BIZCOMMUNITY

Competition Appeal Court clarifies burning issues raised in Loungefoam

By Petra Krusche

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The Competition Appeal Court (CAC) recently dismissed the Competition Commission's (Commission) application for leave to appeal to the Supreme Court of Appeal (SCA) in the long, ongoing Loungefoam case.

The reasons for the dismissal make interesting reading on several hot topics under the Competition Act No. 89 of 1998 (Act) that have worried both the Commission and business. One of them is whether a holding company can be liable for an administrative penalty if its subsidiary is guilty of collusion, upping the stakes for prohibited collaboration between competitors.

Relevant to this topic is that Loungefoam and Vitafoam, firms controlled by Steinhoff, stand accused of two instances of collusion: the first alleged between the two of them and the second count allegedly involving their collaboration with competitors outside the Steinhoff Group.

Conduct not unlawful

The defence raised by Loungefoam and Vitafoam against the first alleged collusive conduct between them is that their conduct is actually not unlawful by virtue of the fact that both firms are controlled by Steinhoff, accordingly they are constituent firms of a single economic entity and, in law, excused from any consequences for collaborative conduct between them by virtue of section 4(5) of the Act. This section exempts conduct that would otherwise be collusive between firms that are in fact one business. For example, a company that has simply divisionalised its various business interests cannot be prosecuted successfully for alignment of prices and such like between its business units, whereas, for example, competing subsidiaries (not wholly owned as they too are exempt from collusion between them) and associated firms run the risk that co-ordinated activities between them could be prohibited collusion under the Act, unless they have the attributes of a single economic entity.

If the Steinhoff-controlled companies succeed with their single firm defence against the first count of collusion, the Commission contends that if it successfully proves the second count of collusion between the Steinhoff-controlled firms and their third-party competitors, then it must follow that the Steinhoff group of companies, a proven single economic entity, must be liable for the administrative penalty. This contention also means that the group turnover be used as a relevant measure for the amount of the fine under the Act. The Act, for example, provides for a cap on any penalty - it may not exceed 10% of annual turnover of a firm. The potential downside for business of a cap determined with reference to group instead of a subsidiary's turnover is obvious, whilst the additional deterrent and punitive effect of a much higher cap must be very attractive for the enforcer.

The EU and New Zealand

The issue of imposing a fine on the holding company for competition transgressions of its subsidiary has not previously been considered by the South African competition authorities, and it may be useful to note that certain foreign jurisdictions will impose a penalty on a parent company for the contraventions of its controlled subsidiary. For example, the European Commission adopts a hardened approach in holding parent companies liable for the EU competition law infringements of their subsidiaries. The New Zealand court of appeal has also recently paved the way for the Commerce Commission to hold overseas parent companies liable for the competition contraventions of their New Zealand subsidiaries. This broader approach is criticised in that it is perceived to overstep the main object of a penalty, namely to deter repeated collusion by the culprit, and tends towards the punitive.

In Loungefoam, the CAC made short shrift of the Commission's ideology. It said that the single economic construct is only a defence available to constituent firms for exempting them from liability for collusion between themselves, but that "Once the conduct involves third parties the section becomes irrelevant and all the participant firms are liable to be held to have contravened s 4(1) and be liable for the penalties that such conduct attracts" and is not "any basis for making a holding company liable for administrative penalties imposed on its subsidiaries".

Put differently, a successfully proven single economic entity defence exempts the firms from collusion under section 4(5) of the Act, but that factual close relationship will not undermine the separate legal identities of the controller and its subsidiaries and associates for fining purposes under the Act.

This explanation by the CAC should provide some comfort to groups of companies whose subsidiaries are implicated in collusive activities and, for example, probably also restrict claims by persons who suffered damages as a result of collusive conduct, as against the colluding firms only.

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