EXPERT REPORT EF

SECTION 8(A) THRESHOLD FOR "EXCESSIVENESS" AS LOWER FOR NECESSITIES THAN LUXURIES

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I understand that major pharmaceutical companies price HIV/AIDS drugs sold in South Africa far above their full costs, including the companies' costs of research and development. I have been asked whether this conduct is or should be an abuse of dominance under South African competition law, and whether such an application would have unwanted implications far beyond this case; i.e., Is the standard for "excessiveness" of price the same for necessities and luxuries?

Excessive pricing is, by definition, a violation of the South African competition law; and, in my view, "excessiveness" of the price of luxuries is different in kind from "excessiveness" of the price of necessities.

The South Africa Competition Law provides:

> 8. It is prohibited for a dominant firm to — (a) charge an excessive price to the detriment of consumers . . . ."

Moreover, the act provides that the following two categories are relevant to the act's interpretation: international standards, and measures to address the nation's legacy of discrimination. The Competition Law, especially in the context of the South African Constitution, counsels that the level of "excessiveness" necessary to constitute abusive pricing in violation of the Competition Law is higher for luxuries of life than for antiretroviral drugs, desperately needed by thousands of poor South Africans.

The competition laws of most nations include a prohibition against excessive pricing. Most of these nations enforce this provision with restraint. I explain why the law against excessive pricing is a foundational part of competition policy; why it is used with restraint; and why this case — a desperate need for health care necessities — is an especially fitting case for application of Article 8a of the Competition Law.

Competition laws are intended to help the market work. The prohibition against abuse of

dominance is one of three critical parts of virtually all competition laws (the others being cartels and mergers).

It is accepted wisdom that the greatest economic evil of monopoly (or dominance) is the condition of market power because market power — especially monopoly power — leads to elevated prices and deflated output. The monopolist gets higher profits even while selling fewer goods; thus by definition the monopolist fails to satisfy demand at cost including a reasonable return on investment. Excessive pricing is theoretically the paradigmatic offense.

But enforcement of an excessive pricing law entails difficulties. First, one might fear that depriving a firm of the fruits of its success (monopoly prices) may undercut its incentives to become successful in the first place. Second, determining when a price is sufficiently excessive and at what level the price is not exploitative are difficult tasks. Thus, there are problems of incentives if "excessiveness" is found too freely, and there are problems of administrability. For these reasons, the United States does not have an excessive pricing prohibition. But in this regard the United States is not the model for the world.

The European Union provides the leading model for an excessive pricing prohibition. Under European Union law, a firm may abuse a dominant position by charging a price "which is excessive in relation to the economic value of the service provided . . . ." *General Motors Continental N.V. v. Commission*, 1975 ECR 1367. In *United Brands Company v. Commission*, 1978 ECR 207, the European Court of Justice laid down the framework for proof: One must "determine[] whether the difference between the costs actually incurred and the price actually charged is excessive, and if the answer to this question is in the affirmative, whether a price has been imposed which is either unfair in itself or when compared to competing products." para. 252. In *Sirena v. Eda*, 1971 ECR 69, the Court of Justice said that a high price of an intellectual property license may, "if unjustified by any objective criteria and if it is particularly high, be a determining factor" in finding an abuse of dominance.

Because excessive pricing is inefficient, the prohibitory rule is justified even in nations that see efficiency as the core of the competition law. But excessive pricing is also unjust; excessive pricing of life-or-death necessities to the poor is particularly unjust; and under South African law justice and fairness share the platform with efficiency as legal bases. Applications of the South African Competition Law would appropriately take account of the distributional concerns found both in the Competition Law itself and in the Constitution of South Africa.

The relevant provision of the Constitution of South Africa is the (qualified) right to health. The Constitution provides: "Everyone has the right to have access to (a) health care services . . . . The state must take reasonable legislative and other measures, within its available resources, to achieve the progressive realisation of each of these rights." (Article 27). As the Constitutional Court observed in the nepiravirene case, *Minister of Health v. Treatment Acton Campaign*, Case CCT 8/02 (2002), quoting the strategic plan:

> "During the last two decades, the HIV pandemic has entered our consciousness as

> an incomprehensible calamity. HIV/AIDS has claimed millions of lives, inflicting pain and grief, causing fear and uncertainty, and threatening the economy." (summary of evidence, para. 5)

In *Minister of Health v. TAC,* the Constitutional Court addressed the claim that a legal rule recognizing the right to health is not administrable. The Court rejected the argument, stating:

> Where a breach of any right has taken place, including a socio-economic right, a court is under a duty to ensure that effective relief is granted. The nature of the right infringed and the nature of the infringement will provide guidance as to the appropriate relief in a particular case. (*Id*., text at footnote 55).

The Court further held that the government must "provid[e] reasonable measures within available resources . . . " to fulfill the promise of right to health. (*Id*., text before footnote 65)

Curing excessive pricing of antiretroviral drugs presents a much easier case than safeguarding the Constitutional socio-economic rights. The Competition Commission need only stop the private firms from illegal exploitation of the sick and needy.

A possible concern by the Commission that reprehending excessive pricing of antiretroviral drugs would set it on a slippery slope of unbounded price control is easily met. This case is confined to the most critical of the life-or-death necessities, where a remedy will do immense good for millions of people. Application of the Competition Law to such critical necessities does not imply that the Commission will become the price regulator for South Africa.

Particularly, there is no reason to apply Section 8a to luxuries, such as Rolls Royce vehicles. This is so for two separate and very different reasons. First, there is no public interest, not even a consumer interest, in using competition law to constrain the price of luxuries. Buyers of Rolls Royce cars do not want the price of their cars to plummet to an affordable price, bringing Rolls Royces within the reach of the common citizen. The pleasure of Rolls Royce buyers – including their feeling of status – derives in large part from the fact that their cars are unaffordable to the masses. By definition, the price to them is not excessive.

Second, the distinction between necessities and luxuries is eminently permissible if not compelled by South African law and its unique responsiveness to issues of distributional equity and fairness. The Commission could appropriately recognize a special mandate to protect poor people from excessive pricing of necessities of life. Such a mandate is not "robbing the rich" when the latter are garnering so much more than a fair return at the expense of the sick; it is merely righting a balance; applying a principle of proportionality. When, as here, the interest to be served by enforcement of the socio-economic right is weighty, the Commission has the special obligation to find a way of practical enforcement.