CPI's Africa Column Presents:

The South African Competition Commission's R1.5 billion Arcelor-Mittal Settlement: A Lesson in Designing Appropriate Remedies

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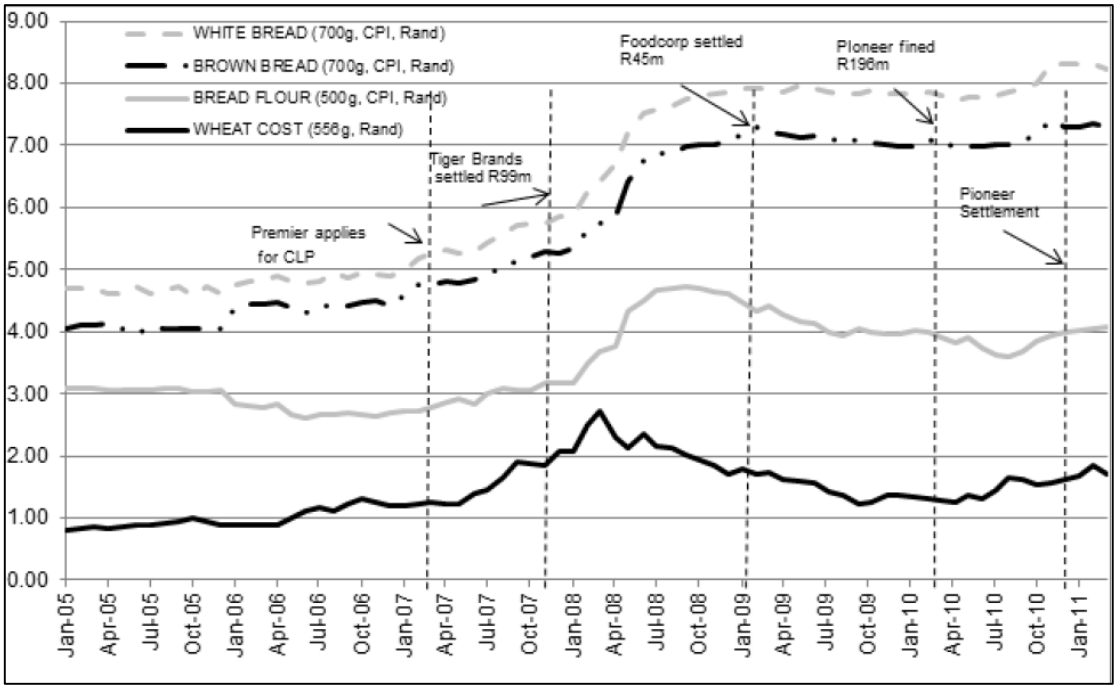
Introduction

One of the shortcomings of competition law enforcement is its perceived inability to redress market outcomes resulting from anti-competitive conduct. This means that the future conduct of guilty firms may not be based on true "competition on the merits" but on the ill-gotten gains of anti-competitive conduct, which often becomes the benchmark for future market outcomes. Traditionally, when the South African Competition Commission ("Commission") fines a firm found guilty of contravening the Competition Act 89 of 1998 ("Competition Act"), this penalty, which is primarily aimed at deterrence of future cartel conduct, is paid into the country's fiscus. The Commission's role in this process generally ends there and the firms in question potentially continue enjoying the fruits of their illegal conduct.

This failure of an administrative penalty to address market outcomes was illustrated in the bread cartel case in South Africa, which was settled between 2007 and 2011. In that case, it was found that despite the Commission's numerous interventions, the price of bread did not decrease post the uncovering of the cartel and the levying of fines on cartel participants (see the graph below).



Source: Mncube and Ngwenya (2010)

Bread producers continued to enjoy inflated cartelised margins even after paying the fines imposed by the Commission, raising the question of whether the Commission's interventions had any real impact on market outcomes.

We believe that this question has more recently driven the Commission's proactive stance on crafting remedies that directly impact market outcomes, instead of simply fining guilty market participants. The recent settlement agreement that the Commission signed with Arcelor-Mittal ("Mittal"), which is subject to approval by the Competition Tribunal, is indicative of such an attempt.

The significance of the Mittal settlement agreement

The Mittal settlement agreement encompasses various elements intended to deal with a number of cases that have been pending against Arcelor-Mittal for some time.

The settlement agreement has the following features:

- R1.5 billion (approximately $105 million) payable in annual installments over the next 5 years for admitting to collusion (that is, fixing prices and discounts, allocating customers and sharing commercially sensitive information) in relation to long steel products. The long steel cartel members include CISCO, Scaw and Cape Gate. In relation to scrap metal, Mittal admitted to having fixed the purchase price of scrap metal with Columbus Steel, Cape Gate and Scaw.
- Although not admitting to having contravened the excessive pricing provision of the Competition Act, Mittal agreed to remedies that address competition concerns arising from its pricing conduct in relation to flat steel. These include capping its earnings before interest and tax (EBIT) on flat steel to 10% (with a tolerance of up to 15%, depending on market circumstances).
- Mittal also agreed to a capital expenditure of R4.64 billion (approximately $325 million) for the next five years.

While the focus of this settlement agreement has been on the staggering R1.5 billion fine, which is the largest fine imposed on a single company under the current South African competition law regime, the incorporation of a pricing remedy and a capex requirement, which are essentially behavioural remedies, to redress and achieve certain market outcomes, represents a different remedial approach on the part of the Commission.

The South African steel industry is strategically important as there are many downstream industries for which flat steel products are key inputs. Factors such as uncompetitive upstream steel pricing, and a lack of capital investment and maintenance have had a significant impact on downstream, labour-intensive, domestic manufacturers and users of those steel products. By designing remedies that are specifically targeted at influencing market outcomes, such as those in the Mittal settlement agreement, the Commission has shown that it is important not only to focus on punitive administrative fines, but also on restoring and enhancing competition in the relevant market, as well as incorporating the public interest objectives that underpin the South African Competition Act. These interventions become all the more applicable in South Africa where private damages and private enforcement of competition law is still in its infancy and weak.

It should be pointed out that this is not the first time within the context of a restrictive practices or abuse of dominance case that the Commission has pursued a settlement agreement of this nature. Following the finding of the bread cartel referred to above involving Pioneer Foods, Premier Foods, Tiger Brands and Foodcorp, the Commission reached a unique settlement with Pioneer Foods. The terms of the settlement agreement included that Pioneer Foods would: (1) create an agro-processing Competitiveness Fund of R250 million (approximately $17 million) drawn from the penalty that was paid by Pioneer Foods; (2) adjust the prices of certain of Pioneer Foods products for an agreed period of time so as to reduce its gross profit by an amount of R160 million (approximately $11 million) (a brief analysis of pricing for quarter 1 in 2011 would suggest that this intervention resulted in lower prices for consumers for a short period of time); and (3) maintain its capital expenditure and increase it by an amount of R150 million (approximately $10 million).

Conclusion

In the context of the debate on whether fines do actually deter anti-competitive conduct, crafting settlement agreements that go beyond an administrative penalty and are designed to address the harmful impact of anti-competitive conduct has the potential to correct market outcomes on a forward-looking basis. This appears to be the approach of the Commission in the Mittal case. Going forward, it will be interesting to track the impact that this remedy will have in the medium to long-term on downstream industries for which flat steel is an important input.