not challenged in cross examination by Senwes. Once counsel has established that the practice he is complaining of is the fact that Cargill does not get the capped tariff, he says he has no further questions of him.[188]

[259] However, Senwes' own witness, Booyens, testified as to the extent of Senwes' pricing power over a mill, when it was the only trader with grain in the vicinity.

> *MR BOOYENS: Because you know the mill is short and we have the grain and he can't really rely on most of the others, because they probably don't' have grain lying close by.*

[186] See transcript page 593 -5.
[187] See transcript page 594
[188] See transcript page 595. No doubt this posture was adopted by counsel due to Senwes' posture that this evidence was not relevant as it was not part of the case pleaded by the Commission. We discuss this more fully below.

So we simply increase the premium to the mill. Where we would normally supply at Safex... let's say the former deals were done at Safex, straight Safex and we have managed to add another R 20.00 premium to that."[189]

[260] Theron summarises the evidence by saying that consumer welfare is harmed in two respects. Farmers do not receive a competitive offer for their grain and thus prices may be too low affecting production decisions, as freed of the cost disadvantage, rival traders could make better bids than they do at present. On the other side of the transactions, processors will pay more for grain as traders are less competitive in tenders against Senwes than they might have been absent the storage costs created by the differential tariff.

[261] Although the evidence on the effect on consumer welfare is largely anecdotal, it is consistent with the theoretical framework of the margin squeeze case, which is that rivals price-cost margins are reduced. This means that they are being squeezed in terms of their competitiveness on both the procurement and sale side of the market. In the pre-cap period however, it is less likely that the practice has affected traders' ability to procure competitively from farmers as they do not have to face long term storage costs here. However, in the post cap period, this will make them less competitive in bidding because they now have to factor this cost into their offers to farmers. On the selling side the effect on consumer welfare is again more likely to be one in the post cap period than in the pre-cap period. Booyens testimony as to how margins can be raised to a mill if there are no other competing bids is illustrative of how this pricing power can be exploited. Contracts that would have been concluded at a price that was a discount to the prevailing Safex price could now be concluded at a significant premium to it.

Conclusion on effects.

[262] In our view the case on effects as concerns the margin squeeze is supported by the evidence we have discussed above. The data of the long term storage increases in Senwes silos (Exhibit G) and the data on tenders (Exhibit W) is consistent with the evidence given by the traders of the decrease of their presence in post cap trading in the Senwes area, and is consistent with the theory of harm advanced by Keyser. What makes this evidence so robust is

[189] See transcript page 1356. This was not just a hypothesis. Booyens recalls a mill door contract with Tiger when he says they got a premium of R30 to R40 per ton as due to a siding failure Senwes were the only ones in a position to supply the mill at the time. See ttranscript page 1354.

that different and non –interdependent sources of data all demonstrate the same trend – in the post cap period trader rivals of Senwes show a decline in the volumes they trade in the Senwes area, relative to their trading nationally, whilst Senwes' fortunes manifest the opposite trend – post cap it increases its volumes traded in a manner that exceeds both its pre-cap performance in the Senwes area and it performance as a trader nationally. The finger prints of an exclusionary practice having an effect are all over the data.

[263] Keyser and Burdairon both gave anecdotal evidence of tenders lost to Senwes where it appeared that Senwes' cost advantage had made the difference. Given that both these witnesses represent efficient traders, and as witnesses made a good impression, we find sufficient evidence that the differential tariff has led to a margin squeeze for trader competitors of Senwes and foreclosed the market for them in the post cap period. The evidence is also consistent with harm to consumer welfare on both the buying side from farmers who receive too little for their grain and the processors who pay too much.

[264] The evidence of foreclosure in the earlier period i.e. the period when the daily tariff applies to all, farmers and traders is not that marked. Both the data offered by the Commission and the evidence of the traders seems to suggest that the exclusionary effect is felt post cap. Indeed this is the express evidence of traders such as Keyser who seems to concede that pre-cap they can compete effectively with Senwes both for purchases from farmers and traders. It seems here that the smaller traders have been affected, but not the larger firms. This is perhaps because the inducement abuse, certainly on the incidents we are aware of, has been targeted at smaller traders or been perceived to be more credible when directed against them. However because this evidence is weaker than that of the post cap period, which shows a marked and consistent pattern, we cannot find sufficient evidence of anti-competitive effects in the pre-cap period. This has important implications for this case. It means that we find that the inducement abuse is not proven – although there is an exclusionary act, we cannot find on the balance of probabilities evidence of a sufficient anti-competitive effect. This means that the Commission's case in terms of section 8(d) fails.

[265] On the other hand the Commission's case in terms of the margin squeeze abuse establishes that the practice has had an anti-competitive effect in both respects contemplated in the *SAA* case, it has, in the post cap period foreclosed the market to rivals, and harmed consumer welfare both in respect of prices paid to farmers and selling prices to processors.

[266] It remains for us to consider the remaining defence of Senwes that even if these effects are established they are de minimus. The case for Senwes on this is put most succinctly in the Genesis report where it is stated:

> *"The data reveals that the grain stored under the capped tariff represents roughly 9% of grain in the Senwes area and 2-3% of the national crop."*[190]

[267] Genesis go on in their report to make the observations that these figures cannot be looked upon statically. They observe that the precise amount stored under cap in any season varies depending on present prices in the market, future expectations of prices, and financial imperatives that producers might have to sell early in the season. Thus as they point out in the 2005/6 seasons prices hit record lows so producers held back more grain till later in the season in the expectation of better future prices. The table of the years surveyed by them reveals that in respect of white maize the proportion under cap, expressed as a proportion of the total crop in the Senwes area, varied from a low of 3% to a high of 17%. The low of 3 % seems an outlier in the period surveyed as well. What this illustrates is the danger in making assumptions about grain under cap being considered de minimus based on some sampling. Clearly these figures are not static over time and grain under cap tends to be increasing.

[268] Further Theron's critique of the de minimus defence, which we discussed earlier, states that Genesis figures need to be questioned as traders suggested a much higher proportion under cap, Genesis considered all grain in the Senwes area and not that in the silos only, further the 9% does not weight sufficiently for the size of the respective crops, (maize is 80% of the crop) whilst Genesis in averaging, treats all crops as of equal size , and most importantly that the de minimus exercise is premised on the quantity of grain not the value of grain, given that grain in the late season is typically more valuable than after the harvest this must be taken into account as well. One is not simply foreclosing rivals from a quantity of grain at a certain time of the season but also the most valuable time.

[269] Nor can we look at the issue statically either. The true counterfactual if the abuse was absent, would be what would producer prices be if traders could tender equally in the market for product, post cap? This would have an effect on improving prices for grain and hence producer

[190] See Witness statement file page 73.

choices to supply more of a type of grain in a season or to risk on planting more. On the other side of the market, the supply of long term competitively priced grain would also affect processor decisions about where to expand production capacity at which mill in which growing areas. Given from the evidence of Vink the centrality of Senwes as a growing area and its location to mills this means that an area with every competitive advantage for production and processing is facing sub –optimal competition in trading. This can hardly be treated as *de minimus.*

[270] But there is another reason for treating Senwes' claims of *de minimus* with extreme caution. The fact is Senwes' own conduct belies this. Why does Senwes persist in the differential tariff after the Commission initiated its investigation nationally and all other silo owners ceased the practice, knowing it might risk an adverse finding and that the Commission was seeking a fine of 10% of its turnover?[191] This suggests that viewed from the Senwes perspective the practice was not *de minimus* and indeed highly profitable and worth the risk.

[271] We find that the margin squeeze abuse has an anticompetitive effect that is not *de minimus*, forecloses rivals from the market in the post cap period and, at least in the post cap period, is adverse to the consumer welfare of producers and processors, with knock on effects to final consumers of grain products. For reasons explained earlier this means that the respondent has contravened section 8(c) of the Act.

[272] However, the anti-competitive effect of the inducement abuse is not established, and thus we cannot find that the respondent has contravened sub-sections 8(d) (i) or (iii) of the Act, which as we explained earlier, are applicable to the inducement abuse, but not the margin squeeze abuse.

Price discrimination

[273] The Commission has also relied on the differential tariff to found a case for price discrimination. In its pleadings the Commission alleges that by applying a differential tariff to producers and traders Senwes is engaged in unlawful price discrimination between these two

[191] Burdairon in his witness statement suggests that the other co-ops changed their behavior after the Commission initiated its investigation. See witness statement file page 202 paragraph 33.

classes of purchasers.[192] In her report Theron describes this as a case of third degree price discrimination.[193]

[274] Economists typically distinguish between three forms of price discrimination.[194] First degree price discrimination, sometimes referred to as perfect price discrimination, occurs when a firm is able to discriminate perfectly between all its customers by being able to have complete knowledge of each customer's willingness to pay for its goods and services. Since this degree of omniscience is seldom available to firms and in addition even if possible, would probably be rendered futile as customers would engage in arbitrage opportunities to negate its advantages to the dominant firm.[195]

[275] The second form of price discrimination relies on customers of the discriminator to self select. The text books typically use volume discounts as an example of this.

[276] Third degree price discrimination, and the one that Theron identifies as being present *in casu,* occurs when a firm is able to discriminate between some segments of its customer base, premised on some characteristic that they have in common. The most frequent example of this is movie theatres discriminating between customers on the grounds of age, by giving pensioners discounts not available to other customers. In this case the price discrimination segmentation is based on whether customers are traders or farmers and hence Theron's view that this is a case of third degree price discrimination.

[277] Senwes denied the price discrimination charge with its principal line of defence being that producers and traders were not competitors, but rather sequential in their relationship – producers sell to traders who sell to other traders or processors. They thus do not compete and so the price differential can have no anticompetitive effect.

[278] We do not need to be drawn into this debate. The true character of harm created by the price differential as we observed above was its effect on the relationship not between traders and farmers, but between Senwes and the traders in the trading market. To state the proposition differently, if Senwes were not in the trading market would there be an

[192] Complaint referral paragraphs 32-34.
[193] See Econex report witness statement file page 291.
[194] We have relied for this discussion on the useful summary of these terms in Bishop and Walker, op. cit. page 195.
[195] This is because customers who rated the good or service lower than others could re-sell the product to another higher valuing customer at a price still lower than that offered by the discriminator to the high value customer.

anticompetitive effect because traders were receiving a different long term storage price to farmers – and the answer on the facts before us would be no. Thus the harm caused by the differential was that it created the margin squeeze as it enabled Senwes to raise rivals costs and thus narrow the price cost margin afforded to them, in the context of a futures market that was not reflecting in its prices, the full long term carrying costs of storage. This theory of harm means that the differential tariff is more properly characterised as an exclusionary abuse under 8(c) than price discrimination under section 9(1). For this reason we find that the case under section 9 fails.

Pleadings

[279] Throughout the hearings and in subsequent argument Senwes has adopted the approach that it does not have to answer the margin squeeze case as this was not the case pleaded by the Commission at the outset and that it was impermissible for it to change its case in the course of the hearings without formally applying to amend its pleadings. Since the Commission never did so, Senwes argues, it is not called upon to answer this case.

[280] Senwes does not deny that the fact of the differential tariff was pleaded. What it disputes was how the consequences of this differential tariff were pleaded. It argues that in the pleadings the consequences related to the differential between producers and traders. However the Commissions' case during the hearing was about the consequences of the differential tariff on the relationship between Senwes' trading arm and its trader rivals.

[281] Senwes demonstrated its intentions at the commencement of the case when it produced a schedule entitled "Objectionable aspects of Commission witness statements". The schedule went through each of the witness statements, listing paragraphs that were objectionable either because they were hearsay, contained opinion evidence from non–experts or contained evidence on *"conduct or practices not referred."* In opening address counsel for Senwes alluded to this and stated that they would not be dealing with issues not on the pleadings. Senwes, despite its reliance on formality did not bring an exception that evidence led was not being pleaded.

[282] The Commission in defence of its right to contend for the margin squeeze, argues that its case on this point, if not clear in the pleadings, is at the very least clear from its witness

statements which were furnished in writing prior to the commencement of the hearing, and prior to the date that Senwes was obliged to furnish its own statements. Had Senwes been prejudiced by this approach it should have brought an application for the Tribunal to rule on this issue. This is precisely what it sought to avoid, seeking to indicate its attitude, but not seeking a ruling.

[283] Both parties rely on the same jurisprudence regarding the status of tribunal pleadings and so the principles are uncontroversial, it is their application to the facts of this case that is. In essence there seems to be agreement that pleadings in our proceedings lack the formality that they do in civil proceedings in a court, but that nevertheless the tribunal must ensure fairness in its proceedings.[196]

[284] We will accept that although the facts establishing the differential tariff have been pleaded, the margin squeeze theory of harm does not emerge from the pleadings. It follows that the key issue then is to consider whether that was unfair to Senwes.

[285] It is clear that if a case is led that raises issues that are not contemplated in the referral then it would be unfair to a respondent if these issues emerged at the hearing without proper notice to the respondent. Proper notice in the formal sense would obviously be an amendment to the pleadings, but this is not the only method of remedying fairness. The context is all important. If the respondent, now sufficiently apprised of the variation in the case, has an opportunity to meet the new issues, then fairness will be satisfied. Considerations that we would take into account would be the stage of the case when the variation occurred, the degree of departure from the pleadings, and the magnitude of the new issues raised relative to what the respondent would need to do to rebut them e.g. calling of new experts or embarking on a lengthy factual enquiry which it had not needed to engage in for the hearing at that stage.

[286] Applying these principles to the facts of this case we note the following. Whilst the margin squeeze case has not been expressly pleaded using these terms, the differential tariff has been pleaded as emerges from the following paragraph in the complaint referral:

[196] See American National Soda Ash Corporation v Botswana Ash (Pty) Ltd *(2001-2002) CPLR 430 at page 441 – 443*

" Alternatively, Senwes' practice of charging differential tariff fees for storage is exclusionary and has an anticompetitive effect, as it impedes CTH and other grain traders who compete with Senwes from expanding in the downstream market for grain trading and is thus is in contravention of section 8(c) of the Act."[197]

[287] Succinct this reference may be, but read with other paragraphs of the referral, Senwes would be aware what the differential tariff was, and that it had as an implication that traders costs were raised and that its effect was that traders were being prevented from expanding in the downstream market.

[288] Senwes in its plea does not seek further clarity on this point, but pleads a bare denial.

[289] It seems to be common cause that the issue of the margin squeeze as a theory of harm arises for the first time when the Commission filed its witness statements. It is given theoretical expression in Theron's report.[198] It is also given factual expression in the witness statement of Konrad Keyser from Brisen, who as we noted earlier was the key witness for the Commission on this aspect of the case.[199]

[290] Although we provided for the Commission to file its witness statements in advance of those of Senwes, we are not certain if this was the case, and even if it was, whether Senwes had at that time an adequate opportunity to respond to the margin squeeze aspect. We will assume in Senwes' favour that at that stage it did not.

[291] Despite this it is interesting to note that Genesis in its witness statement still shows an appreciation of the margin squeeze issues. Whilst noting that the Commission's theory of harm was not explicit from the complaint referral, Genesis observes in one passage that the possibilities of harm could come about from margins being reduced on the procurement and on the other side in respect of sales to processors.[200] In another passage from the same report this is even clearer:

[197] See Complaint referral paragraph 30.
[198] See witness statement file, pages 282 to 288 where this theory is comprehensively set out.
[199] See witness statement file pages 22 to 29. Curiously, and inconsistently, Senwes' objection in its schedule to Keyser's evidence objects to some aspects of the margin squeeze theory paragraphs 15,19, and 25-6, but not other facts that are part of that theory e.g. paragraphs 6,7 and 8.
[200] See witness statement file page 87 paragraph 86-7.

> *"However as the theory of harm is not entirely evident from the pleadings, this section assesses whether there is any evidence of a negative impact on sales prices to processors, It is only this side of the market that appears relevant given that it is the complaint of traders that <u>margins are being reduced on the procurement side due to the alleged Senwes practices</u>."* [201] (Our emphasis)

[292] The fact that Genesis showed an appreciation of this aspect of the complaint without it being *"…entirely evident from the pleadings"*, indicates that the theory of harm was neither exotic nor beyond the wit of persons with experience in competition economics to divine. Note that in coming to this conclusion, Genesis relies solely on the pleadings and documents discovered.

[293] Obviously once the Commission had filed its witness statements it became clear that it would be relying on a margin squeeze as one of its theories of harm.

[294] However, assuming in Senwes' favour that it felt that it had not dealt with this issue adequately in its own witness statements, what remedies were open to it at this time?

[295] The most obvious would have been to seek an opportunity to supplement its witness statements to deal with this point. This may or may not have occasioned a postponement, but even if it did, that was a course open to them. The second, as suggested by the Commission, was to bring an objection to the evidence being led. We agree that this was an option open to them because the purpose of such an objection is to enable their opponent to respond by either, (1) asserting successfully that the issues are properly on the pleadings, or (2) if not on the pleadings, that it will either amend them to reflect them if that does not create prejudice, or to drop the allegations that are the subject of the exception. This is not about formality for the sake of it, but for the sake of fairness to the other party to the case.

[296] Senwes chose not to follow either of these procedures, but instead it chose the unorthodox route of producing its schedule of material in the witness statements of the Commission that it said it was not obliged to respond to. There seems to have been an assumption by Senwes that once it had tabled its schedule it was then for the Commission to apply to lead the evidence it felt it was entitled to do. This is an erroneous approach. The party

[201] See witness statement file page 97-8 paragraph 115.

alleging unfairness has the duty to bring the matter to our attention not by the way of a refusal to engage the issue, but by way of requesting a ruling. At no stage did the Tribunal indicate that it would not consider this evidence and therefore Senwes by adopting the stance it did, risked the adverse consequences of not engaging on this issue to obtain a ruling.

[297] Senwes instead elected for tactical reasons to avoid the margin squeeze case by asserting whenever it emerged that it was under no obligation to meet it. Yet even in adopting this course it was inconsistent. Whilst for the most part when a trader witness traversed margin squeeze issues, the cross examiner signalled an unwillingness to engage the issue[202], when it suited Senwes to challenge the Commission' case on this aspect it did so. Keyser is told by counsel for Senwes at one stage in his cross examination that certain aspects will be dealt with only briefly as they are not relevant to the case.[203] Later Keyser is cross examined on issues pertinent to the margin squeeze case.[204] Some aspects of Theron's evidence on the margin squeeze are challenged, but the rest ignored.[205]

[298] Booyens was led to suggest that carrying costs were only an issue with white maize and no other product, although this assertion was never put to any traders in cross examination. Senwes used both Hodge and Booyens to deal with aspects of the margin squeeze case.

[299] The only area where, arguably, Senwes was required to lead new evidence was on the objective justification for the decision to apply the differential tariff. However even for the inducement case, and the price discrimination case, which are predicated on the differential tariff, and which it is common cause were sufficiently pleaded, objective justification would have been an appropriate line of defence for Senwes to consider.

[300] In any event when Senwes' did engage in the margin squeeze case, it offered the de minimus defence as its main defence. Since this was the same that it had in relation to the inducement abuse it did not have to radically alter its approach to the case.

[202] See for example response to Bester at 475-6, and Bird at 595, where once it is confirmed that Bird is complaining about the differential tariff he is not further cross examined on this point.
[203] See transcript page 341.
[204] See transcript pages 369 – 383 where the issue relates to the spread and hedging strategies available to traders. See also transcript 412 where counsel suggests that there are too few traders storing on after the cap to affect the spread.
[205] For example at 1135 Theron is cross examined on the rationality of using the differential as an exclusion strategy post cap and at 1156 why the market does not capture storage costs .Both extracts relate to a line of cross examination that challenges the margin squeeze theory.

[301] Nevertheless, to the extent that it needed to deal with new issues, we permitted Senwes to introduce its objective justification defence, the so-called selecting against concern, at a very late stage of the case, at a time prejudicial to the Commission, but which it nevertheless dealt with in cross examination.

[302] To summarise our application of the test we propose to the facts of this case, we note that: the amendment is not a major departure from the pleadings, the conduct has been pleaded the theory of harm associated with it was not; the theory of harm was introduced at an early stage of the case prior to the commencement of the hearing; Senwes was not required to perform major surgery to its defence to meet the new theory of harm; it did raise the new defence when it opened its case, despite not having been pleaded, and its major defence that the effects were de minimus was part of its case from the beginning and continued to be so.

[303] Thus Senwes was not prejudiced by the introduction of the margin squeeze case.

[304] To allow Senwes the benefit of its tactical election would be manifestly unfair to the Commission and the public interest in competitive markets that it represents. We are satisfied that the margin squeeze aspect of the complaint is properly before us and that there has been no unfairness to Senwes in us considering it.

<u>Conclusion</u>

[305] We find that the complaint in respect of the inducement has not been established, because although the Commission has proved that representations made by officers of Senwes amounted to inducements to customers not to deal with trader rivals of Senwes' trading arm, it has not been established on a balance of probabilities that these remedies had an anticompetitive effect. The complaint in respect of the margin squeeze has been established and we find that this amounts to a contravention of section 8(c) of the Act, but not sections 8(d) or 9(1). In accordance with our agreement with the parties we will decide remedies at a later stage after allowing the parties to make representations to us in this respect.[206]

[306] However, Pretorius' confession of perjury cannot be left ignored. The Commission is requested to report the matter to the relevant authorities for prosecution.

[206] See transcript page 3308.

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Concurring: Y Carrim and M Holden

Tribunal Researcher: Jabulani Ngobeni

For the Commission	: Adv. Rafik Bhana SC (with him Adv. P.L. Mokoena)
For the Respondent	: Adv. MSM Brassey SC (with him Adv. M.J Engelbrecht instructed by Hofmeyr Herbstein & Gihwala Inc