



## **DISCRIMINATORY CONDUCT GUIDELINES**

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# DISCRIMINATORY CONDUCT GUIDELINES

## 1.0 INTRODUCTION

- 1.1 These Guidelines are intended to be used by staff of the Competition & Consumer Authority when reviewing a case of discriminatory conduct for purposes of assessing the effects on Competition.
- 1.2 These Guidelines provide the steps upon which the assessment of discriminatory conduct can be done. It also defines the concept of discriminatory conduct and the theory upon which it is premised.
- 1.3 The document provides the general approach for the investigation of discriminatory complaints under the Competition Act, CAP 46:09 (hereinafter referred to as the Act).
- 1.4 The Discriminatory Conduct Guidelines address a number of key issues related to the provisions of the law; but they cannot anticipate all questions that may arise in the market place and may be updated from time to time to account for future developments in law and policy.
- 1.5 These Guidelines are not a substitute for the Act. They must, therefore, be read in conjunction with the Act, Regulations and other guidelines. Their purpose is to complement what is in the law.

## 2.0 DISCRIMINATORY CONDUCT

- 2.1 According to section 27(2) (b) of the Act, Discriminatory conduct is prohibited since it “applies dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage”. The application of ‘dissimilar conditions’ refers to the practice of providing goods or services at different prices or terms to different buyers, even though the sales costs are the same for all transactions. For price discrimination to happen, other entrepreneurs must be unable to purchase goods at the lower price and resell them at a higher one.
- 2.2 Discriminatory conduct is also a form of abuse of dominant position in the market and it is prohibited under section 30(1) of the Act, which states that:  
  
*Any conduct on the part of one or more enterprises is subject to prohibition by the Authority if, following an investigation by the Authority, such conduct is determined to amount to an abuse of dominant position in any market.*
- 2.3 The above section prohibits enterprises from abusing their dominant market position. That means, it is an offence or illegal to abuse the state of dominance in any market in the country.

- 2.4 Discriminatory conduct is a broad concept in competition law and economics that encompasses a number of themes, each of which entails behaviour that has the potential to adversely affect the competition process (i.e., unilateral conduct<sup>1</sup>) or similar anti-competitive behaviour by more than two enterprises (joint dominance). Instances of discriminatory conduct include, and are not limited to such conduct as listed below:
- 2.4.1 Price Discrimination (in the course of buying and selling), which includes discount on cash or quantities purchased.
- 2.4.2 Non-price Discrimination (in terms and conditions) such as:
- i. Credit terms;
  - ii. Payment terms;
  - iii. Standards;
  - iv. Delivery schedules;
  - v. Quantities to be supplied/purchased; and
  - vi. Any other non-price commercial terms.

### **3.0 THE CONDUCT OF PRICE DISCRIMINATION**

- 3.1 Price discrimination theory requires the following as necessary conditions for the conduct to be existing:<sup>2</sup>
- 3.1.1 the discriminating enterprise must have market power;
- 3.1.2 there are, at best, imperfect arbitrage<sup>3</sup> opportunities for consumers; and
- 3.1.3 under perfect price discrimination, the discriminating enterprise must be able to segment customers according to willingness to pay for each unit.
- 3.2 According to European Competition Law, the theory of price discrimination refers to the application of ‘dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage’. Competitive disadvantage in this case refers to the enterprise’s risk for losing business or customers to a competitor because of being given a raw deal. Due to that, the business would be unable to compete fairly. Therefore, according to European Competition Law, the definition of Price Discrimination addresses the absence of ‘equivalence of transactions’<sup>4</sup> for a certain

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<sup>1</sup>Unilateral conduct is anti-competitive conduct undertaken by an individual enterprise. Intervention against such conduct is done when the enterprise already has a position of dominance. (International Competition Network, Report on the Objectives of Unilateral Conduct Laws, Assessment of Dominance/Substantial Market Power, and State-Created Monopolies, 2007, <http://www.internationalcompetitionnetwork.org/uploads/library/doc353.pdf>.)

<sup>2</sup>OECD Glossary of Industrial Organisation Economics and Competition Law, <http://www.oecd.org/regreform/sectors/2376087.pdf>

<sup>3</sup>This refers to speculative trading with positive risk adjusted returns. Refer to article *Imperfect Arbitrage with Wealth Effects* by Wei Xiong (1999).

<sup>4</sup>These are business deals of equivalent magnitude, or orders placed by different customers that are of same size.

product or service in a market. It also specifically explains that Price Discrimination usually negatively affects the competitiveness of downstream customers, rather than exclusionary effects on competition.<sup>5</sup>

3.3 Price Discrimination occurs frequently and in a wide range of industries, including industries where competition is effective. Price Discrimination is a generic term that covers many specific types of pricing behaviour that can either be good or anti-competitive. Therefore, it is not necessarily the case that Price Discrimination by a dominant enterprise is abusive, especially when the favourable/lower price favours other customers.<sup>6</sup>

3.4 Price Discrimination is a form of abuse of dominance<sup>7</sup> in a market for products and services.

3.5 Abuse of dominance is prohibited under section 30(1) of the Act, which states that:

*Any conduct on the part of one or more enterprises is subject to prohibition by the Authority if, following an investigation by the Authority, such conduct is determined to amount to an abuse of dominant position in any market.*

3.6 A dominant enterprise<sup>8</sup>, as the seller or buyer of goods or services, is prohibited from practicing price discrimination, if:

3.6.1 it is likely to have the effect of substantially preventing or lessening competition;

3.6.2 it relates to the sale, in equivalent transactions, of goods or services of like-grade and quality to different purchasers without objective justification; and

3.6.3 it involves discrimination between those purchasers in terms of:

i. the price charged for the goods or services;

ii. any discount, allowance, rebate, or credit given or allowed in relation to the supply of goods or services;

iii. the provision of services in respect of the goods or services; or

iv. payment of services provided in respect of the goods or services.

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<sup>5</sup> Glossary Of Industrial Organisation Economics And Competition Law (explaining Price Discrimination), also available online at <http://www.oecd.org/regreform/sectors/2376087.pdf>.

<sup>6</sup> <http://www.internationalcompetitionnetwork.org/uploads...> The Competitive Effects of Price Discrimination. Pongracic, Ivan. Lecture on the Competitive Effects of Price Discrimination and Antitrust Cases Dealing with Price Discrimination. Hillsdale College. Hillsdale, MI. November 20, 2007.

<sup>7</sup> See abuse of dominance guidelines.

<sup>8</sup> Refer to regulation 4 (Threshold for determining dominant position) of the Competition Regulations, 2011.

## 4.0 EFFECT AND CLASSIFICATION OF PRICE DISCRIMINATION

### 4.1 Effects

Price Discrimination constitutes a threat to the economy for the following reasons:<sup>9</sup>

- i. Price Discrimination by dominant enterprises may reduce consumer surplus<sup>10</sup> and adversely affect consumer welfare, and this is called ‘exploitative’ price discrimination. The exploitation of a non-dominant enterprise comes into effect when the dominant enterprise uses its market power to foreclose<sup>11</sup> the market of smaller or weaker firms.
- ii. Price Discrimination can lead to exclusionary effects. Such effects can either affect the dominant enterprise’s rivals or the dominant enterprise’s downstream customers as in the case of Competition Commission of South Africa and South African Airways (Pty) Ltd (SAA) Case 18/CR/Mar01.<sup>12</sup>

### 4.2 Classification

Price Discrimination has been characterised in various forms.<sup>13</sup> The following have been described as classes of Price Discrimination:<sup>14</sup>

- i. Direct Price Discrimination is where the price depends on customer characteristics; and
- ii. Indirect Price Discrimination is where a menu of options at different prices is offered and customers self-select.

4.2.1 For Price Discrimination to be feasible, an enterprise not only has to segment the market in some way, but must also be able to enforce the segmentation, so that trading between the different categories of customers who are charged different prices is not possible.<sup>15</sup>

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<sup>9</sup> Office of Fair Trading (July 2001) “*The role of market definition in monopoly and dominance enquiries*”, Economic Discussion Paper 2, accessed at <http://www.oft.gov.uk>.

<sup>10</sup> Consumer surplus is the difference between what a consumer is willing to pay and what he or she actually pays. If consumer valuation of the good is higher than the price they actually pay for it they receive the net benefit or surplus from consuming that good.

<sup>11</sup> Foreclosure means that the competitive and productive capacity of the affected or weaker enterprise would be unduly weakened.

<sup>12</sup> In July 2005, the Competition Tribunal found that South African Airways (SAA), the country’s largest domestic airline, had engaged in incentive schemes which induced travel agents not to deal with competing airlines. One aspect of the incentive scheme was to offer travel agents target rebates or commissions in various formats. The Competition Tribunal noted that as the scheme was structured in a way that clearly provided a financial incentive to agents to move customers from rival airlines to SAA, and the agents had the ability to do this, the agreement had the effect of inducement as prohibited by the South African Competition Act. The agreements were also sufficiently long in place to have anti-competitive effect and were not transparent to customers, which prevented them from policing opportunist behaviour by agents. It was concluded that the target rebates/commissions substantially foreclosed the market to rivals of SAA and, in this manner, substantially lessened competition. The Competition Tribunal did not accept any of the efficiency enhancing benefits raised by SAA and fined SAA R45 million.

<sup>13</sup> OECD Glossary of Industrial Organisation Economics and Competition Law, <http://www.oecd.org/regreform/sectors/2376087.pdf>

<sup>14</sup> *The Competitive Effects of Price Discrimination*. Pongracic, Ivan. Lecture on the Competitive Effects of Price Discrimination and Antitrust Cases Dealing With Price Discrimination. Hillsdale College. Hillsdale, MI. November 20, 2007, <http://www.internationalcompetitionnetwork.org/uploads>.

<sup>15</sup> OECD Glossary of Industrial Organisation Economics and Competition Law <http://www.oecd.org/regreform/sectors/2376087.pdf>.

## 5.0 THE ASSESSMENT PROCESS

### 5.1 Elements of the Offence

The following must have taken place for an offence to have been committed:

- i. the alleged price discriminator must be shown to be an enterprise as defined under section 2 of the Act;
- ii. the discriminating enterprise must have market power;
- iii. the price differential must relate to equivalent transactions (i.e., business deals of equivalent magnitude, or orders placed by different customers that are of the same size);
- iv. the different prices must be charged to competing buyers for the same product;
- v. the discriminating enterprise must be able to segment customers according to their willingness to pay for each unit; and
- vi. the conduct must be shown to be designed to, or to have the effect or tendency of bringing about one of two effects of ‘substantially lessening competition or eliminating a competitor’.<sup>16</sup>

### 5.2 Price Discrimination by Application of Dissimilar Conditions

5.2.1 Price discrimination may be prohibited under section 27(1) of the Act, as it states that:

*“A horizontal agreement or vertical agreement other than one referred to under section 25 or section 26 (1) respectively, may be prohibited by the Authority if, following an investigation by the Authority, such agreement is found to have the object or effect of preventing or substantially lessening competition in a market for any goods or services in Botswana.”*

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<sup>16</sup> As in the *United Brands v Commission of the European Communities* Court of Justice of the European Communities, Case 27/76 [1978] ECR 207, judgment of 14 February 1978. The case relates to alleged abuses a dominant position by United Brands Company, the importer of the Chiquita brand of Latin American bananas. United Brands supplied these bananas unripe and in bulk to distributor/ripeners operating in various EC countries. The distributors would buy them while still green, ripen them using their own facilities and distribute them to retailers across their national markets. The other abuse identified by the Commission was the differential pricing charged by United Brands to distributors in different member states. Bananas were generally supplied by United Brands to distributors in Rotterdam so the transactions were directly comparable. United Brands argued that the differences were justified because the prices applied to distributors were directly linked to the final market price for bananas in each country. The Court found that this argument provided no justification for discriminatory prices, which were imposed by United Brands, and affected cross-border trade, thus amounting to abuse irrespective of any commercial logic underpinning them. The Court of Justice (there was no Court of First Instance at the time) upheld the Commission decision on dominant position, on the restrictive conditions abuse, the refusal to supply abuse and the discriminatory pricing abuse.

### 5.3 Price Discrimination as an Abuse

5.3.1 Price Discrimination and discrimination generally, by a dominant enterprise, may be prohibited under section 30 of the Act.

5.3.2 Price discrimination raises two potential issues.<sup>17</sup>

- i. It may be **exclusionary**. For example, in the automobile insurance industry, males have traditionally been charged higher rates than women drivers, and much higher rates for ages under 30. This might be considered an exclusionary type of price discrimination. In the dry cleaning sector of some countries, the dry cleaners typically charge higher prices for the laundering of women's clothes than for men's. Dry cleaners justify the price differences because women's clothes require more time to press than men's clothes due to more pleating. This only qualifies as an example of price discrimination if part of the reason for the higher pricing is truly due to the dry cleaner's belief that women will be willing to pay more than men.
- ii. It may be **exploitative**. Price discrimination may allow an enterprise to exploit market power by charging certain customers high prices. For example, following the financial recession in USA, business travellers made it clear to airlines that they were not going to be buying air travel at rates high enough to subsidise lower fares for non-business economy class travellers. The business travellers felt that the price discrimination was exploitative on their part.

5.3.3 When considering whether Price Discrimination is an abuse, it is often relevant to consider whether the pricing structure in question allows the efficient recovery of fixed costs and expands demand substantially or opens up new market segments. For example, enterprises often have fixed costs of production (costs which do not vary directly with output, at least in the short run).<sup>18</sup> This means that they will usually need to set at least some prices above their average variable costs to generate sufficient revenues to break even (i.e., earn normal profit). In this case, Price Discrimination can be beneficial if it leads to a sufficiently large increase in output in relation to the output level that would have applied if there was no price discrimination. In some cases Price Discrimination may allow a new market segment to emerge. This might occur in industries characterised by relatively high fixed costs, where customers can be split up into groups according to their willingness to pay, and where groups with low willingness to pay would not buy in the absence of Price Discrimination.

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<sup>17</sup> OECD Glossary of Industrial Organisation Economics and Competition Law, <http://www.oecd.org/regreform/sectors/2376087.pdf>.

<sup>18</sup> The Competitive Effects of Price Discrimination. Pongracic, Ivan. Lecture on the Competitive Effects of Price Discrimination and Antitrust Cases Dealing With Price Discrimination. Hillsdale College. Hillsdale, MI. November 20, 2007, <http://www.internationalcompetitionnetwork.org/uploads>.



5.3.4 Just because Price Discrimination can be beneficial does not mean that the chosen form of Price Discrimination adopted by a dominant enterprise in that industry is presumed legal. The Competition and Consumer Authority will assess Price Discrimination on a case by case basis, and impose appropriate remedies.

## 5.4 Defences

### 5.4.1 Defences Under the Competition & Consumer Act

Public Interest grounds may be used as a defence against abuse (including Price Discrimination). Section 30(2) states that:

*In determining whether an abuse of dominant position has occurred, the Authority may have regard to whether the agreement or conduct in question-*

- a) *maintains or promotes exports from Botswana or employment in Botswana;*
- b) *advances the strategic or national interest of Botswana in relation to a particular economic activity;*
- c) *provides social benefits which outweigh the effects on competition;*
- d) *occurs within the context of a citizen empowerment initiative of Government, or otherwise enhances the competitiveness of small and medium sized enterprises; or*
- e) *in any other way that enhances the effectiveness of the Government's programmes for the development of the economy of Botswana, including the programmes of industrial development and privatisation.*

### 5.4.2 Justified Price Discrimination<sup>19</sup>

A supplier that levies unequal prices (Price Discrimination) between competing customers that buy the same product is considered not to engage in prohibited Price Discrimination if one of the following defences is available:

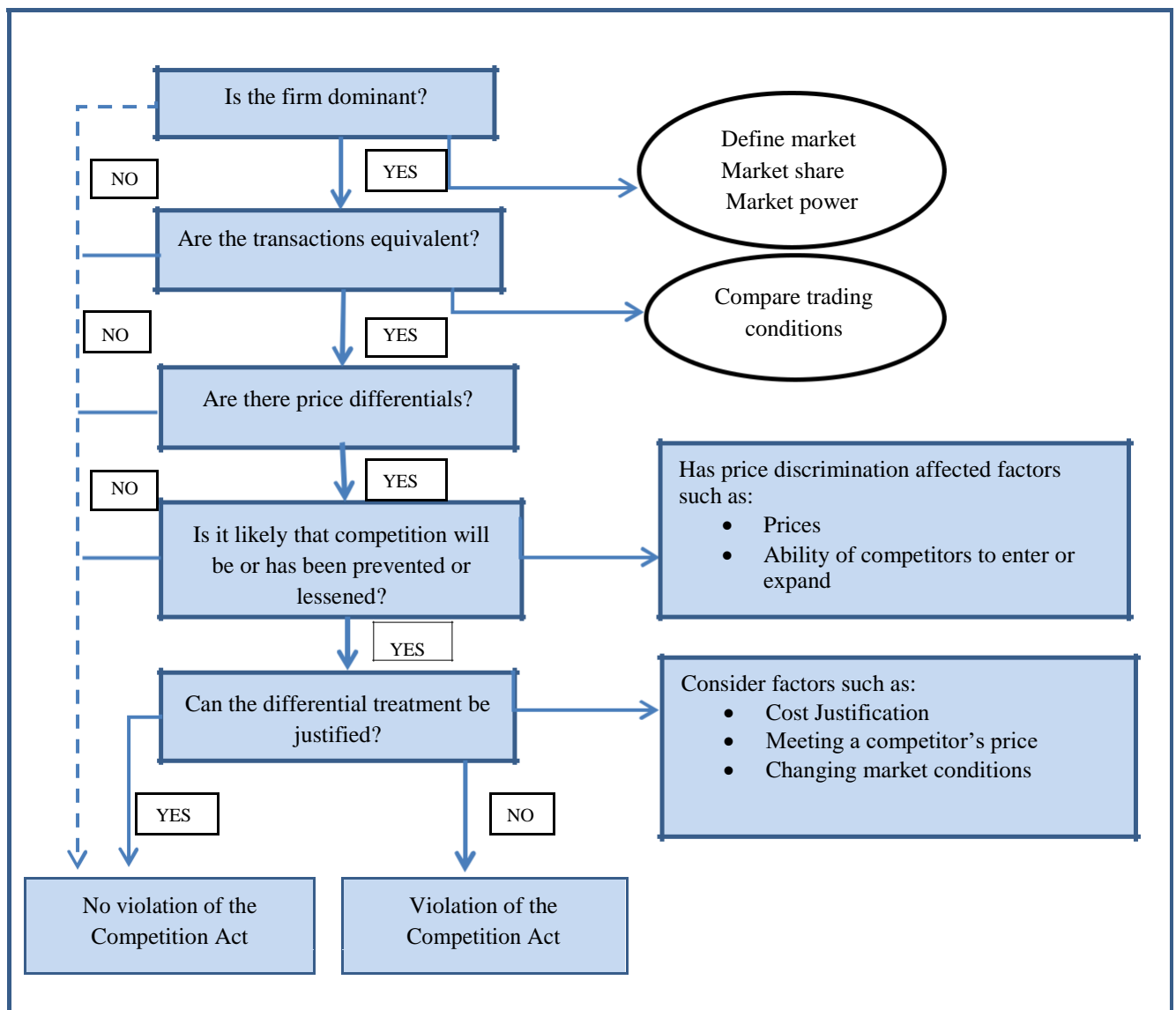
- (a) If the price difference was made in good faith out of the following reasons:
  - i. To make reasonable allowance for differences in costs or likely costs of manufacture, distribution, sale, promotion, or delivery resulting from the differing:
    - places to which;
    - methods by which; or
    - quantities in which goods or services are supplied to different purchasers; and
  - ii. To meet the price or benefit offered by a competitor.

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<sup>19</sup>Reflections on the Robinson-Patman Act: *A Review of International Perspectives on Price Discrimination*. The Concept of Price Discrimination under EC and UK Law. By P. Whelan and P. Marsden (2006), [http://www.biicl.org/files/60\\_reflections\\_on\\_the\\_robinson\\_patman\\_act\\_a\\_review\\_of\\_international\\_perspectives\\_on\\_price\\_discrimination.pdf](http://www.biicl.org/files/60_reflections_on_the_robinson_patman_act_a_review_of_international_perspectives_on_price_discrimination.pdf).

- (b) If the price differential resulted from changing market conditions, including:
- i. any action in response to the actual or imminent deterioration of perishable goods;
  - ii. any action in response to the obsolescence of goods;
  - iii. a sale pursuant to a liquidation or sequestration procedure; or
  - iv. a sale in good faith in discontinuance of business in the goods or services concerned.

**Figure 1. The Process/Procedure of Proving Price Discrimination.**



Source: A Practical Guide to the South African Competition Act

## **5.5 Non-Price Discrimination as an Abuse<sup>20</sup>**

- 5.5.1 Discrimination is regarded as applying dissimilar conditions to equivalent transactions or similar conditions to different transactions; it is not concerned solely with price.
- 5.5.2 Discrimination on terms other than price can also have anti-competitive effects. For example, an enterprise which controlled the supply of a key input might supply a downstream enterprise with a poorer quality of service than it provides to its own business competing in the same downstream market (for example, delivery taking longer).
- 5.5.3 If the difference in service quality was not reflected in the pricing by the upstream enterprise, the enterprise could be regarded as acting in a discriminatory way.
- 5.5.4 The analysis of non-price discrimination, for example, quality of service discrimination, would be similar to that of Price Discrimination. This is because raising the price of a product of a given quality is effectively the same as lowering the quality of a product sold at a given price.
- 5.5.5 As with Price Discrimination, the Non-Price Discrimination will not necessarily be subject to abuse. It would be subject to abuse only where it was exploitative or reduced (or could be expected to reduce) existing or potential competition.

## **5.6 Justified Non-Price Discrimination**

A dominant enterprise or group of enterprises acting together would be justified to continue with non-price discrimination on the following grounds:

- i. quantity/volume discounts as are commercially reasonable in the relevant market;
- ii. offer reasonable cash discounts (i.e., to clients who pay cash by a stated date); and
- iii. pay different amounts based on standard of products supplied/offered.

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<sup>20</sup> Office of Fair Trading (July 2001) *"The role of market definition in monopoly and dominance enquiries"*, Economic Discussion Paper 2, accessed at <http://www.offt.gov.uk>.

## **6.0 CONCLUSION**

- 6.1 A dominant enterprise applying dissimilar conditions to equivalent transactions which it enters into with different trading parties may be charged with abuse of its market power and subjected to appropriate remedies as determined by the Authority or Commission.
- 6.2 It is not enough for an enterprise to cite a defence. The defence must be self-evident in relation to the abusive conduct and must be of such value to society that it outweighs the detriment to competition (see the Authority's relevant guidelines on Public Interest).
- 6.3 Staff of the Authority or any party using or referring to these Guidelines needs to ensure that he/she compares the process or conclusions herein with the latest decisions or judgments of the Commission, competition tribunal/s, or superior courts in Botswana or other relevant comparable jurisdictions.