BEFORE THE
COMPETITION COMMISSION OF PAKISTAN
IN THE MATTER OF

SHOW CAUSE NOTICES ISSUED TO

UREA MANUFACTURERS
(F. NO: 01/UREA/C&TA/CCP/2010)

Dates of hearing:	July 30, 2012, August 13, 2012 November 6, 2012, December 11 & 12, 2012
Present:	Ms. Rahat Kaunain Hassan **Chairperson**
	Mr. Abdul Ghaffar **Member**
On behalf of:	
M/s. Fauji Fertilizer Company Ltd	Syed Shahid Hussain Mr. Mohammad Munir Malik, GM Marketing Mr. M. Inam Ur Rehman, GM Eng Mr. Mohammad Salim Khan, Legal Advisor Mr. Hasnain Ibrahim Kazmi, Advocate Supreme Court, Kazmiz Hafiz Naeem, Advocate
M/s. Fauji Fertilizer Bin Qasim Ltd	Barrister Shahid Raza, Orr Dignam & Co. Syed Hassan Ali Raza, Advocate Mr. Shakeel Ahmed Mr. Iqbal Hashmi, Advocate Syed Aamir Ahsan Brig Shaukat Yaqub Malik Mr. M. Javed Akhtar, Manager (Planning & Budgeting)
M/s. Engro Chemicals Ltd	Mr. Andaleeb Alvi

M/s. Pak Arab Fertilizers Ltd	Mr. Salman K. Chima, Chima & Ibrahim Mr. Ibrahim Chima, Chima & Ibrahim Mr. Shazil Ibrahim, Advocate
M/s. Fatima Fertilizer Ltd	Mr. Salman K. Chima, Chima & Ibrahim Mr. Ibrahim Chima, Chima & Ibrahim Mr. Shazil Ibrahim, Advocate
M/s. Agritech Ltd	Ms. Zainah Qureshi, Raja Muhammad Akram & Co. Ms. Amna Hussain Mr. Taneem Haider, GM Finance Barrister Haroon Dogar
M/s. DH Fertilizers Ltd	Mr. Uzair Karamat Bhindari, Bhindari Naqvi & Riaz, Mr. Adil Tirmizi Mr. S.M. Asghar
M/s. Farmer Associates (Guarantee) Ltd	Mr. Waqqas Ahmad Mir, Advocate

O R D E R

1. This order disposes of proceedings initiated under Section 30 of the Competition Act, 2010 (the "Act") vide Show Cause Notice (the "SCN") nos. 71 to 77 issued to the Urea Manufacturing Companies operating in Pakistan namely:

    a. M/s. Engro Fertilizers Ltd
    b. M/s. Fauji Fertilizer Company Ltd
    c. M/s. DH Fertilizers Ltd
    d. M/s. Agritech Ltd
    e. M/s. Fatima Fertilizer Company
    f. M/s. Pak Arab Fertilizer Ltd
    g. M/s. Fauji Fertilizer Bin Qasim Ltd

2. The primary issue in this case is whether Urea Manufacturers enjoy a position of individual/collective dominance and whether they abused this dominant position by charging unreasonable/excessive prices in contravention of Section 3(3) (a) of the Act in the period December, 2010 to December, 2011.

UNDERTAKINGS:

3. Urea Manufacturing Companies operating in Pakistan namely M/s. Engro Fertilizers Limited ("EFL"), M/s. Fauji Fertilizer Company Ltd ("FFC"), M/s. Fauji Fertilizer Bin Qasim Ltd ("FFBL"), M/s. DH Fertilizers Ltd ("DHFL"), M/s Agritech Ltd ("AGL"), M/s. Fatima Fertilizer Company ("FFL") and M/s. Pak Arab Fertilizer Ltd ("PAFL") are engaged in the manufacturing and sale of fertilizers and are therefore undertakings as defined in clause (q) of sub-section (1) of Section 2 of the Act.

BACKGROUND:

4. In January 2011, The Competition Commission of Pakistan (the "Commission") took notice of the increase in prices of 50 kg Urea bags by the Urea manufacturing units operating in Pakistan through several newspaper reports. Keeping in perspective the agricultural orientation of the country and the implications this

could have not just on farmers but the economy as a whole, letters were written to all the major Urea manufacturers demanding an explanation for the increase and the dates they became effective.

5. The main ground given by the Urea Manufacturers for these increases was the Government of Pakistan ("GOP") induced gas curtailment (natural gas being a primary raw material in the production of Urea) faced by their plants, Two of the manufacturers also took the grounds that they were mere price followers and had no option but to follow price increase once it was carried out by the price leader. From the responses it turned out that the increase in prices were more or less simultaneous and the quantum of this increase did not vary from one manufacturer to the other. This raised a suspicion of collective action and exploitative behavior especially when seen in the light that the efficiency and the factors affecting each company were too different to warrant a similar reaction under the circumstances.

6. As the year 2011 progressed, the pattern of price increase continued as noted in various newspaper reports. It reached the extent where a Pakistan Today's report of July 28, 2011 quoted the then chief executive officer of Engro Corporation Mr. Asad Umar as admitting that a price increase of PKR 750-800 in the last eighteen months was equivalent to an accumulative increase over the last 32 years.

7. Such unprecedented increases in the price of Urea appeared to be anti-competitive under the Act and the Commission deemed it necessary to appoint an Enquiry Team by powers vested in it under section 37 of the Act. Ms. Shaista Bano Director (C&TA) and Mr. Qasim Khan Junior Executive Officer (C&TA) (hereinafter collectively referred to as 'Enquiry Committee') were appointed as Enquiry Officers in the matter. The Enquiry Committee was assigned the task to investigate the relevant reasons behind the price hike that took place in the period starting December 2010 and to submit before the Commission whether the price hike was a result of anti-competitive behavior adopted by the relevant undertakings individually/collectively in violation of the provisions of the Act.

8. At this point it was deemed necessary to have a deeper understanding of the matter. Consequently it was decided to carry out an analysis of costs involved in

the production of Urea to determine whether there was any room for exploitative behavior in the situation prevailing in the relevant period and if so whether there was an apparent violation of Section 3 of the Act. To fulfil this task the Commission hired an independent consultant who was given the task to carry out a comprehensive analysis of the prevailing prices of Urea and determine the rationale, reasonability or otherwise of the price increases that took place in the relevant period. The work of the consultant was to mainly focus on the cost components, profit margins and the subsidies available from GOP along with other factors.

9. To carry out the Analysis the consultant mainly relied on

    a. The information Collected by the Enquiry Committee from fertilizer producers including details of accounts;
    b. The information Collected by the Enquiry Committee from various sources such as National Fertilizer Development Centre, planning and Development Division, GOP;
    c. The information Gathered by the Enquiry Committee from various GOP functionaries;
    d. Published Annual and Interim Financial Reports of the Fertilizer Producers;
    e. Print Media and Analysts Reports;

10. The Enquiry Team incorporated the findings of the independent cost analysis to prepare a detailed Enquiry Report (the "ER") that was submitted before the Commission on the 25th day of June, 2012.

11. On the recommendation of the ER, SCNs were issued to each of the undertakings for prima facie violation of Section 3(3) a of the Act, the relevant portions of which are produced as under:

> ***AND WHEREAS,*** *the Competition Commission of Pakistan (the '**Commission**') took notice of unprecedented hike in the price of Urea fertilizer during the period starting from December 2010 to December 2011 and deemed it relevant for the purposes of the Act to enquire, while taking into*

account all the relevant factors whether the price hike was unreasonable or a result of anticompetitive practices in terms of Section 3 or Section 4 of the Act.

***AND WHEREAS**, a formal enquiry under the provisions of Section 37(1) of the Act was initiated, which was concluded vide Enquiry Report dated 25 June 2012. Copy of the Enquiry Report along with its annexures is appended herewith as '**Annex-A**' and these may be read as an integral part of this Show Cause Notice;*

***AND WHEREAS**, in terms of the Enquiry Report in general and paragraphs 14 to 18 in particular, the relevant market for the purposes of the Enquiry Report and this Show Cause Notice is the market of '**locally manufactured Urea fertilizer**' in Pakistan;*

***AND WHEREAS,** in terms of the Enquiry Report in general and paragraphs 19 to 31 in particular, market of locally manufactured Urea in Pakistan is a 'captive market' and all the undertakings in this relevant market have the ability to behave to an appreciable extent independent of its customers, consumers & competitors, irrespective of their market shares. Therefore, the Undertaking, prima facie, holds a dominant position in this relevant market;*

***AND WHEREAS,** in terms of the Enquiry Report in general and paragraphs 85 to 91, simultaneous and coherent increases in prices of Urea (same rate same time) in the absence of an objective justification by the industry players indicates common policy/economic linkages between Urea producers and therefore, the fertilizer market also appears to satisfy the conditions for existence of 'collective dominance';*

***AND WHEREAS**, in terms of the Enquiry Report in general and paragraphs 77 to 85 in particular, 86% increase in the price of Urea fertilizer i.e. from Rs.850 per bag to Rs. 1580 per bag during the period December 2010 to December 2011 seems to be unjustified and unreasonable.*

***AND WHEREAS,** in terms of the Enquiry Report in general and paragraphs 77 to 93 in particular, the Undertaking, while taking into account all the factors, such as gas curtailment, input costs, subsidies, profitability analysis and government policies, appear to have indulged in the practice of unreasonable price increase;*

***AND WHEREAS**, in terms of the Enquiry Report in general, the Undertaking being dominant in the relevant market appears to have abused its dominant position in the relevant market both individually and collectively vis-à-vis other fertilizer manufacturers by increasing the price of Urea fertilizer unreasonably and without any justification, which is a prima facie violation of clause (a) of sub-section (3) of Section 3 read with sub-section (2) & (1) of Section 3 of the Act;*

***AND WHEREAS**, the Commission is mandated under the Act to ensure free competition in all spheres of commercial and economic activity to enhance economic efficiency and to protect consumers from anti-competitive behavior.*

ER AND SCN FINDINGS:

12. As per the findings of the ER and the SCN issued to the relevant undertakings:

13. The market of locally manufactured Urea in Pakistan is a 'captive market' where all the undertakings in the relevant market have to an appreciable extent the ability to behave independent of their customers, consumers and competitors regardless of their market shares;

14. The lack of any objective justification by the industry players for coherent increase in prices indicate common policy/economic linkages among them and the fertilizer market appears to satisfy the conditions for existence of 'Collective Dominance';

15. After taking into account all the factors namely the affect of gas curtailment, input costs, subsidies, profitability analysis and GOP Policies the undertakings appear to have indulged in the practice of unreasonable price increase;

16. The undertakings being dominant in the relevant market appear to have abused their dominant position in the relevant market both individually and collectively by carrying out unreasonable price increases in Urea without any justification which stands to prima facie violate clause (a) of sub-section (3) of Section 3 read with sub-sections (2) & (1) of Section 3 of the Act;

Responses to the SCN & Submissions made in the Hearings:

17. In addition to the submission made in response to the SCN, there were a total of six hearings conducted by the Commission. These hearings took place on July 30, 2012, August 13, 2012, November 6, 2012, December 11, 2012, December 12, 2012 and December 21, 2012 respectively. Before proceeding further, we deem it appropriate to list down the grounds that were most commonly raised by the undertakings.

COMMON GROUNDS TAKEN BY THE PARTIES

Relevant Market:

18. The most common ground raised by the undertaking, was with respect to the definition of the relevant market. The undertakings submit that since imported Urea is sold in the market and is indistinguishable in terms of its characteristics, price and intended usage from the locally produced Urea, therefore it should be included in the definition of relevant market. Furthermore AGL and DHFL disagree with the definition of relevant market in the ER claiming that there are other types of fertilizers (particularly CAN) that can serve as substitutes for the consuming farmers and should have been included in defining the product market.

Individual Dominance:

19. With respect to Individual dominance the undertakings was contended that they face competitive pressure from GOP imports. To substantiate this claim some of the undertakings made a further claim that they were unable to pass on the effect of Gas Infrastructure Development Cess (GIDC) due to excessive imports carried out by the GOP in 2012.

Collective Dominance:

20. With respect to collective dominance the undertakings argued was that increasing price in tandem is a regular feature of an oligopoly and amounts to 'tacit collusion' in terms of law. Tacit collusion is a lawful conduct that does not amount to collective dominance or cartelization in the light of American anti-trust jurisprudence and in particular the Judgment made in the DG khan Cement Companies Ltd vs MCA case.

Excessive Pricing/Unreasonable Price Increase:

21. A common ground raised by the undertakings with respect to excessive pricing was that they sell their Urea to the dealers or distributors of Urea. These distributors presumably indulge in black marketing and take advantage of the shortage of Urea supply in the relevant market to charge high prices. If the

undertakings do not increase their prices after the dealers have done so all the price differential would be pocketed by them.

PARTY WISE RESPONSES:

22. A summary of the Party wise responses to the SCN and any additional submissions made during the hearings are provided as under.

FFC:

Individual Dominance:

23. FFC refuted the stance taken by the ER, that the market of locally manufactured Urea is a captive market and that FFC has a dominant position on the following grounds:

    a. FFC is a price taker as established in the ER itself

    b. FFC is not independent of competition owing to the following actions of GOP:
        i. Import of Urea necessitated by the product shortage caused by curtailment of gas supply by the GOP.
        ii. Delay of imports when required causing a demand supply imbalance
        iii. Import quantities surpass demand and sell at below market price to bring down prices

    c. Dip in market demand by consumers during second quarter of 2012 forced FFC to reduce its prices by PKR 145 per bag. FFC therefore cannot act independent of its consumers

    d. FFC cannot act independent of its gas supplier Mari Gas Company limited in which the GOP has 40% share.

    e. FFC is not independent of the GOP as the GOP does not allow it to carry out any exports of Urea

f. No Urea manufacturer and Urea importer including GOP can act independent of each other as market demand supply forces do not allow any undertaking to set rates other than the prevailing market price

g. Furthermore the ER says that FFC and FFBL hold a combined market share of 41% however the two entities cannot be clubbed together as FFBL is an independent legal independently responsible for its actions.

h. The Market share of FFC is 32.24% which is below the 40% established by the Act to render a dominant undertaking.

i. Mere statement of a captive market does not render all the players in the industry dominant rather the onus is on the Commission to show that each undertaking is dominant in its own right.

j. The criteria used in the EU to determine dominance of an undertaking are: market position of its competitors, threat of future expansion or entry and countervailing buyer power

k. US courts have held that a party has monopoly power if it has the power of controlling prices or unreasonably restricting competition over any part of trade among several states. Furthermore this power may also be inferred from having a predominant share in the market. Something in the vicinity of 50-60% was considered to be the minimum as a monopoly power criterion.

l. Thus whether U.S, EU or the Pakistani law an undertaking cannot presumed to have dominant position with a market share below 40%

24. Coming to the issue of Captive Market in the Commission's order of 23rd July 2010 a captive market was defined as the one where owing to legislation or lack of alternatives purchasers are forced to buy a product. This does not apply in the case of Urea fertilizer as there is diversity in the form of a number of fertilizer producers in Pakistan. In 2011 total Urea production capacity of the country exceeded local demand by virtue of which not only is the local industry sufficient

for attending to domestic demand but can also export provided the gas supply is not curtailed.

Collective Dominance:

25. With respect to Collective Dominance FFC made the following submission during the Hearings.

26. FFC disagrees with ER's approach in establishing Collective Dominance since there has been no application of an established three pronged test defined in the Airtours case.

27. FFC submits that if it is collectively dominant with respect to competitors, then there should be structural or economic links between FFC and them (so far all cases found to have collective dominance had horizontal agreements with the exception of Irish Sugar where a vertical agreement existed)

Excessive Pricing:

28. FFC submitted that the Increase in the prices of Urea during 2010-11 was a result of a peculiar situation brought about by the GOP by curtailing Gas supply and making delayed imports despite reminders by the undertakings in several meetings.

29. As per FFC, since Competition Act, 2010 ('the Act') favors a free market economy, the prices of commodities are best left to the market. The increase in the prices of Urea was a normal demand and supply phenomenon and prices only went up as a result of shortfall. This was not just true of Urea but prices of other goods including necessities.

30. FFC contended that the correct interpretation of subsection 3(3)(a) would bto see an unreasonable price increase in the context of an undertaking limiting its production and supply. This is so because the "unreasonable increases in price" has been used conjunctively with "limiting production, sales", therefore the "AND" cannot be read as disjunctive. Therefore, the Commission may take action

against such unreasonable price increase that is an outcome of limiting production and sales and which prevents, restricts, reduces or distorts competition in the relevant market. The duty of proving a reasonable nexus between the price hike and distortion of competition has not been fulfilled in the ER.

31. FFC submitted that in the context of the existence of the Price Control and Prevention of Profiteering and Hoarding Act, 1977 (the "Price Control Act, 1977") which deals with excessive pricing and whose list of Commodities to be regulated under the Act include chemical fertilizers, it is beyond the commission's mandate to control prices. Furthermore the Act lacks an explicit provision that authorizes the commission to probe into matters of excessive pricing.

32. Under clause 5.1 of the Fertilizer policy, 2001 a committee has been established to review the prices of fertilizer products. The said committee meets regularly and reviews Urea prices.

33. As per the Judgment in the **"D.G. Khan Cement Companies Limited v. Monopoly Control Authority ("MCA"), PLD 2007 Lahore 1",** case**,** MCA is the regulator and restorer of competition and not of prices. By fundamentally confusing two entirely separate and distinct functions, the authority has asserted a power that does not vest in it under law.

34. FFC submitted that the Commission has shown to follow the legal principals of Competition law applied in the U.S and U.K as shown in a plethora of its orders passed from time to time. Regimes in either of the countries do not see excessive pricing as a competition concern on its own, particularly as they don't deem themselves as price regulators and have policies driven by the rules of laissez faire.

35. In terms of FFC's submissions, the ER states that the purpose of subsidy forwarded by the GOP to the fertilizer industry is to make Urea available to the farmers at affordable rates; however the term affordable is not defined. Since FFC sells Urea at rates much below international prices the prices are affordable.

36. The following additional points were raised by FFC in respect of 'Excessive Pricing' during the Hearings.

    FFC shared views of an article that competition authorities should ideally refrain from cases of excessive pricing except for where pricing has an exclusionary effect. In UK the only case where excessive pricing was found to hold true was that of NAPP. Excessive pricing is not checked by Competition authorities in the U.SThere is no accepted yardstick to measure unreasonableness of price. Regardless of the costs it is the market value that determines the price.

37. The ex -factory price of Urea was PKR 1225 but sold for PKR 1800 in the end market. The GOP was a quiet spectator of this black marketing. Owing to untimely imports, Urea suffered a shortage of 30% in the market. With such a huge shortfall prices shot up and the rate was established in the market. FFC is not the price leader rather it is a follower and when EFL raises its price FFC has to follow suit. FFC cannot sell at a lower price to the dealer because if it does the dealer would indulge in black marketing and pocket the difference. The GOP also increased the price of its Urea from PKR 1300 to 1600 for the same reason.

38. FFC contended that it is incorrect to say that subsidies are not being passed on to the farmers. In fact they are being passed on 100% as the prices of International Urea are very high and the subsidy provided to the undertakings is based on international gas prices.

39. In the case of Attheraces Ltd (ATR) vs the British Horse Racing Board (BHB), ATR filed a case of excessive charging against BHB in the High Court of Justice Chancery division. While the decision was made in favor of ATR, when this matter entered the court of appeal the cost plus approach was found insufficient in establishing that the price despite being excessive was unfair and the behavior abusive as 'other benefits' accrued by ATR and not accounted for in the costs were ignored.

40. Another case in EU is that of Scand lines vs. Port of Helsenborg. The main questions addressed with regard to excessive pricing were whether the price was

unfair in of itself or when compared with competing products. Other than the actual costs other costs such as high sunk costs for the port, intangible value of the product, the fact that the land used by the port is very valuable and comparative advantages with respect to other ports were considered. No such analysis was carried out in the ER. The burden of such proving the same is on the Commission.

41. Case of NAPP pharmaceuticals ("NAPP") that the Office of Fair Trade ("OFT") in England took cognizance of is another example. NAPP manufactured morphine tablets were sold at a price 90% higher to the community segment when compared with the price charged to hospitals. The case of United Brands was taken as a reference and an analysis involving accounting comparators such as the comparison of prices over time, comparison of prices charged to the hospitals, consumers and exported medicines was employed to arrive at the conclusion that prices were indeed excessive.

42. External factors pertaining to FFC are shortage of Urea, opportunity cost since we have invested money in Urea plants. Efficiency of operations is another factor. The ER did not account for any of these external factors. Cost plus approach is a very narrow approach. Benefit to the farmer or the utility derived was another factor to be looked at.

43. As per FFC, the only case where a fine was imposed was that of **British Leyland** where they were penalized for charging a very high price for issuance of certificates making use of their monopoly position. The case of **General Motors** was annulled in the appeal

FFBL:

Individual Dominance:

44. FFBL contended that based on its sales in 2011, FFBL's market share is a mere 7% far below the threshold of 40% at which an undertaking is deemed dominant under Section 2 (1) (e) of the Act.

45. As per FFBL the Commission has first deemed FFBL as having a dominant position under section 2(1)(e) of the Act based on its alleged collective dominance and then deemed it to have abused this position in terms of section 3(2) of the Act read with 3(3)a of Act based on the alleged unreasonable increase in prices by the local Urea manufacturers in the period December 2010 – December 2011. It follows from the foregoing that the SCN relies on the application of two sets of deeming provisions but for which it has no basis.

46. Section 2(1)(e) involves deeming provisions and as per precedent set by superior courts for deeming provisions to be applicable all conditions laid down in the relevant provision must be fulfilled before it can be regarded to have taken effect. Thus it means that for an abuse of dominant position deemed to have taken place all conditions must be established in terms of Section 2(1)(e) of the Act, which is not attracted in case of FFBL due to its market share as well as not having the ability to behave independently of its competitors and consumers as explained in this reply.

47. Contrary to the enquiry team's claim FFBL is unable to act independently of its competitors or consumers.

48. FFBL has a mere market share of 7% that is not enough to establish dominance. In the case of French Republic and Societe commerciale des potasses et de l'azote (SCPA) and Enterprise miniere et chimique (EMC) v Commission of the European Communities, a withdrawal test was applied in the context of a merger that if a party with a 7% market share pulled out of the deal would it have any impact on the market. Collective dominance was not seen to hold true because such a withdrawal was not deemed to have an impact. In Pakistan dominance is established when a party is capable of behaving to an appreciable extent independent of its supplier, customers and competitors. The further one goes down 40% the harder it is to establish dominance.

Collective Dominance:

With respect to the issue of 'Collective Dominance' FFBL made the following submission during the course of hearings.

49. FFC and FFBL cannot be clubbed together as one entity. The main point is how their price increase is unreasonable and in that context the only question of a link between the two could be in the sense of Collective Dominance.

Excessive Pricing:

50. FFBL submitted that the Commission's issuance of SCN has been without jurisdiction in light of the Price Control Act, 1977 and the decision of the LHC in the DG Khan Cement Company Ltd vs MCA. Despite having additional powers with respect to MCA owing to the inclusion of Section 3(3)(a) in the, the principle established in the judgment that CCP is not a price regulator is unaffected. Furthermore, in the presence of Price Control Act, 1977, the SCN issued to FFBL would be contrary to the rule against double jeopardy.

51. Since the European Commission does not want to establish itself as a price regulator the very few investigations carried out by it with respect to article 82(2) were often motivated by considerations such as Excessive Pricing amounting to an obstacle to parallel imports or leaving a substantial share of the demand unsatisfied

52. As per FFBL, the failure of the ER to establish absence of a reasonable relation between prices of Urea and its economic value is fatal to the case against FFBL. The ER further erred by focusing on profitability rather than whether the difference between costs and price charged is excessive. In the United Brands and Scandlines v port of Helsenborg cases, the European Commission was of the view that a cost plus approach was insufficient and it was necessary to look at the economic value of the services provided to establish price abuse.

53. The price increases averaged 13% over the 5 years preceding 2011. In 2012 until July 5 price had increased by a mere 5.5%. Thus the price increase in 2011 was an aberration attributed to unprecedented short supply situation.

54. Urea is a commodity and in a commodity market prices are determined by supply and demand. High capital costs and gas allocation by GOP determine and limit the

number of local Urea manufacturers. Assurance of gas supply and timely imports would ensure stability in prices. Urea manufacturers have always run their plants at highest possible levels thus their behavior is not monopolistic.

55. The price increase in the said period is not unreasonable as explained. The total increase in the relevant period was PKR 730/bag. Of this increase PKR 191/bag was on account of GST and increase in feed and fuel gas prices (accounting for 20.6 and 1.8% respectively). PKR 299/bag (35.1%) was on account of gas curtailment and the remaining PKR 240/bag (28.1%) catered to inflation (CPI inflation was 13.81% in 2010-11) and increase in market price.

56. As per FFBL, the ER itself shows a 35% reduction in capacity utilization of FFBL and therefore it is wrong for it to assert that FFBL was not hard hit by gas curtailment. It is also incorrect to club FFBL with FFC as 'not connected to SNGPL network' as FFBL's plant is located in Bin Qasim Karachi and is connected to the sui network. FFBL's profits should also not be clubbed with those of FFC. FFBL's profit before tax in 2011 was 67% higher and profit after tax was 65% higher than the profits earned in 2010 rather than twice that as stated in the ER.

57. With regard to subsidies, the ER fails to mention that if FFBL had not produced Urea the total subsidy that the GOP would have had to pay on importing the same quantity of Urea would have been much higher. Against a GOP based subsidy of PKR 3.5 bn that FFBL availed in 2011, the GOP would have paid a subsidy of PKR 13.71 bn if the same quantity was imported. Net saving to the GOP and additional benefit to the farmer thus amounted to PKR. 10.21 bn. Even as per fertilizer policy 2001 the aim of subsidized gas is to ensure that local Urea prices remain below the import price.

58. FFBL believes that ER's use of gross margin and profit before tax is an incorrect indicator as profit ultimately realized is profit after tax. FFBL's gross profit margin as noted in the ER is 36% and not greater than 49% as erroneously noted later. FFBL's gross profit margin was 31% in 2010. FFBL's profit before tax margin was 29% in 2011 as against 22% in 2010 and its profit after tax margin was 19% in 2011 as against 15% in 2010. In these circumstances the ER's use of

expressions such as ‘massive gross margins’, ‘increase in profits manifold’ and ‘exorbitant profits’ and the statement that local industry enjoys profits that no other industry enjoys locally or abroad are grossly exaggerated and unfounded.

59. FFBL contended that the ER is a one sided critique. It ignores the fact that Urea prices increased to PKR 850 per bag in May 2011 and not December 2011. It also ignores that the GOP increased the price of imported Urea from PKR 1300 to PKR 1600 in February 2012 and that price of GOP Urea was PKR 780/bag on 1st January 2011. It ignores the impact of gas curtailment and delayed imports by the GOP.

60. FFBL’s gross profit margin of 36% is modest when compared with KSE top 25 companies or international companies such as SAFCO and QAFCO.

61. The ER has completely ignored the role of ‘price leadership’ as explanation for price increases. Such omission was given as a reason by the court for quashing the order of MCA in the DG Khan Cement Companies Ltd vs MCA case. How can FFBL be dominant when price increases result from price leadership and the retail price, in any case is the highest manufacturing price. Thus Had FFBL not increased prices the difference would have been pocketed by the middleman without any advantage to the consumers or the exchequer.

The following additional points were raised by FFBL with respect to Excessive Pricing during the course of hearings:

62. The unreasonable increase in price mentioned in clause (a) of sub-section 3 of Section 3 of the Act must be read in the context of sub-section 2 of Section 3 of the Act and when seen that way an abuse of dominance can only take place when there are practices involved that prevent, restrict, reduce or distort competition in the relevant market. Price increase cannot be seen as a violation unless it is established to be anti-competitive or a result of unfair trading conditions. Since there is no allegation of such nature these proceedings are not maintainable

63. Excessive pricing is not regulated in Competition law in the EU. US follows a similar approach and with regard to OFT in U.K price increases are seen as

justified when carried out in the wake of a supply shock or increased demand. If the before and after scenario is looked at in the prevailing case, this one year was an anomaly or aberration owing to the effect of gas curtailment.

64. In the South African jurisdiction there is reluctance to pursue such cases owing to technical difficulties. They are of the opinion that such determination be best left to the market dynamics.

65. Gas curtailment reduced FFBL's production by 35% over two years which in turn resulted in increased cost of production. The cost of production increased by 21% over the last two years. The actual price increase turns out 13% and not 86% when the imposition of GST by the GOP, Reduction in production capacity owing to gas curtailment and inflation are accounted for.

EFL:

66. EFL pointed out that unlike how it referred to in the ER and SCN, Engro Chemical Pakistan Limited (ECPL) was de-merged and transferred to the EFL by virtue of Company Ordinance 1984 and by virtue of a court decision all its assets and agreements were transferred to the EFL. Therefore for the purpose of this reply where ever there is a mention of ECPL it is to be read as a reference to the EFL.

Individual/Collective Dominance:

67. As per EFL owing to huge upfront capital investments in establishing fertilizer plants and gas constraints it is inevitable that there will be a few manufacturers of Urea in Pakistan. In respect of "ECPL and DHCL" group while DHCL and its associates hold a substantial share in the EFL's parent company their involvement is only limited to the board as management of each company is independent and make their own decisions regarding operations. With regard to the installed capacity for Urea manufacturing the EFL and DHFL have 32.6% and 7.7% market share respectively but owing to Gas curtailment and actual production the market shares have been 26% and 4% for 2011 respectively.

68. The assertion that supply of Urea is less than its demand misses the dynamics of Urea fertilizer market in Pakistan. Prior to 2011 it was because the total installed capacity could not cater to the demand and that trend continued because of gas curtailment. To fill the gap between supply and demand the GOP imports Urea and makes it available at highly subsidized rates. Price competition therefore exists not just between the local manufacturers but also between each manufacturer and GOP's imported Urea. Since Urea is a commodity with very little quality differentiation its price equalizes in the market.

69. GOP in 2005-6 had approved gas allocation of 100 million cubic feet per day (MMSCFD) to be supplied by SNGPL to a fertilizer plant. This was to be awarded through a bidding process and the EFL was successful in obtaining it. The EFL set up a plant at a cost of over 1.1 bn USD, that on initiating operation in December 2010 suffered heavy gas curtailment. Other plants on SNGPL and SSGC networks have also suffered. Plants on Mari Gas suffered lower curtailment of 7-9% per day. If the curtailment had not happened the supply would have surpassed the demand.

70. In the gas curtailment scenario utilized capacity cannot be a measure of production efficiency. While there is difference among local manufacturers in production and gas consumption, the much lesser capacity utilization has been due to gas curtailment. The gas supply to EFL's new plant has been so meager that it allowed it to operate but inefficiently.

Excessive Pricing:

71. The Assertion that the GOP has always supported the Fertilizer Industry to ensure sustained availability of Urea to farmers has proven wrong in the last few years. The curtailment of Gas to fertilizer Industry has been much more than other parts of the Economy. While other industries can substitute gas with other fuels the gas input is necessary for Fertilizer plants. The subsidy given by the GOP in the form of reduced prices on natural gas is for the farmers and its benefits are more than passed on to them.

72. Although the EFL increased the prices of Urea in 2010 and 2011 but a large part of the increase is attributed to gas curtailment imposed upon it. The prices in the end market were even higher due to black marketing by the middle-men. The report in Dawn mentioned in the ER pertains to black marketing of Urea by dealers.

73. Fertilizer industry is not the only one where the prices of gas crisis are being passed on as increases in fuel prices are regularly passed on by the GOP in the form of higher tariffs for electricity, petrol, diesel, CNG etc. In fact all sectors pass on their cost increases to customers. Frequently the increases are even greater for margin improvement purposes as in Cement, Steel, Plastic and Steel products in line with multiple factors such as international commodity prices, local demand increase, local inflation margin improvements etc. The Fertilizer sector is no different and therefore the expectation that fertilizer sector will increase price only with respect to gas price increase is unreasonable.

74. Like other commodities international Urea prices have also exhibited a significant jump over the last four years, however this trend was not matched by the local Urea prices up until 2010 on account of relative stability of input prices and steady supply of gas. Only gas curtailment caused supply shortages putting pressure on EFL and others to increase prices. As pricing is always at margins therefore the Urea price moved up unilaterally due to the differences in impact on Urea producers (with some raising prices and others following). With much higher international prices, these price rises would even otherwise be justifiable but would have been much lower had the curtailment been equally distributed.

75. Price increase in the ER needs to be adjusted for GST. Urea prices in November 2010 were PKR 830/bag (ex GST) and PKR 1362/bag (ex GST). Thus the price increase was 64% as against the 86% mentioned in the ER. Prices increased from PKR 830/bag to PKR 1720/bag between November 2010 and July 2012. Gas curtailment while the greatest contributory is only 32% of the variables responsible for the increase in price. The remaining 68% is accounted for by GIDC, GST imposed by GOP and inflation driven increase.

76. Prices of other commodities have also registered abnormal jumps over recent years. Cotton Jumped from PKR 1070/maund to 3600/maund between FY 2009 and 2010. Wheat also increased from Pkr 660/maund to pkr 875/maund in 2010-11. Based on international demand/supply and other factors, commodity price changes are normal e.g. crude oil prices jumped up 79% in 2009 resulting in significant profit jump for oil related firms. None of these increases were preceded by similar level of increases in their input costs but were primarily driven by supply/demand dynamics. Unfortunately Fertilizer Industry is the only one being singled out. Even in 2011 when Urea prices increased by 64% after incorporating GST its price differential with the international prices increased to PKR 879/bag as against PKR 493/bag in 2010. Unless the EFL attempted to sell over the international Urea price how could the question of abuse of dominance arise.

77. Urea fertilizer is a market driven product. This is apparent from pricing behavior in 2011 and the first half of 2012. In 2011 GOP imposed gas curtailment on the industry resulting in lower production of Urea. The GOP did not import Urea on a timely basis. To offset losses Urea manufacturers increased prices and the market moved in tandem due to shortage of Urea. Market prices remained 150-200 PKR/bag higher than the EFL in the market due to black marketing. In 1Q 2012 GOP's imported Urea price was PKR 1300/bag but was sold in the market for 1500-1550/bag with the difference pocketed by the middleman. At this time the EFL's Urea price was PKR 1790/bag. Later the GOP also increased its price to PKR 1600 due to the middleman factor. Market based behavior of Urea can also be substantiated from the fact that when due to improved availability on account of imports, the EFL was forced to reduce its price by PKR 145/bag despite a weak financial position.

78. For the old plant the capacity utilization was 85.3% and not 97.7% in 2011. This utilized capacity could have been a little higher had some gas not been diverted to the new plant. Capacity utilization for the new plant was only 42% in 2011.

79. The EFL always increased its prices after taking into account the curtailment and production levels on both its plants. It is therefore incorrect to say that the old plant is the major beneficiary of the price hike as both the plants are owned by the

same legal entity. The profitability figures quoted are misleading due to capitalization of massive investment made.

80. Regarding the Assertion that the EFL's remedy for gas curtailment to its new plant lies in obtaining the 'default gas', SNGPL never provided the gas as committed in the GSA. It has provided gas enough only to enable 222 days of production from January 2011 to June 2012. The default gas that became due for the first month of supply i.e. December 2010 expires in December 2012. The default gas can be a maximum of 20 MMSCFD over the 100 MMSCFD that SNGPL is obliged to provide. EFL's plant is unable to take more than an extra 7-8 MMSCFD. When SNGPL is not even able to provide the 100 MMSCFD that it was obliged to the outlook for the future appears to be even bleaker.

81. As per EFL they have already invoked legal remedies by filing a writ in the honorable Sindh High Court and despite the Court's order to supply gas it remains unimplemented to date despite initiation of contempt proceedings against the non-conformist.

82. EFL is in great financial distress and has approached its lenders for re-profiling of loans through extension of tenor by around two and a half years. The EFL has taken loans to the tune of PKR 70 bn which have to be serviced and the EFL is already in a position where it is not able to do so. While the net cash generation for 2012 is now estimated PKR 8.5 bn the total debt that needs to be serviced stands at PKR 18 bn i.e. a net cash deficit of PKR 9.5 bn.

83. EFL is on record to have stated publicly and officially in writing to GOP and the Commission that it will reduce its prices if the regular gas supply is restored. The EFL has always provided a basis to both the Commission and GOP as to why it is increasing price and the rationale for the quantum of the increase.

84. In view of the above the assertion that the EFL should not have increased prices rather should have exhausted the stipulated remedies (default gas) has no merit whatsoever.

85. Apart from financial charges, principal repayment of long terms should also have been included as costs that need to be recovered. It is submitted that the price of fuel gas PKR/MMBTU is the same among all the manufacturers. While the fuel cost/ton may vary among the manufacturers on account of some differences in efficiency the range of PKR 29/bag to PKR 176/bag is too wide and seems incorrect. The EFL's old plant cost of fuel gas/ton is PKR 126/bag and that of the new plant is 130/bag. Had the new plant received its full allocation of gas the fuel cost would have been PKR 50/bag.

86. EFL's packing material cost was PKR 26/bag, Chemicals and supply cost was PKR 3/bag. For the full year 2011, EFL's cash fixed cost (excluding depreciation) was PKR 3,342M. With a production of 1,158 Metric tons this works out to PKR 144/bag. The fixed cost appearing in the accounts and financial numbers were lower on account of delayed capitalization of the new plant. Ignoring the capitalization, the EFL's cash fixed cost (excluding depreciation was PKR 3,942M and actual production was 1,279 million tons (including production of 121,000 tons capitalized) cash fixed cost is therefore PKR 154/bag a 10% increase compared with 2010.

87. The assertion that input cost did not change significantly is not correct as per the increases shown for fuel gas and fixed costs above. EFL also needs to account for repayment of loans as a part of its input costs.

88. The EFL's input cost has in fact increased by 93% from PKR 641/bag in 2010 to PKR 1240/bag in 2011. Cash fixed costs per bag increased from PKR 140/bag to 154/bag and financial charges exhibited a whopping increase of 770% as the new plant started incurring financial charges. Therefore it is incorrect to say that input cost did not register any notable increase to warrant increase in prices. These input prices would have been far less had gas supply not been curtailed

89. As for the subsidy it is submitted that it is to the farmer and not fertilizer industry. In any case the scenario has changed since Jan 2012 after imposition of GIDC. Feed gas price for the fertilizer plants was increased by a massive 206% through

an imposition of PKR 197/MMBTU GIDC. When compared with other sectors this increase was highest for the fertilizer sector.

90. The discounts mentioned in the ER are therefore much lower now. However the price at which gas is supplied to Urea producers is the same as that of IPPs, captive power plants and other general industrial consumers.

91. It is also important to understand the global dynamics of the fertilizer industry. International prices of Urea during 2011 were USD 517/ton compared to USD 267/ton in Pakistan in spite of massive capacity utilization decline faced. Middle East and North Africa who are key Urea producers enjoy gas price of USD 0.7-USD 1.00. In US this price is USD 2/MMBTU. Urea producers in Pakistan paid USD 1.95/MMBTU in 2011 (barring specific investment driven lower feed stock prices, for a period of 10 years to two plants) While the international prices of Gas have remained unchanged after the imposition of GIDC, Urea producers in Pakistan are paying USD 3.95/MMBTU for gas. Therefore it is imperative to understand that prices of Urea are not a function of input costs only. High international prices are a reflection of global supply/demand dynamics as well as highly capital intensive nature of the industry since these factors warrant high margins over input costs.

92. As per EFL, there are two types of Subsidies.

93. Every year GOP imports Urea to bridge the supply-demand gap. Since International prices are significantly higher than local Urea, GOP imports at international prices and sells at local prices, the differential being the subsidy incurred by GOP. EFL's new plant can meet 21% of the total demand for Urea in Pakistan. It has the potential to save precious foreign exchange and the huge amount of cash subsidy incurred by GOP.

94. Second type of subsidy given by GOP is through differential in feed and fuel gas prices. While the quantum of subsidy of PKR 77 bn is correct, the Commission must consider the benefit being provided by the fertilizer industry to the farmers by maintaining a huge differential with international prices. This is despite incurring a higher cost of gas than other regions. The industry is under no legal

obligation to maintain such a differential and is within its right to sell at import parity price like other industries in Pakistan. In 2011, the total benefit that goes to the farmer owing to the differential between the local and import prices is calculated to be PKR 23 bn as against PKR 34 bn attributable to feed and fuel gas cost differential.

95. Abnormal profits should be reflected in a high return on equity ("RoE"). There are many companies who have managed RoEs and RoAs which are comparable or better than the EFL. Margins are a function of capital structure, industry dynamics, management strength and multiple other variables. High RoA or RoE do not imply unfair prices. Moreover with respect to EFL, RoE is not reflective of its worrisome financial position.

96. Considering the three scenarios

    a. EFL received full gas supply and kept the prices at pre-curtailment level (passing only cess and gas price increases)

    b. Gas curtailment happened but the EFL kept prices at pre curtailment level (passing only cess and gas price increases)

    c. Gas curtailment happened and the price increases implemented as in the current scenario

    EFL's calculations show that the first scenario would have rendered the EFL much better off.

97. EFL denies that its gross margins have improved and that the price increase has been used to earn additional margins. The gross margins have been taken from published accounts which are missing some key financial events that impacted the EFL in 2011. Due to non-availability of gas the EFL was forced to delay commercial production until June 2011 even though it achieved production in Dec, 2010. All costs including financial charges, cash costs etc were capitalized and the EFL did not start booking the depreciation up until June 2011.

98. If not for the accounting standards the EFL's net profit margin would have been 6% vs 15% in 2011. The EFL's gross margin should have gone up due to huge

new investment but it rather fell as a result of gas curtailment. The EFL's cash generation in 2011 was barely enough to meet its debt obligation. Had it not increased prices it would have faced a cash deficit of PKR 8.6 bn.

99. As a further proof, in 2012 the EFL is facing a difficult financial situation contrary to the allegation of abnormal profitability growth achieved through price hikes. During the first half of 2012 the EFL suffered an estimated pre-tax loss of PKR 2.5 bn owing to availability of gas for only 45 days. The profit for the first half of 2010 was PKR 2 bn.

100. The profits after tax for 2011 after adjusting for capitalized costs (from Jan to June 2011) were only PKR 1.7 bn which is 54.5% decline compared with 2010. This decline should be seen in the context that the EFL took loans of more than PKR 70 bn for the new plant and servicing of those loans necessitated substantial increase in profitability and cash generation.

101. The prices of Urea in Pakistan are far below international prices and they are higher when compared with India, Bangladesh and Sri-lanka because the governments there offer much greater subsidy than the subsidy provided through lower gas prices in Pakistan.

Miscellaneous:

102. The GOP through various acts and fertilizer policies expressly agreed not to regulate the prices of Urea which is why when the GOP fixed the price of Urea at PKR 1480/ bag through its notification dated 25/11/2011 the EFL pointed out to GOP through a letter that it did not agree with the price fixation. In consideration of a promise of regular gas supply by end December 2011 the EFL had agreed to a price reduction of PKR 100/bag but reversed it when the GOP did not make good on its promise.

103. The figure for PAFL of annual capacity utilization of 35% is misleading as it was curtailed much less than the EFL's new plant. However they reduced Urea

production and used the available gas for CAN and NP production whose capacity utilization at 54% and 76% was much higher.

104. Some of the additional points made by EFL during the Hearings are as under**:**

105. Some manufacturers were greatly impacted by gas curtailment, others were not. Some found their profit margins/profits go up while others did not. Urea is a commodity and this is bound to happen. If EFL's profits went down in 2011 and 2012, then going by the united brands case EFL cannot be told that its prices were unreasonable.

106. The main culprit in the matter which is the GOP is not present here. Ministries have never intervened because since deregulation the GOP cannot regulate under the Price Control Act, 1977. The fertilizer policy however has a provision to keep a check.

107. With regard to the suggestion of capping of prices by the intervener, a cap would force all the plants on SNGPL to shut down.

DHFL:

Simultaneous Issuance of ER and SCN:

108. The simultaneous issuance of both the ER and the SCN show that the SCN was issued without considering whether the content of the ER warranted it. The mechanical nature of the process is in violation of due process of law.

Signs showing that the ER was prepared in a haphazard manner:

109. Several signs such as a blank denoted by [.] where a date needed to be inserted, needless underlining of two paragraphs and the names of two fertilizer companies appearing in brackets with four question marks

110. It appears that the data regarding supply-demand and import of fertilizer from 2006-2011 has been obtained from Pakistan Economic Survey 2011-12 whereas the correct official source is National Fertilizer Development Centre (NFDC).

111. The ER has made error in reporting DHFL's prices of Urea despite this information been provided to the Enquiry officers through DHFL's letter dated December 7, 2011. DHFL's price of Urea for August 2011 was misreported as PKR 2330/bag instead of PKR 1398/bag. The ER failed to mention that DHFL's price for November and December was the same as October 2011 namely PKR 1750/bag. Furthermore DHFL's prices for 2010 shown in the ER do not include price changes made in April and July 2010 despite provision of this information in the said letter. DHFL's price of Urea for May 2010 was PKR 880/bag instead of the PKR 855/bag reported in the ER.

112. ER's capacity utilization figure of 30.5% for PAFL is incorrect and misleading because in addition to Urea, PAFL also manufactures CAN and NP. 30.5% is only related to PAFL's Urea production.

113. DHFL only manufactures Urea and the figure of 44.9% relates to the overall plant capacity of DHFL. Keeping this in perspective, PAFL was not affected by gas shortage to the same extent as DHFL.

114. With effect from 1st January 2011 the fertilizer business of DHCL de-merged into DHFL. The ER failed to refer to it correctly as DHFL.

115. Regarding Subsidies provided by GOP to fertilizer manufacturers the information with respect to PAFL is missing for all three years.

116. The ER claims that DHFL and EFL hold a combined market share of 43% whereas no source or evidence is provided for the same. Even if EFL and DHFL are treated as one during the period October 2010 to September 2011 their combined market share is 27% as per NDFC data regarding their sales**.**

Institutional Bias:

117. Circumstances surrounding the enquiry, preparation of the ER, issuance of the SCN and the adjudication of the same gives rise to institutional bias since the Commission does not seem to comprise separate branches for investigation, prosecution and judging. This seemingly overlapping of roles may undermine a EFL's right to due process of law.

118. The ER and SCN have sought to apply the notions of 'Collective Dominance' and 'Excessive Pricing' in a most superficial manner. These areas are uncertain areas of jurisprudence even in advanced Legal systems such as the 'EU' and the 'US'. Such laws should not be applied in Pakistan where both the economy and the Competition law are underdeveloped.

Collective Dominance

119. The Act does not use the expression "Collective Dominance". 'Collective Dominance' is a concept taken from European jurisprudence and must be understood in the same context. In EU, case laws have been evasive about establishing collective dominance among undertakings. It is well settled that price parallelism is insufficient evidence in itself to establish 'Collective Dominance' between undertakings. This features stems from the interdependence undertakings have in an Oligopoly.

120. The European Court of Justice (ECJ) is clear that price parallelism alone is insufficient to constitute anti-competitive conduct. This is evident from the **Wood Pulp case** and **Hoffman-la Roche**. In Wood Pulp the ECJ annulled much of European Commission's decision finding that the Commission did not appreciate that the behavior of undertakings was a consequence of the non-collusive interdependence that existed in an oligopolistic market. In Hoffman-la Roche ECJ rejected the idea of parallel courses of conduct constituting a dominant position stating that such conduct is peculiar to oligopolies.

121. As described in the ER, Urea market in Pakistan is characterized as an oligopoly, Parallelism of conduct may therefore be most inevitable in this market. The Criteria for determining whether undertakings enjoy 'Collective Dominance' requires the establishment of 'economic links' or more recently 'connecting factors' between undertakings. As per ECJ the undertakings in this group must be linked in such a way that they adopt the same conduct on the market. More recently in **Compagnie Maritime Belge Transporters** it was held that it must be ascertained whether economic links exist among undertakings that enable them to act independently of their competitors and consumers. It further held that the existence of a collectively dominant position may flow from the nature and terms of an agreement, the way it is implemented and consequently from **links and factors which give rise to a connection between undertakings** which result from it.

122. Nevertheless the existence of an agreement or of other links in law is not indispensable to finding of a collectively dominant position as such finding may be based on other connecting factors and would depend on an economic assessment and particularly **assessment of the structure of the market** in question. The ambiguity in the terms **'economic links'** and **'connecting factors'** is one of the difficulties in applying the test. The allusion by the ECJ in **Compagnie Maritime Belge Transporters** to the 'structure of the market' as a connecting factor implies certain stringent conditions that need to exist in an oligopoly for finding of a collectively dominant position. These conditions have been clearly laid out in **Airtours** and subsequently in **Laurent Piau**:

a. Each member of the dominant oligopoly must have the ability to monitor other members for compliance with common policy.

b. Some form of credible deterrent mechanism in case deviation by an oligopoly member is detected to sustain tacit coordination over time.

c. Foreseeable reaction of current and future competitors and consumers must not jeopardize the results expected from the common policy.

123. The difficulty in ascertaining the meaning of 'economic links' and 'connecting factors' can only be understood by examining the situations in which EU

jurisprudence has found 'Collective Dominance' to exist in practice. 'Collective Dominance' has only ever been found when certain explicit consensual arrangement existed between independent undertakings. For Example in:

a. **Compagnie Belge** undertakings were members of a shipping conference;

b. **TACA** undertakings had contractual links with each other and were members of a liner conference which contained common pricing provisions;

c. **Italian Flat Glass** undertakings were found to have formed a cartel;

d. **Almelo** undertakings were members of a trading association;

e. **Wouters** undertakings were contractually linked through their membership in an association although ECJ did not think these links were close enough to establish 'Collective Dominance';

f. **Laurent Piau** undertakings were members of an association with legally binding rules as to members' transactions.

In the absence of such evidence EU jurisprudence has been unable to assert 'Collective Dominance' between undertakings. It is small wonder that this is the case as commentators have argued that collusion is unsustainable without some form of communication between undertakings. The ER and SCN do not refer to any evidence of communication between the fertilizer manufacturers except price parallelism which as mentioned before is legally incapable of supporting a finding of 'Collective Dominance'. The ER and SCN do not describe how the relevant characteristics of the 'structure of the market' are met in the instant case in particular the second requirement of a credible deterrent mechanism. Further there is no allegation in the ER or SCN that price parallelism occurred as an outcome of some communication between the fertilizer manufacturers. Therefore 'Collective Dominance' cannot be said to exist in the instant case.

124. Where the ER lays out the characteristics considered essential for the existence of collective dominance, the characteristics it notes are really those of an

oligopolistic market (Paragraph 87 of the ER). By omitting to refer to the existence of economic links or connecting factors the ER and SCN have erred in law.

US Jurisdiction and Plus factors:

125. This idea also finds resonance in Anti-trust jurisprudence of the US.

126. Oligopolies, price parallelism or coordinated effects are not treated as being anti-competitive in the absence of **plus factors**. The US Supreme Court's treatment of such coordination is as follows:

> *'Tacit Collusion, sometimes called oligopolistic price coordination or conscious parallelism, describes the process, not itself unlawful, by which firms in a concentrated market might in effect share monopoly power, setting their prices at a profit maximizing, supra competitive levels by recognizing their shared economic interests and their interdependence with respect to price and output decisions.'*

127. Even more pertinent is that this aspect of antitrust jurisprudence has received endorsement by the higher judiciary in Pakistan as well as MRTP (Control and Prevention) Ordinance 1970.

128. In **D.G. Khan Cement Companies Ltd vs MCA**, Justice Saqib Nisar after citing several US decisions summarized the legal position as follows:

a. *"Parallel business behavior or conscious parallelism is not in itself sufficient to indirectly establish an agreement in violation of the Sherman Act. Parallel business behavior is all the more possible in the case of standardized products where it is expected that prices will ordinarily tend to move in parallel. Furthermore in a concentrated market where there are relatively few sellers, conscious parallelism is also to be expected.*

b. *If there are certain factors, referred to as 'plus' factors, in addition to and over and above, parallel business behavior, then a presumption arises that there has been unlawful price fixing and in such a situation,*

a violation of the Sherman Act can be indirectly inferred. The 'plus' factors may include evidence demonstrating that the conspirators acted contrary to their economic interests and were motivated to enter into a price fixing conspiracy. The nature of a ***'plus' factor*** *must be such that it tends to exclude the possibility that the alleged conspirators acted independently.*

c. If parallel business behavior and ***'plus' factors*** *are found to exist, the alleged conspirators can nonetheless rebut the inference of collusion by presenting evidence establishing that it could not reasonably be concluded that they entered into a price fixing conspiracy."*

129. Like economic links or connecting factors in EU jurisprudence **'plus factors'** is the extra proof required to conclude that parallel conduct is anti-competitive. US courts often describe conspiratorial motivation and acts against self-interest as evidence of plus factors. While the Supreme Court has not recounted a list of plus factors, numerous plus factors such as 'motive to conspire', 'opportunity to conspire', 'high level of inter-firm communications', 'irrational acts or acts contrary to a defendant's economic interest, but rational if the alleged agreement existed and departure from normal business practices, have been considered by other circuits.

130. The burden of proof for establishing these factors lies with the body alleging anti-competitive conduct. With the establishment of plus factors only a presumption of anti-competitive behavior arises meaning thereby that there undertakings involved are free to present evidence to rebut that presumption.

131. There is a significant body of evidence under EU, US and Pakistani law that has settled the need of persuasive plus factors for undertakings to have 'Collective Dominance'. SCN and ER are against the law for not being in accordance with the law.

132. In addition to price parallelism the only factor mentioned in the ER for 'Collective Dominance' of undertaking is that FFC, FFBL, DHFL and EFL hold a combined market share of 84%. The analysis that DHFL and EFL are connected through

their shareholding is flawed. As per the Competition Assessment study of the Fertilizer sector published by the Commission itself Dawood group holds a 34% stake in DHCL which in turn holds a 38% share in ECPL which is too dilute a shareholding for there to be a cause for concern. Shareholding in itself does not show that the management of the companies is linked. Secondly ECPL and DHCL are holding companies with several businesses and the two do not have any direct link. It is well settled that a subsidiary is independent and distinct from its holding company.

Excessive Pricing

133. Price levels which constitute unfair pricing is another concept inspired by EU jurisprudence. EU has however failed to provide a consolidated and firm view on the issue.

134. According to **Gal** and **Michal** after three decades there is still no sufficiently predictable and concrete definition of what constitutes excessive pricing. **Whish** indicates how the practical difficulties involved in applying this concept have made the European Commission reluctant to scrutinize prices owing to difficulty of translating this into a sufficiently realistic legal test.

135. Under EU jurisprudence an excessive price is ambiguously defined as one having no relation to the economic value of the product. Determining the point at which a price bears no relationship with 'economic value' has produced great difficulties. Sparse EU jurisprudence applied different tests in different cases each time underlining the open textured nature of determining excessive prices. Tests that have figured prominently thus far include:

    a. Comparison between production costs and prices and if the profit margin is deemed excessive whether it is so in comparison with competing products or in itself
    b. A Comparison between prices charged by a dominant firm in different markets and

c. A comparison of prices charged by the dominant firm and other firms in the same market or other markets.

136. Each of the mentioned tests is fraught with difficulties as accounted for in various EU decisions. For example test a does not clarify what a suitable profit margin is leaving it to arbitrary or value judgment. Further test a has been interpreted differently by different courts. According to English court of Appeal it is insufficient to add on a reasonable profit to production costs in determining the economic value. On the other hand the test laid down in United Brands i.e. test a was criticized by the Competition tribunal of South African in Harmony Gold Mining Co. v. Mittal Steel case which adopted a different approach and focused on the causes of dominant power in the relevant market. Without appreciating this complexity the ER and SCN have attempted to apply test a superficially. Keeping in mind these difficulties the ECJ has applied alternative tests as well. Tests b and c however require comparable market to access whether price levels in one market are excessive. These tests are better suited to the EU where the markets of different member states can serve as useful comparators.

137. Most cases brought by the European Commission under the rubric of unfair pricing involve some form of exclusionary conduct rather than exploitative. For example the British Leyland and General Motors cases focused on artificial barriers to trade in cars. In British Leyland the ECJ affirmed the decision of the European Commission without a close scrutiny of cost-price differentials. The decision was based on the discriminatory nature of the charge that was deemed excessive because it hindered competition between British Leyland suppliers.

138. In Deutsche Post AG, the excessive charge for onward transmission of cross-border mail was preventing users from taking advantage of the developing single market for postal services and was therefore the focus of the decision.

139. More recently the European Commission has been vigilant in investigating allegedly high prices charged by dominant firms controlling essential facilities.

140. The ER and SCN have not alleged any form of exclusionary conduct on the part of fertilizer manufacturers and instead only cited adverse effects of high prices on the 'farmer community'. The adverse effects if any of high prices are better left to bodies equipped to deal with such matters. A specific statute Price Control Act, 1977 empowers the GOP to decide whether price levels are fair and to set prices if necessary. In DG Khan Cement case the Honorable High court clearly delineated the proper role of Competition Authorities and Price regulators.

Us Jurisprudence:

141. In the American Jurisprudence, from its inception to present anti-trust law has consistently refused to classify excessive pricing per se as abusive or anti-competitive instead the focus has been on artificial barriers to entry in a market such as exclusionary conduct by undertakings. Anti-trust law recognizes that monopolies may still arise and are legitimate if created through market forces and are allowed to enjoy monopoly profits. This is reflected in the **pronouncement of the US Supreme Court** in the matter of Verizon v Trinko where it was held that charging monopoly prices for at least a short period attracts business acumen and in turn innovation and economic growth.

Discrimination in Gas supply

142. The ER portrays an inaccurate picture of the relationship between the fertilizer manufacturers as it omits to take note of the hostile litigation pending between various players on the issue of gas supply. A writ petition pending in the Lahore High Court instituted by DHFL against most of the other fertilizer manufacturers on the SNGPL network alleges that SNGPL has been discriminatory in supplying gas by providing DHFL lesser quantities of gas than PAFL and AGL. Similarly some other undertakings have challenged the gas supply agreement between EFL and SNGPL in the honorable Supreme Court. Evidence of such legal proceedings depicts the relevant market as an area of contest or competition rather than collusion or coordination.

143. Since the ER mentions the GSA agreement between EFL and SNGPL as a remedy for gas curtailment and the same arrangement does not exist between DHFL and SNGPL, the latter is justified in increasing its Urea prices to overcome the losses incurred as a result of gas curtailment.

144. In any event DHFL has invoked the writ jurisdiction of the Lahore High Court to seek a remedy against SNGPL for the gas curtailment it has faced. This does not mean that DHFL does not have the right to increase Urea prices when necessitated by business considerations.

145. The analysis in the ER to the effect that a fertilizer manufacturer cannot raise its price since it has a contractual remedy to avail makes little sense for the following reasons:

a. Increasing price of a product is a rational decision in the wake of falling output and declining revenues.

b. Any going concern cannot be precluded from taking legitimate business decisions on the chance that recourse to contractual or legal remedies may yield relief sometime in the future.

c. The analysis in the ER ignores the fact that gas reserves in Pakistan are depleting and there is little chance of gas supply improvement in the future thus even the presumed contractual/legal remedy available to ECPL is solely on paper.

146. The ER despite acknowledging the huge (55%) drop in DHFL's capacity utilization and the drop in its profit margin (even after increasing price) has lumped it with the entire fertilizer industry by proclaiming that gas curtailment only affected 27% of the total Urea fertilizer production and that fertilizer manufacturers raised Urea prices unreasonably during the period in question reaping windfall profits. While this may or may not be true for other fertilizer producers it is certainly incorrect for DHFL whose profits admittedly plummeted during 2011 and which took an independent business decision of increasing price to salvage its deteriorating profit margins.

147. GOP being the sole importer of Urea into Pakistan fills the demand supply gap mentioned in the ER through its imports. Earlier GOP imported Urea comprised a small portion of total Urea supply in Pakistan but In years 2008-09, 2009-10, 2010-11 and 2011-12 GOP it comprised 16%, 23%, 11% and 28% of the Urea consumption in Pakistan. This increase in imports was on account of reduced production due to gas curtailment. The amount of Urea available in the market varies owing to the quantity of Urea imported by the GOP and the timing of these imports. Urea is in high demand during the Kharif and Rabi seasons and if is unavailable during these times its prices escalate.

148. While the demand for imported fertilizer was increasing in 2010 as a result of diminishing domestic production, the GOP for some reason decided to reduce imports in 2010-11. This resulted into an already acute shortage being exacerbated, thus causing the prices to shoot up.

149. The importance of GOP's influence in the fertilizer market is acknowledged in the Competition Assessment Study of the fertilizer Sector in Pakistan, published by the Commission itself. The said study states:

> *"Overall, therefore, direct and active intervention by the government in the pricing mechanism considerably restrains the fertilizer producers in charging prices that are either too high or low."*
>
> and that:
>
> *"… a case of exploitative pricing and excessive profiteering solely as a result of anti-competitive practice cannot be established for the sector, again due to the subsidy mechanism and policy interventions such as Urea imports."*

It is surprising that the ER or SCN do not bring out the role of GOP in this perspective.

150. By not indicating the type of action the Commission may take pursuant to the SCN, DHFL's due process rights have been affected as it is not able to make appropriate submissions as to why a particular order should not be passed against it.

151. The ER states that letters were written to all major Urea producers on 31 December 2010, asking for reasons of Urea price increase. DHFL did not receive any such letter perhaps because it was not considered to be a major producer.

152. The market of locally manufactured Urea in Pakistan cannot be termed as captive as is evident from the data provided in the ER regarding the demand-supply situation during Rabi 2010-2011 and Kharif 2011. According to tables on page 10 of the ER, for each of the 12 months during the relevant period there were substantial opening inventories implying a surfeit of Urea in the market. This negates the idea that the Urea market is captive as all Urea produced by the fertilizer manufacturers is readily sold. As a matter of fact the demand for Urea is elastic and fluctuates seasonally.

153. By holding that DHFL is individually dominant the ER and SCN expose themselves to an internal inconsistency as they also allege that DHFL is collectively dominant. It is impossible in a situation of 'Collective Dominance' for one undertaking to act independent of its competitors. In order to be individually dominant an undertaking has to be able to act independently of its competitors. DHFL has less than 10% market share and cannot be simultaneously individually and collectively dominant as it cannot work independent of its competitors and in cahoots with them simultaneously.

154. The assertion that the price increases were simultaneous and coherent is not established in the ER and incorrect. The table purporting to a summary of price increases during last 3 years in the ER does not mention the actual dates on which prices were increased but only months. By not having the exact dates the allegation that prices were increased simultaneously or that ECPL raised its prices prior to others and is a price leader cannot hold true. DHFL sought to maintain higher prices than the market during the period April-June 2010 and then again October-November 2011 but was unable to maintain that because of falling sales and had to reduce its prices. Without an increase in prices DHFL would have been in dire financial straits and may not have been able to survive as a viable concern.

155. The assertion that Urea fertilizer prices have increased by 86% is incorrect given the imposition of GST in March 2011. In this context the real price increase is 60%.

156. The so called assessment of input costs undertaken in the ER is superficial and hopelessly deficient. For instance the cost of natural gas as a raw material has been determined as a percentage of revenues rather than total costs. Furthermore as per data provided by DHFL in its letter dated December 7 2011, DHFL's cost of manufacturing Urea/ton increased by 17% in 2010 and a further 27% in 2011. This information has been overlooked in the SCN and ER. With a fall in production, it was inevitable that per unit fixed costs and financial costs would increase. Despite the fact that these figures were provided to the enquiry officers the ER inexplicably concluded that the other cost components remain more or less unchanged in the year 2011.The ER has missed the point that the issue is not about the cost of raw material but its non-availability. During 2011 the plant operated at below 45% of its capacity and the supplies dwindled further so that till July 22, 2012 the plant only operated at 18.8% of its designated capacity. DHFL could not have closed its eyes to this eventuality in 2011 and was therefore justified to build reserves to tide over curtailment period in 2012.

157. The analysis in the ER with regard to the subsidy provided by GOP to fertilizer manufacturers is incorrect as this subsidy is entirely passed on to the consumers or else the prices of local Urea would be at par with imported Urea.

158. In determining the reasonableness of prices the quantum of profits alone is not decisive. No evidence is provided backing the claim of ER that no industry in the world makes such gross margins. A passing reference is made in the ER stating the prices of Urea are higher in Pakistan when compared with India, Bangladesh, Sri-Lanka and Afghanistan. This observation in itself amounts to nothing without an analysis of market conditions prevailing in those countries.

PAFL:

159. Taken to it logical conclusion, the SCN amounts to price regulation, a role competition authorities are not best equipped to handle given international

practices and precedents. Prices of Urea are much lower in India because of the massive subsidy offered by the Indian Government.

160. The SCN is based on the ER of the same date suggesting that the Commission may not have had the chance to properly evaluate the ER before issuing the notice.

Individual/Collective Dominance:

161. The GOP itself is a huge supplier of Urea. The retail price of Urea supplied by the GOP is more or less the same as undertakings since factors that compel a change in price apply across the board and reflect a rational economic response by all manufacturers.

162. The SCN is liable to be discharged as the PAFL is not in a dominant position in the market whether individually or collectively with other manufacturers. In assuming that Urea market in Pakistan is captive the ER relies on a decision of the Commission dated July 23, 2010. Pak-Arab was not a party to the above matter and therefore not heard. It respectfully disagrees with the reasoning and conclusion of the Honorable Commission.

163. The Urea manufactured and sold by the PAFL constituted less than 0.59% and 0.47% of the Urea manufactured and sold in Pakistan during the relevant period and therefore cannot be considered dominant by any stretch of imagination. Even if Pak-Arab is considered along with its associated company i.e. FFL it does not have the ability to act independent of its competitors or consumers and cannot be considered part of any oligopolistic structure with its sales too low in comparison to other manufacturers.

164. The ER's assertion regarding lack of competition is incorrect on multiple scores. Excess capacity compared to demand suggests that there is always an incentive to compete on prices. The ER overlooks the massive expenditure incurred by Urea manufacturers on advertisements which would be unnecessary in case of ensured sales. The ER fails to appreciate that the price reversal carried out by EFL from

PKR 1980/bag to PKR 1580/bag was a result of competitive pressure exerted by other undertakings by not following its price increase rather than GOP intervention. The ER overlooks that when GOP imports are accounted for the demand does not exceed supply. Huge inventories carried from one season to another belie the assertion that consumers have no choice but to buy every single ounce of Urea.

165. Urea market in Pakistan is not characterized by 'Collective Dominance' especially when imported Urea is included in the 'relevant market'. For an oligopolistic market to exist the market shares should be approximately similar and since PAFL's market share by itself or even combined with its associated company is too low (8%) it cannot be considered a part of an oligopolistic structure. The PAFL does not have a common policy with other Urea manufacturers or links as envisaged in the EU case law to show it to be collectively dominant with other manufacturers.

166. Professor Whish has stated that one of the most complex and controversial issues in Community competition law has been the application or non-application of Article 102 EC to so called 'Collective Dominance'. There have been no cases in the European union in which firms that have been accused of engaging in abusive conduct under Article 102 have been found to be collectively dominant on the basis of tacit collusion of the nature being alleged in the ER rather such decisions have been limited to firms having some sort of economic or contractual links.

167. Simultaneously, the Enquiry committee ('the Committee') tries to establish that the undertakings in the Urea fertilizer market are dominant collectively as well as individually. The Committee relies on an earlier decision of the Commission that found the Urea market in Pakistan to be 'captive' and which is belied by reasons set out in Annex-A and the following facts

168. The characteristics set out by ER even if necessary do not constitute sufficient conditions for collective dominance particularly as applicable to Urea market in Pakistan and more specifically to the PAFL. Based on these or otherwise, PAFL

denies being collectively dominant with other manufacturers by itself or along with its associated company.

169. There are not three but four groups of manufacturers. Additionally the GOP is a significant participant as an importer. The PAFL itself or together with its associated concern is not mutually interdependent with the remaining manufacturers as with its limited sales it has no ability to influence prices. Any attempt to sell at a higher price will be met with failure as dealers would not be willing to buy and lowering of price would not lead to similar behavior by other manufacturers due to lack of mutual interdependence. A change in output by the PAFL is also unlikely to impact other undertakings as the PAFL along with FFL accounts for less than 9.5% of the total installed Urea production capacity in Pakistan.

170. Regarding entry barriers, Both FFL and EFL did set up Urea plants after incurring heavy investments. This belies that new investment is not taking place since it was only been impacted in the last year or two due to gas curtailment.

Excessive Pricing:

171. The actual price increase was 60% (the rest being attributable to GST). While natural gas constitutes a small percentage of input costs (10-15%) it is the lifeline of the industry. Before Gas curtailment Urea prices in Pakistan remained steady for a number of years showing the industry cannot be accused of either tacit or express collusion. While plants on SNGPL/SSGC networks that constitute 44% of total available capacity of Urea were more significantly impacted, there was also a 12% curtailment of gas to plants on Mari Gas. The impact of this massive curtailment can be fathomed from the GOP imports of Urea rising from 2% of total Urea supply in 2007 to 52% up to April 2012 due to resulting idle capacity. During the period considered by the ER and thereafter the PAFL has made significant losses on Urea production and sales.

172. When 44% of the industry is so directly impacted by the gas curtailment the uncertainty it creates is naturally going to affect prices. Under these circumstances and the 'dealer factor' the response from even a firm that was not so significantly impacted by the gas crisis was to increase prices lest the middleman took advantage of the situation.

173. Even the GOP found the need for price increase justifiable and reasonable due to changed dynamics and therefore fixed its price at PKR 1480/bag in November 2011 after instructing Urea manufacturers to reduce theirs from PKR 1580/bag. This was done with the assurance that gas supply would be restored. This implies that price increase to this level at least, cannot be considered unreasonable though any increase beyond it is also justifiable.

174. PAFL is neither dominant nor has it abused any 'dominant position'. The PAFL has not made any 'excessive profits' during the relevant period. Its revenue from Urea sales went down significantly from 2010 to 2011 and it even suffered a loss.

175. The ER does not set out any realistic or legally justifiable basis for determining the 'unreasonableness' of price increases in terms of section 3 of the Act. Even the EU case law has been inadequate in this respect.

176. In the United Brands Case, the ECJ held that a price is deemed excessive when it has no reasonable relation to the economic value of the product and adopted the following two stage approach in determining it: (1) Whether the difference between price and cost incurred is excessive; and having established that (2) Whether the price charged is unfair in itself or when compared to competing products. What is evident is that meeting only one of the two conditions is not sufficient, needless to say that the ER is even deficient in meeting that.

177. Profit as a percentage of sales is not the appropriate criterion to prove excessive profits. The profitability analysis set out in the ER is based on accounts of undertakings. A growing body of economic literature holds that accounting profits do not reflect economic profits (except under most unrealistic assumptions).

178. The undertakings passed on the affect of GOP based subsidy to the farmer by maintaining a price differential with international Urea prices that far exceeded the subsidy.

179. The actual increase in price was 60% and not 86% as the rest is attributable entirely to imposition of new taxes. To the extent that price was increased it was largely dictated by gas curtailment. While FFL was not impacted to the same extent as EFL, the two constitute one economic unit, where one is making huge losses it is reasonable for the economic unit to charge prices keeping this in perspective.

180. The ER's assertion that gross margins enjoyed by Urea producers in Pakistan are unmatched by other industries in Pakistan and elsewhere has been without any supporting data. In any case it is misleading to place reliance on 'gross profits as a percentage of sales'. In case of the PAFL these gross margins are misleading as Urea sales are only one segment (3.4%) of the PAFL's sales revenues for 2011 and 4% of fertilizer sales revenue. If one takes out the CDM project revenues and income from other sources the numbers are significantly impacted, in fact the PAFL made a net loss in 2011 on sales of Urea.

181. It is totally misleading to rely on profits before tax as a percentage of sales as modest profits if spread over limited sales may yield a higher figure of 'profits before tax as % of sales' even though the profit after tax may remain the same. This shows the Enquiry Committee's bias against the undertakings. The proposition that despite being on SNGPL network fertilizer plants were able to increase profits manifold is not substantiated when we look at profits after tax which is the only meaningful figure to consult.

182. The Enquiry Committee's conclusion that only 27% of the available capacity of the industry was hit by gas curtailment in 2011 is ex facie incorrect and should be 35%. It does not take into account that FFBL's plant is also located on the sui network and supplied by SSGC. The gas curtailment of FFBL was 30% (over and above the 20% announced by the GOP). In fact overall gas curtailment was 48% instead of the 20% originally notified. If FFBL's plants unplanned reduction in

gas supplies is taken into consideration it translated to 44% of the its total manufacturing capacity in 2011. The unscheduled gas curtailment has led to serious uncertainly among manufacturers with plants on the SNGPL network. The analysis of FFL's capacity utilization is incorrect as it does not appreciate that FFL was only carrying out test operation in 2010 and it only declared commercial production in July 2011.

183. The ER places significant reliance on the GSA between SNGPL and EFL which is erroneous because it is not representative of GSAs of other undertakings on the SNGPL network. The ER focuses on input costs without appreciating that high fixed costs when allocated over fewer units produced cause the cost per unit to go up. The ER relies on what it considers to be excessive profits by some to suggest all undertakings are making similar profits.

184. The ER fails to account for some relevant considerations. While it laments that some manufacturers have made more profits than previous years, it fails to factor in the huge investments made by them. Specifically with regard to PAFL it fails to note that it is in fact making losses with respect to its Urea business. PAFL's RoE (6%) and return on capital employed (3%) are far too low to qualify as excessive profits. It fails to take on board the fact that even projects based on Mari gas faced a 12% gas curtailment. It fails to give proper weight to the fact that before gas shortages there were no price increases of the kind under discussion. What should also have been accounted for is the uncertainty affecting the industry.

185. The ER's assertion that the demand for Urea surpasses its supply is erroneous when the imported Urea is taken into account. There was no time in Rabi 2010-11, Kharif 2011, Rabi 2011-12 or even subsequently that demand exceeded supply. Even the finding of the honorable commission with respect to captive market in the matter of 'Tie in',of which FFL was not a party needs revision as it is not based on sound legal or factual foundation. The statistics in paragraph 27 of the ER although misleading do not lead to the conclusion that Urea production always lags its demand. With PAFL and FFL's combined market share of less than 10% and no shortage in the market as per NDFC figures, PAFL can not set a higher

price in the market. At the same time selling at a lower price would be economically irrational by creating `arbitrage opportunities for the dealers.

186. Pakistan's Urea market is not captive because GOP itself is a significant supplier of Urea and ensures that all shortage is catered to. Resultantly there are always inventories carried forward by the undertakings.

187. Gas curtailment was more extensive than noted in the ER. PAFL was not made part of the enquiry so the analysis has been made without its input and some of the numbers provided for its cost/bag are incorrect. The ER concluded that exorbitant profit was made from the sale of Urea in 2011 whereas PAFL's total revenue from the sale of Urea was PKR 614 million while gross profit was PKR. 9513 million and profit before tax for the year was PKR. 6,311 million- which obviously cannot be earned from a revenue of 614 million. The Enquiry Committee's assertion that natural gas's price remained unchanged overlooks the impact of lower production of Urea on the economies of scale and prices.

188. The ER notes that an important indicator used by economists worldwide to assess reasonableness of prices is the profitability of the undertakings concerned. This is misleading because the determination of what constitutes excessive profits is itself controversial. Recent decisions of EU have held that even if the profit margin of a dominant firm is high or even excessive it would be insufficient to establish that the price charged is abusive.

189. It is incorrect that GOP did not intervene as it did so by fixing the price no lower than PKR 1480/bag and by importing Urea.

FFL:

Being part of the same group as PAFL and represented by the same lawyers the gist of FFL's major submissions were more or less the same as that of PAFL.

AGL:

Individual/Collective Dominance:

190. The very basis of the ER is questionable as it conflates principles applied in cases of abuse of dominant position with those applied in ex ante merger analysis. AGL is a victim of a duopolistic market structure that has stifled growth and competition in the market.

191. The SCN is ambiguous in identifying the alleged violations of the Act by PAFL. Unclear allegations of tacit collusion and common policy/economic linkages are made without referring to any supporting data. Concepts of 'captive market' and 'Collective Dominance' are incorrectly employed to arrive at erroneous conclusions. There is also nothing to support the allegation of the so-called 'monopoly profits' as even the ER itself shows the PAFL as accruing losses in the relevant period.

192. In the present context the concept of collective dominance is at best an economic theory which has yet to be applied. While American and Indian jurisprudence do not recognize this concept, judgments from European Union have alluded to its theoretical possibilities without ever holding an undertaking liable for abuse of collective dominance.

193. The Urea fertilizer market is a duopoly comprising Fauji Group and Dawood Group having 41% and 43% market shares respectively. They are the market leaders and price setters while the remaining firms lack control and have smaller shares in the market.

194. The AGL has 7% market share. Due to financial difficulties the it's capacity utilization fell from 111% to 63% from 2008 to 2011. This may be easily traced to the enormous increase in per unit cost of raw material from PKR 1812/bag to PKR 4467/bag (146% increase). Even comparing 2009-10 to 2010-11 the cost of manufacturing a bag went up by 81%.

195. It was suffering from frequent and persistent gas load-shedding imposed on it by the GOP authorities. GOP introduced levies served a further blow to the AGL's balance sheet. Despite increasing price it suffered a loss of PKR 295 Million in the financial year 2010-11.

196. The ER alleges that the AGL is enjoying a dominant position however no data or supporting facts are provided to show how a small market share holder (7%) has control over the market in terms of production or pricing.

197. It is a settled law that an undertaking with less than 10% share cannot be said to hold a dominant position in a market. In Metro II the European court held that no dominance can arise when a super market chain had less than 10 percent share of the general electronic equipment market for leisure purposes and less than 7 percent in the colour television market. In establishing dominance in Hoffman La Roche case, ECJ relied upon great disparity in market shares between HLR and its next largest competitor and technical superiority of HLR over its competitors. The ECJ maintained that the existence of a dominant position may derive from several factors which taken separately are not necessarily determinative, but among which a highly important one is the existence of a very large market share. The AGL does not fulfill any criteria mentioned above including the highly important one of a large market share to qualify as a dominant player in the relevant market.

198. The benchmark set by Competition Commission of India is higher than 36% to declare an undertaking dominant in a market. As per American Supreme Court a firm is monopolist if it can profitably raise prices substantially above the competitive level. In nearly all cases involving abuse of dominant position the accused had much larger market shares than the AGL.

199. Much is made in the ER of the concept of 'captive market'. The lag in supply against demand for Urea is a macroeconomic problem that has come about due to a complex interplay of national policy objectives, shortfalls in basic raw materials, constitutional factors favoring certain undertakings and other important factors. The ER fails to provide a rationale for holding it individually or jointly liable for a macro-economic industry wide problem.

200. The ER connects disparate economic theories to allege that all the undertakings in the relevant market have the ability to behave to an appreciable extent independent of customers, competitors and consumers and are therefore dominant. If the criteria applied by learned commission is one where firms may be held liable irrespective of their market share then it is unclear how firms holding 1% share in a perfectly competitive market escape liability. Not only is such reasoning based on faulty legal and economic presumption but also undermines the whole premise of a section 3 offence under the Act. As per ECJ in HLR, abuse of a dominant position takes place when the behavior of a dominant undertaking hinders the maintenance of the degree of Competition prevailing in the market or its growth. By allowing AGL to survive the tough market conditions its price increases led to greater competition in the market rather than hindering it.

201. The ER despite admitting that AGL was part of the 27% manufacturers severely impacted by gas prices proceeds to hold it liable for abuse. While the ER provides details regarding FFC and EFL, it does not present any cost/benefit or profit and loss analysis regarding AGL and incorrectly generalizes allegations.

202. AGL has suffered enormous losses due to increase in input costs such as price of natural gas. Paragraph 52 of the ER shows that it faced the highest costs as a percentage of revenues when compared with others. The ER discusses the subsidy provided by the GOP without taking into account the tremendous increase in GOP levies and 57% decrease in capacity utilization of the AGL from 2010-2012. Despite factoring in the subsidy, gas prices in Pakistan are some of the highest in the world while prices are some of the lowest. According to the internal assessment of the AGL's the total impact of increase in gas prices and GOP levies during the relevant period was PKR 347/bag.

203. The most blatant example of the perverse logic running through the ER is when it states AGL to be incurring a loss in the year 2011 and yet goes on to accuse it of "excessive profiteering". The ER fails to establish why the Urea price was not increased by the AGL in the same manner prior to gas load shedding despite the so-called dominant position. The American anti-trust law takes an even more

lenient view to increased pricing and dominant position. In the Verizon Commun case it was held that:

> *"The opportunity to charge monopoly prices at least for a short period is what attracts "business acumen" in the first place; it induces risk taking that produces innovation and economic growth. To safeguard the incentive to innovate, the possession of monopoly power will not be found unlawful unless accompanied by an element of anti-competitive conduct."*

204. As costs of production went up the AGL having fewer economies of scale had no choice but to increase price to break even. The conclusions drawn in the ER only take into account the market conditions faced by EFL and FFC and fail to incorporate the setbacks faced by a small undertaking such as the AGL.

205. Regarding the GSA between SNGPL and EFL, it is the main cause of unprecedented and enormous gas load-shedding that AGL has been subjected to by SNGPL. This discriminatory treatment meted out to the AGL is a subject matter at the Honorable Lahore High Court and the Honorable Supreme Court.

206. Collective Dominance is a European law concept specifically invoked by the Commission in cases involving ex ante merger approval. Despite the Airtours and Impala Judgment clarifying that ex ante and ex post rules regarding collective dominance should be clearly separated the ER has combined disparate areas of law to form a novel and untested offence that is simply not an offence under the Act.

207. The case of Airtours (involving merger control) lays down three stringent conditions for a finding of collective dominance. First, there must be sufficient market transparency for all members of the dominant oligopoly to be aware sufficiently precisely and quickly of the way in which the other members' market conduct is evolving. Second the Situation of tacit collusion must be sustainable and third the foreseeable reaction of current and future competitors and consumers would not jeopardize the results expected from the common policy. It is submitted that even the requirements necessary to apply the merger control conditions of collective dominance have not been met through the ER. In the instant case no cogent evidence has been provided to show even the prospect of collective

dominance or tacit collusion in the future or past. It is further highlighted that no undertaking has been held liable under Article 102 of EU law on the basis of collective dominance.

208. Under European Union law the criteria for showing collective dominance in ex ante merger analysis is quite strict in that economic links need to be proved. The undertakings identified as collectively dominant in most cases were linked by consensual agreements. Relevant case laws in this regard are Maritime Belge, TACA, Italian Flat Glass, Almelo, Wouters and Laurent Piau. No such structural or economic links are alleged in the ER, let alone proved. The concept of collective dominance is not envisaged in the Indian Competition Act 2002.

Constitutional Objections:

209. The Competition Act, 2010 is liable to be declared ultra-vires the Constitution of Pakistan, 1973. Federal legislature has no power to legislate in respect of matters not enumerated in either the Federal or Concurrent Legislative list of Fourth Schedule and examination reveals that it contains no entry related to monopoly, competition or of similar nature. The subjects being residuary in nature fall within the exclusive competence of provincial legislature in terms of Article 142(c).

210. While the 1956 constitution authorized the federal legislature to legislate in respect of monopolies and competition and the same also existed under article 131(2)(c) of the 1962 constitution no similar authorization has been allowed in terms of the 1973 constitution. The Act is ultra vires of the legislative power of the federal legislature and is liable to be declared as such.

211. The Act purports to bestow the judicial power of the state of Pakistan on the Commission as it has been allowed to adjudicate regarding rights and obligations of the parties under the Act. It is an integral principle of the Constitution that the judicial power of the state can only be exercised by a properly constituted court. In seeking to provide Judicial power to the Commission the Act has violated the constitutional principle of separation and independence of judiciary. The members

of the Commission are to be appointed by the Federal Government and are not independent as required by the constitution.

212. The Act is also ultra vires of the Constitution as it does not provide a certain, consistent and reliable method of determining the course of action available to a party in any given situation. As provided by various Judgments of the Superior Courts, this is a violation of fundamental rights enshrined in the Constitution as well as Article 10-A. It is absurd that based on the whim of the Chairperson an undertaking can either have two or three appeals arising out of the same matter. If the hearing on an SCN is conducted by one member, then the undertaking is entitled to three rounds of appeal. However if the hearing is conducted by two or three members, then the undertaking is entitled to only two rounds of appeal. Furthermore no rationale has been provided by the Act to explain the basis on which one right of appeal can be taken away by the Chairperson of the Commission. The discretion available to the Chairperson is at the expense of the substantive rights of an undertaking, is untenable under law and should be struck down.

213. Section 38 of the Act is also ultra vires of the Constitution as it leaves it entirely to the discretion of the Commission to either impose a penalty upto 75 million rupees or an amount not exceeding ten percent of the annual turnover of the concerned undertaking. Depending on the nature of the business the difference between the two could be astronomically large. The Act does not provide any criteria based on which one option may be preferred over another thus leaving it entirely on the whim and will of presumably the Chairperson.

214. The Act is bad in the eye of law and liable to be struck down as it does not provide a meaningful right of appeal. It is an established principle of constitution law supported by the judgment of the Honorable Supreme Court and the Honorable Lahore High Court that one appeal before an independent judicial forum is mandatory. The appeal to the appellate bench of the Commission provided for in the Act is illusory and basically an appeal from caesar to ceasar.

215. The Competition Appellate Tribunal envisaged under the Act has also been unlawfully vested with judicial power even though it fails to qualify as a Court in terms of the Constitution. This so called tribunal consists of a retired judge of the Supreme Court or a High Court along with two technical members to be appointed by the Federal Government. The setting up of the aforesaid Appellate Tribunal as an appellate court amounts to a violation of the Constitution. Since the appointments made to the tribunal are made by the executive it does not operate under the supervision and control of the relevant High Court and therefore violates article 203 of the Constitution.

216. Furthermore no security of tenure has been granted to appointees of the Appellate Tribunal rendering their independence illusory. An appointment of three years compromises requirements of independence and a meaningful appeal before an independent forum.

217. The appeal to the Supreme Court provided for in the Act is also ultra vires of the Constitution as the Federal legislature cannot expand the jurisdiction of the Supreme Court except in accordance with entry No. 55 of the Federal Legislative List. With regard to the Supreme Court the powers of the Federation are sharply curtailed and are exercisable only under the following conditions:

a. An express authorization by or under the Constitution in relation to the jurisdiction of the Supreme Court itself

b. If such authorization exists then the Federation can make a law which (a) enlarges the jurisdiction of the Supreme Court; and (b) in relation to such enlarged jurisdiction, confers supplemental powers on it.

218. In terms of the Act, an aggrieved party has either two or three rights of appeal depending on whether a decision is given by a single member or two member bench. However the Act does not lay down the criteria which govern whether a case should be heard by one or two members. It is entirely at the whim of the chairperson as to how many members hear the case thus in effect the chairman decides whether a party gets one or two rights of appeal.

219. The Act is over-broad and does not distinguish between inter-provincial and intra-provincial trade and commerce. Assuming without conceding that Entry 27 of the Federal Legislative List allows the Federation to make a law regarding inter-provincial trade and commerce it does not allow the Federation to enact a law that does not distinguish between inter and intra provincial commerce. The Act therefore impinges on provincial autonomy and is therefore a law outside the legislative competence of the parliament.

220. The fact that the Commission plays the role of judge, jury and executioner by issuing SCNs under the Act and then sits in judgment over its own actions is clearly in violation of Article 10-A of the Constitution that guarantees due process and trial.

Intervener's Application:

221. The Farmers Associates Pakistan ("FAP") in its letter dated September 4, 2012 FAP requested the Commission to allow it to file an intervener application in accordance with the Regulation 27 of the Commission's (General Enforcement) Regulations, 2007 (the "Enforcement Regulations") in the matter of SCNs issued to Urea fertilizer producers. The aforesaid request of FAP was granted by the Commission vide its letter dated September 12, 2012.

222. FAP filed its intervention application on the 25th day of September, 2012 (the "Intervener's Application"). In the Intervener's Application, FAP requested the Commission to allow FAP to become a party to the titled proceedings as an Intervener. It made a further submission that the intervener may also be allowed to place further evidence, case-law and supplemental written submissions (including rebuttals) before the Learned Commission during the course of hearings and at any time before a final decision in the title proceedings.

223. In its written submission the FAP apprised the Commission that it represents a broad cross-section of farmers approximately 1900 hailing from all over Pakistan and that its membership is extended to them without regard to the size of their

landholdings. It therefore represents the interests of the farmers of Pakistan in general and its sizeable and diverse members' community in particular.

224. During the course of hearing parties (FFC, FFBL and DHFL) raised objection that FAP cannot be allowed to join the proceedings as an intervener whereas other parties (Engro, Agritech and Fatima) did not press this issue.

Principle Submissions of Parties With Respect To Intervener's Application: (FFBL, FFC & DHFL)

225. FFBL submitted that the Intervener's Application for intervention does not meet the criteria laid down in Regulation 27 of the Enforcement Regulations.

226. DHFL submitted that FAP did not have sufficient interest in the proceedings, and its application was liable to fail on this account.

227. FFBL further stated that if FAP has interest in the matter as it claims then why it delayed filing its application. It needs to bring in evidence in addition to that which exists along with its application failing which it does not meet regulation 27 of the Commission's Enforcement Regulations.

228. FFBL submitted that the onus lies on the Intervener to satisfy the Commission that its intervention is timely and that it has sufficient interest. The intervener is a company and not an association and does not represent farmers rather it represents the shareholders. Furthermore it is not an undertaking for not being involved in any sort of production, sales etc.

229. It also argued that in the case of Akzo Nobel vs. European Commission the court of justice found that an association seeking to promote the general and collective interest of a profession does not have the permission to intervene. FFBL also relied on the Judgment of the honorable Supreme Court of Pakistan in the PLD 1975 SC 463 case to plead that FAP should not be allowed as an Intervener based on its reasoning.

230. FFC pleaded that the main question is whether the Intervener's Application has any substance beyond the ER and whether it is frivolous.

231. FFC stated that FAP did not qualify as "consumer" of Urea Fertilizer, by virtue of the definition of "Consumer" in the Consumer Protection Act 2007, and that the Intervener's Application was *prima facie* frivolous as no new material had been submitted by FAP.

232. FFC also relied on judgments passed by Courts in Pakistan to plead that FAP cannot be allowed to join the proceedings based on the reasoning given in the cases which are (1998 CLC 678, 1996 SCMR 781, PLD 2009 Lah 57 and 2010 CLC 273).

INTERVENER'S SUBMISSIONS:

233. The Intervener made the following submissions in the hearings in response to the concerns raised by the undertakings.

a. A company limited by guarantee is a **person.** Among other things the mandate of this guarantee limited company is to advocate the views of the farmers before the GOP, to provide technical advice to the farmers, offer services to generally promote agriculture in the country etc as read from the memorandum of association.

b. The intervener stated that FAP qualifies as an 'Undertaking' and represents consumers of Urea fertilizer, and had sufficient interest to intervene.

c. The Intervener clarified that there was no bar of time limit for intervention. The intervener is bringing in the farmer's perspective and not coming in as a prosecutor, that its intervention does not prejudice FFBL in any way. In its defense of why the intervener should be entertained in the light of regulation 27 the intervener further clarified

that when the law does not set a time limit for intervention actually doing so would be prejudicial.

d. Addressing the concern that the intervener did not bring in any thing beyond the substance that exists in the ER, the intervener argued that its basic contention is unreasonable price increase and for that it needed to comment on the case laws presented by the defendants earlier. The Intervener committed to file an affidavit within a week detailing evidence to support its stance. The intervener added that it had already mentioned the factors to be looked at in evaluating the case at hand. It agitated that the Competition Law throughout the world should be sensitive to local concerns and problems. It said that it has agitated case laws and will bring in more in the future with respect to the case at hand and committed to file all that information with the commission as well as other interested parties.

234. In the affidavit submitted on 14th Day of November, 2012 and written submissions filed in reply to objections raised by the parties, the intervener made the following submissions to clarify how it meets the test for having a sufficient interest in the outcome of the instant proceedings and is therefore eligible to be made a party of it.

a. FAP qualifies as an "undertaking" for the purposes of Competition Act, 2010.

b. Relevant details of FAP's membership, spreading throughout Pakistan, have been appended with a schedule of evidences/affidavit in the titled manner.

c. Farmers' community, a broad cross-section of which section is represented by FAP, has suffered directly as a result of unreasonable price increases in the price of Urea fertilizer.

d. Various Urea fertilizer manufacturing companies, through their newspaper advertisements, have conceded the direct and sufficient

interest of farmers in matters relating to Urea fertilizer market, a body such as FAP clearly has a sufficient interest in the outcome of these proceedings – and is therefore a necessary as well as a proper party to instant proceedings.

235. The intervener offered clarification to FFBL by referring to the case of NAPP as an example where penalty was imposed for excessive pricing.

236. The intervener argued that its basic contention is unreasonable price increase and for that it needed to comment on the case laws presented by the defendants earlier. It further added that the word 'unreasonable' should be analyzed in the context of Pakistan's economy. The price dynamics of B.M.W are not the same as that of Urea.

237. The term unreasonable must also be analyzed keeping in mind historical trends. Urea sector was regulated to make Urea available to consumers at reasonable rates. Fertilizer policy must also not be ignored whose purpose is to ensure that food prices do not go up.

238. Anti-trust or Competition Law represents the economy in which it exists. When any undertakings says that in U.S prices are not regulated they are incorrect as government to this day intervenes in keeping the fertilizer prices in check.

239. With regard to the Price Control Act, 1977 it may be in place but there is no rule that two laws cannot deal with a similar matter. These industries did not come up competitively but were rather nurtured by the GOP with the mindset that Agriculture is important to the country's economy.

240. It is not ideal for competition agencies to enter the realm of 'Price Regulation', but there are numerous cases where competition agencies did look into excessive pricing particularly in the UK. Competition Agencies wait for the sector regulators to act first, however if one party is not providing remedy it can be sought from the other party.

241. Our suggested remedy for the problem is that the Commission should cap the Urea prices in whatever reasonable form or way possible. In an earlier order

regarding a merger, the case was taken to the Supreme Court but was referred back to the Commission as Section 3 gives it the mandate to deal with this subject. A competition agency can set a cap because a cap does not tell you what a reasonable price is rather it gives a certain band of what reasonable is. Competition agencies throughout the world set caps. People have been going out of food business lately. Urea prices are very closely linked to the food security situation in the country.

Intervener's submission on case laws presented by the undertakings.

The intervener made the following submissions with respect to the case laws relied by the Urea manufacturers:

242. Referring to the **United Brands** Case, the European Commission had expressly recognized that it can order price reduction. The European Court of Justice in its judgment only said that the Commission's assessment of costs was improper; it never disputed the European Commission's authority to order price reduction.

243. Looking at the two pronged test, the fundamental criteria takes into account the profit margin and on satisfying this condition it is to be determined whether the price is unreasonable in itself or against competing products. The question of competing products does not arise here and the question of whether the price is unreasonable in itself with considerations such as Agro-centric nature of economy is central to this case.

244. In real competition the Urea industry would not have reaped the benefits that it did. Every player so conveniently raised prices. If they were so hard hit by circumstances and some player/players managed to adjust their losses but even make profits, it is only possible in one of two scenarios - efficient operation gains or price increases.

245. One last submission with respect to the United Brands case is that the standard for Urea in Pakistan can not be at par with banana in Europe. The benchmark in evaluation of both has to be fundamentally different.

246. Referring to Whish's book, it is stated there that action can be taken against excessive pricing in an oligopoly. Point is that such actions are rare but it would not be unusual for the learned Commission to go that route.

247. Cases have been dealt with by OFT (UK) showing abuse of dominant position with respect to excessive pricing. One such example is the case of NAPP pharmaceuticals. Urea consumers in Pakistan are more vulnerable than consumers in those cases. Industry players are aware that Urea consumers are fundamentally dependent on them. Even if competitive pressure could be anticipated by the undertakings they would not have taken the convenient decision of increasing prices at their will.

248. With reference to the book "Economics for Competition Lawyers" cases talked about such as ATR vs British Horse Racing Board and Belgacom Telephonie and separately the Commission's handling of LSE's charging of prices to listed companies are examples where competition agencies intervened in issues pertaining to pricing. The book even argues that 'excessive' can be measured. When markets do not have a corrective mechanism, it creates a space for competition agencies to step in. In the current case the market lacks a self correcting mechanism and only a helicopter from above can fix things here.

249. Arguing for DHFL Mr. Bhandari made reference to Whish's book that lists 3 conditions for establishing Collective Dominance. He took the second condition that says 'tacit coordination must be sustained' and claimed that it implied that there should be something of the nature of an association. In my understanding the above is not necessary as the above can also be established from the fact that it is not worth the while of any manufacturer to depart from a common consideration which in this case is 'profit incentive'. No player has the incentive to undercut other players and so all of them follow price increase. Thus with the adequate deterrence in the form a long term incentive the condition that the 'situation of tacit coordination must be sustainable' seems to be fulfilled.

250. Representatives from Fauji companies adopted the stance that they can not act independent of other players in the industry in respect of pricing, It is submitted that such a stance is adopted when there are no advantages to gain from competing

with other firms. Furthermore in the cases they quoted they never mentioned any market as central as Urea is to the Pakistani economy.

251. Some of the undertakings maintain that there are no defined benchmarks to follow in setting a price. Microsoft took this plea before the District Court in the U.S. The court held that with Sherman Act in place whenever a violation takes place, an action is to be taken against it.

252. The Intervener quoted three examples from the developed economies and one instance where the Commission itself took action in a case of abuse of dominance with respect to excessive pricing.

253. In view of the foregoing we are of the considered view that the following issues arise and need to be addressed for disposal of the matter at hand.

ISSUES

a. Whether the Intervener's application could be allowed in the proceedings under Section 30 of the Act in this matter?
b. What is the relevant market?
c. In relation to alleged 'unreasonable price increase' whether each of the undertaking can be termed 'dominant'?
d. Whether the undertakings found dominant (if any), abused their dominant position through unreasonable increase in prices in violation of Section 3(3)(a) of the Act?
e. Whether the undertakings concerned exercised 'collective dominance' in relation to the alleged violation?

As for the constitutional objections the Commission reiterates the view taken earlier in various decisions including cement order dated 27-08-2009 wherein, based on the principles laid down by the superior courts, it has been held that it is not for the Commission to address the objections raised as to the constitutional vires of the Act. The Commission must proceed on the assumption that the law is validly enacted unless a Court of competent jurisdiction determines otherwise.

INTERVENER'S ISSUE:

254. We have gone through the submissions made by the undertakings and before we delve into their objections regarding the admissibility of 'intervener' in these proceedings we will briefly go over the trend of interventions. Interventions are a method by which a person or undertaking not involved in the litigation as claimant or defendant may make representation and submit information/evidence or expertise and may make an effective contribution to the decision-making process.

255. Since the year 2000, there has been a noticeable increase in the number of interventions and interveners may include campaign groups, government department, the Commission for Equality and Human Rights and the business enterprises affected by the outcome of the claim.[1]

256. This has invited both critics as well as supporters. On one hand the Court's decision making may benefit from the perspective of interveners owing to different and broader legal points or additional facts but on the other hand the Courts have only begun to articulate the principles that should govern and when an intervention should or should not be allowed.[2]

257. Coming back to the objections raised by the parties, first we would like to address the issue that who can be an intervener. For that we refer to the definition of 'Intervener' which has been laid out in regulation 2(1)(j) of the Enforcement Regulations and is being reproduced below for sake of ease

> *"Intervener means any person or undertaking permitted to intervene by the Commission in any proceedings under these regulations"*

258. The definition clearly spells out that an intervener could be either a **person or an undertaking** to be allowed intervention in any proceedings under the Enforcement Regulations. There is no prerequisite of being an undertaking to be allowed to join the proceedings as an intervener. We are of the considered view that FAP is a Company limited by guarantee and therefore a **legal person.** Since

[1] De Smith's Judicial Review, Sixth Edition, London Sweet & Maxwell 2007, page 99, citing Sir Henry Brooke, "Interventions in the Court of Appeal" [2007] P.L. 401.
[2] *Ibid*

it is established that FAP is a legal person we do not need to go into the discussion of whether it is an undertaking or not.

259. Further the major objection raised by the parties was that FAP did not meet the criteria of having sufficient interest set out under Regulation 27 of the Enforcement Regulations. Subsection 1 of regulation 27 of the Enforcement Regulations states that:

> *"Any person may be permitted to intervene and participate, subject to the conditions noted hereunder or as the Commission may deem appropriate, in any proceeding if such person satisfies the Commission that such person has sufficient interest in the outcome of the proceedings."*

260. The Regulation clearly lays out that the Commission may allow any **person** to intervene in any proceedings as per its own discretion as long as the intervener is able to satisfy the Commission that it has **sufficient interest** in the proceedings.

261. Also we deem it relevant to refer to the concept of 'sufficient interest' as has been has been summarized in the context of locus standi in the case of Ardeshir Cowasjee Vs. Karachi Building Control Authority (1995 SCMR 2883). The Supreme Court in this case held:

> *"The sufficient interest has to receive a generous interpretation. It has to be treated as a broad and flexible test.*
> *If the applicant has a special expertise in the subject matter of the application that will be a factor establishing sufficient interest. This applies whether the applicant is an individual or association. The fact that the applicant's responsibility in relation to the subject of the application is recognized by statute is a strong indication of sufficient interest.*
> *A variety of factors are capable of qualifying as sufficient interest. They are not confined to property, financial other legal interest. They can include civic (community) environmental and cultural interest. The interest can be future or contingent."*
> *The gravity of issue which is the subject of the application is a factor taken into account in determining the outcome of question of standing. The more serious the issue at stake the less significance will be attached to arguments based on the applicant's alleged lack of standing.*

In deciding what, if any, remedy granted as a matter of discretion, the Court will take into account the extent of applicant's interest.

262. FAP is a not for profit company whose main objective as stated on its website is to help the socially, economically and technologically backward areas of the agrarian sector of Pakistan to catch up with modern times. As stated in its memorandum of association, the mandate of FAP among other things is to advocate the views of the farmers before the GOP, to provide technical advice to the farmers and to offer services to generally promote agriculture. The non-profit orientation of FAP, its mandate and its stated objective to bring about advancement in the agriculture sector shows that FAP's primary interest is the advancement of agriculture in Pakistan which ultimately translates into the welfare of the farmers.

263. Furthermore FAP has a huge and diverse member base of farmers in terms of their place of origin as well as the size of their landholdings in Pakistan. Owing to this diversity in membership, FAP represents the farmers of the entire country and due to this it is only natural that it would have sufficient interest in their well being.

264. Last but not the least Urea is a major input in agriculture and its prices have far reaching impact on the utility that a farmer draws from cultivation. The Bench is of the view that FAP represents a large and diverse group of farmers in Pakistan and therefore has sufficient interest in the outcome of these proceedings. Thus objection of parties that FAP does not meet the criteria of intervener given under Regulation 27 of the Enforcement Regulations is baseless.

265. FFBL has relied upon the judgment in the case of Akzo Nobel Chemicals Ltd and Akcros Chemicals Ltd Vs. Commission of the European Communities Case (T-253/03) (hereinafter referred to as the "AKZO Case") and submitted that the Court of First Instance found that an association seeking to promote the general and collective interest of a profession does not have the permission to intervene[3].

[3] Order of the resident of the First Chamber of Court of First Instance in Case T-253/03 *Akzo Nobel Chemicals and Akcros Chemicals* v *Commission* [2004] ECR II-1603, paragraph 20, rejecting the application for leave to intervene by the Section on Business Law of the International Bar Association, paragraph 20.

266. We believe that before jumping to the conclusion on admissibility of Intervener in the afore mentioned case it would be relevant to refer to the facts of the case and the findings of the Order of the President of the First Chamber of the Court of First Instance particularly in the matter of leave to innerve filed by International Bar Association in this case.

267. In the case of AKZO, during the course of on-spot investigation, the European Commission officials took copies of few documents which were claimed to be covered by legal professional privilege (LPP) by the officials of undertaking. Later on, the European Commission refused the request to treat those documents as confidential and gave decision that these documents are not covered by LLP and added them to the file without placing them in a separate sealed envelope. Such decision of the European Commission was challenged before the Court of First Instance.

268. As AKZO case raised fundamental issues regarding the principle of legal professional privileges, therefore, the Council of Bars and Law Societies of the European Union ('CCBE'), the Algemene Raad van de Nederlandse Orde van Advocaten ('the Netherlands Bar'), the European Company Lawyers Association ('ECLA'), the American Corporate Counsel Association ('ACCA') – European Chapter and International Bar Association ('IBA') applied for leave to intervene and were granted the permission. However, application to intervene filed by the Section on Business Law of the International Bar Association was rejected as that was merely a representation, not protection of interest.

269. The Court while deciding the issue of admissibility of Intervener applied the principle laid down under the Statute of the Court of Justice, Arts 40, second Para., and 53, first Para and held that:

> *the right to intervene in cases submitted to the Court of First Instance is open not only to the Member States and institutions of the Communities, but also to any other person establishing an interest in the result of the case.*
> *Representative associations whose object is to protect their members in cases raising questions of principle liable to affect those members are allowed to intervene. More particularly, an association may be granted leave to intervene in a case if it*

> *represents an appreciable number of operators active in the sector concerned, its objects include that of protecting its members' interests, the case may raise questions of principle affecting the functioning of the sector concerned and the interests of its members may therefore be affected to an appreciable extent by the judgment to be given.*

In fact the Principle laid down in the AKZO is akin to the test provided under Regulation 27 of the Enforcement Regulations to allow an application for intervention by the Commission. In view of criteria given in the Regulation 27 of the Enforcement Regulations which finds support even from the judgment of the Court of First Instance in the case of AKZO, we are of the considered view that FAP satisfies the conditions essential to be intervener:

270. We would also like to refer to case of Smuck v. Hobson[4] presented before the Bench by the counsel of FAP which gives a comprehensive picture of how the issue of intervention is tackled in the U.S. Law.

271. The case primarily relied on a three pronged test to determine whether a party was fit for intervention. Followings are the conditions to meet the test of intervener which have similar rationale of 'sufficient interest' as discussed in preceding paras:

    a. Having an 'interest' in the transaction challenged before the Court;

    b. Disposition of the action might impair the applicants' ability to protect their interests if they were not allowed to intervene; and

    c. Lastly interests of intervener cannot be represented adequately by others.

272. Initially a class action was brought on behalf of black and poor children in the case of Hobson v. Hansen. The District Court found that the plaintiffs were denied their constitutional rights to equal opportunities since the District of Columbia schools operated on a racially and economically discriminatory basis.

[4] U.S Court of Appeals, District of Columbia Circuit, 1969. 132 US App. DC 372, 408 F. 2d 175.

273. The Board of Education voted not to appeal against this decision but Dr. Carl Hansen, the Superintendent of Schools and Carl Smuck, one of the dissenting Board members filed notices of appeal before the Court of Appeal. In addition Dr. Hansen and twenty parents who did not agree with the decision of the District Court made motions to intervene in the proceedings. The Court of Appeal held:

> *"Dr Hansen thus has no "interest relating to the property or transaction which is the subject of the action" sufficient for Rule 24(a), and intervention is therefore unwarranted.*[5]*"*

With regard to the intervention of parents a more comprehensive approach was adopted by the Court. It was the court's view that:

> *Need for an "interest" in the controversy should or can be read out of the rule. But the requirement should be viewed as a prerequisite rather than relied upon as a determinative criteria for intervention. If barrier are needed to limit extension of the right to intervene, the criteria of practical harm to the applicant and the adequacy of representation by others are better to the task……..Both courts and legislatures have recognized the concern for their children's welfare which the parents here seek to protect by intervention……..We conclude that the interests asserted by the interveners are sufficient to justify an examination of whether the two remaining requirements for intervention are met.*[6]
>
> The Court of Appeal further held:
>
> *The nature of the action may impair the applicants' ability to protect their interests if they were not allowed to intervene…….the remaining element for intervention is that the applicant not be adequately represented by others.*[7]

With regard to the objection of parties that FAP's intervention has not been timely we would like to clarify that the law does not provide any bar in this regard and in any case we note that the SCNs were issued on June 25, 2012 while the Intervener requested the Commission to file for Intervention in the matter vide its letter dated September 4, 2012. Till that time only two of the six hearings were concluded the last one being held on December 21, 2012 even the case of delay does not hold merit.

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[5] American Casebook Series, Civil Procedure, Case and Materials, Tenth Edition, page 735.
[6] Ibid, page 736
[7] *Id*, page 737

274. In view of foregoing we do not see any reason that why FAP should not be allowed to become an intervener in this case, hence objections raised by the parties regarding the admissibility of intervener are not found tenable.

RELEVANT MARKET:

275. As per the Act a relevant market is defined under section 2(1)(k) as follows:

> " 'relevant market' means the market which shall be determined by the Commission with reference to a product market and a geographic market and a product market comprises of all those products or services which are regarded as interchangeable or substitutable by the consumers by reason of the products' characteristics, prices and intended uses. A geographic market comprises the area in which the undertakings concerned are involved in the supply of products or services and in which the conditions of competition are sufficiently homogenous and which can be distinguished from neighboring geographic areas because, in particular, the conditions of competition are appreciably different in those areas;"

276. The ER defines the relevant market as follows:

> *The Commission in its earlier order dated July 23, 2010[8] in the matter of SCNs issued to M/s. ENGRO Chemicals Pakistan Limited, M/s. Fauji Fertilizer Company Limited and M/s. Dawood Hercules Chemical Limited with reference to the "Tie in of Urea Sales with DAP" held that Urea Fertilizer is a distinct product market with respect to products characteristics, prices and intended uses and is not interchangeable or substitutable with any other nitrogen fertilizer such as Calcium Amonium Nitrate (CAN). Therefore, for the purpose of this enquiry the relevant product market is the market of Urea fertilizer.*

As for the relevant 'geographic market' as observed in the earlier referred Order,

[8] http://www.cc.gov.pk/images/Downloads/fertilizer_order_final_draft.pdf

> Relevant geographic market *consists of all the areas where there are homogenous conditions of competition. Two areas are said to have homogenous conditions of competition as long as regulation, availability and pricing of the product in the two areas is such that consumers from region A can buy the product from region B, and vice versa, without incurring significant differences in price. As per the order of the Commission, nothing was brought on record to indicate that the product supplied to all four provinces have any significant price differential, in particular by EFL and FFC who have presence in all four provinces.*
> *Also, the factors: that Pakistan's economy is heavily dependent on agriculture, the use of the product remains the same, the price of Urea Fertilizer is less likely to be substantially different from one area to the other and that no barriers exists on the movement or transportation of the product, strengthen and support that the relevant geographic market is the whole of Pakistan and the relevant market as defined under the Act for the purpose of this case is also the Urea fertilizer market in Pakistan.*

277. We find merit in the reliance being placed on the earlier Order to the extent of this aspect as no appeal was filed against such finding and it has attained finality. No new or significant ground has been brought forward for Commission's deliberation in this regard. However, we consider it appropriate to deliberate further on the objection reiterated by the manufacturers that the relevant market should not just constitute locally manufactured Urea as determined in the ER but it should also take the imports by GOP into account.

278. In this regard, having examined the GOP's role in the import of Urea it is evident that GOP's role is not that of commercial entity competing with the manufacturers with the aim and purpose of making profits in the market. Unlike the manufacturers it is actually making Urea available at its own cost rather than making any money out of it. Furthermore, in doing so GOP has no intention of gaining greater market share at the expense of Urea manufacturers and is hesitant while importing Urea as it offers subsidy on its distribution to make it available at affordable prices in terms of GOP's fertilizer policy. In fact through fertilizer policy 2001 the GOP encourages investment to make Pakistan more self sufficient in its Urea needs. In fact GOP only imports Urea to fulfill a shortage in the market and we note that in some of the replies to the show case notice the undertakings have complained about the GOP not making timely imports and mentioned appealing to the GOP to do so.

279. In view of the foregoing, we are of the considered view that the GOP as an importer of Urea cannot be considered an actual competitor of Urea manufacturing units in Pakistan by any yardstick and therefore it would be incorrect to include imported Urea in the definition of relevant market.

280. Moreover, it may be relevant to add that upon review of the treatment of government entities while defining relevant market under various jurisdictions we have come across the guidelines[9] provided by Office of Fair Trading UK (OFT) that explains the criteria as to when a public body should be considered an undertaking with respect to behavior falling in the realm of anti-competitive behavior as set out in the UK and EU law.

281. As per these guidelines a 'public body' will fall within the definition of an undertaking when it carries out an 'economic activity'. In making this assessment it is the nature of a particular activity which is important rather than the legal form or the 'public' or 'private' status of a body that carries it out.

282. The guide sets out the factors that should help in determining whether a public body is acting as an undertaking with respect to a particular activity. These guidelines lay out that a conduct amounts to economic activity when the body is

a. Supplying a good or service, and
b. That supply is of a commercial nature

283. Under the guidelines exercise of certain public powers is deemed not to involve a supply of goods and services. These are activities specific to a public authority, carried out as state prerogatives or essential function of the state. We consider it pertinent to draw attention to the following paragraphs from the said guidelines.

> ***Identifying 'economic activity'***
> *2.6 Whether a particular activity carried on by a public body is treated as an economic activity necessarily depends on the specific facts at hand. For this reason, past cases may provide only limited wider guidance to public bodies seeking to apply legal precedent to their own specific circumstances. Nevertheless, the case law has set out certain broad principles that public bodies should take into account when assessing whether their own conduct amounts to economic activity.*

[9] http://www.oft.gov.uk/shared_oft/ca-and-cartels/OFT1389.pdf

2.7 In broad terms, a public body should ask itself the following questions for each of its activities separately:

• Am I offering or supplying a good or service, as opposed to, for example, exercising a public power?

• If so, is that offer or supply of a 'commercial' – rather than an exclusively 'social' – nature?

2.8 If the answer to both these questions is yes, then – ***for the purposes of that activity (and any related upstream purchasing)*** *– the public body is likely to be regarded as an undertaking subject to UK and EU competition law. Further detail on each of these elements of the assessment is set out below*.

284. Therefore, seeking guidance from the above, the government is offering or supplying Urea in exercise of its public power and not carrying out this activity as a commercial activity. It is important to appreciate that Urea being on the list of essential commodities ensuring its availability is part of the essential state function. Since agriculture sector continues to be an important segment of Pakistan's economy and agriculture generates employment opportunities for a significant percentage of the country's labour force and about 60 percent of the rural population is dependent upon this sector for its livelihood. It plays a principle role in ensuring food security, generating overall economic growth, reducing poverty and transformation towards industrialization. Hence this given background cannot be overlooked as Urea is an essential input in carrying out agricultural activities and whenever the market faces any shortage, Urea is imported by the GOP in performance of its essential function of the state. When seen in this perspective the import of Urea by the GOP and its supply in the market is not deemed to involve a supply of goods and services.

285. In sum it has been established and substantiated that import of Urea by GOP cannot be considered as part of relevant market.

INDIVIDUAL DOMINANCE OF THE UNDERTAKINGS CONCERNED:

Individual Dominance:

286. Section 2 (1) (e) of the Act defines dominant position as follows:

> *"dominant position" of one undertaking or several undertakings in a relevant market shall be deemed to exist if such undertaking or undertakings have the ability to behave in an appreciable extent independently of competitors, customers, consumers and suppliers and the*

position of an undertaking shall be presumed to be dominant if it is share of the relevant market exceeds forty percent;"

287. The ER relies on the earlier finding of the Commission that found all the players in the Urea market as dominant owing to the captive nature of the market. The relevant portion of the ER is being reproduced below for the sake of reference:

> *"the above discussion clearly indicates that the market for Urea fertilizer in Pakistan is a captive market and all the undertakings in this relevant market have the ability to behave to an appreciable extent independent of the customers, competitors and consumers and are therefore dominant undertakings irrespective of the individual market share held by each undertaking in the relevant market in terms of Section 2 (1) (e) of the Act."*

To understand the concept of captive market first, it will be helpful to look at the following definitions of Captive market taken from different sources:

> *"a group of consumers who are obliged through lack of choice to buy a particular product, thus giving the supplier a monopoly"*[10]
>
> *"Markets where the potential consumers face a severely limited amount of competitive suppliers; their only choices are to purchase what is available or to make no purchase at all."*[11]

288. In the Urea market the total production carried out by the manufacturers lags the demand in the market. Owing to this shortage and no availability of real substitutes in the market the consumers are left with nothing but the 'take it or leave it' option. Since Urea is an essential commodity and its consumers rely on it for their livelihood they do not have the option of leaving it and end up buying it inspite of any harsh conditions imposed upon them including unreasonable price.

289. In our considered view, the Commission in its earlier order held the Urea market to be captive and found all the undertakings not withstanding their market shares as dominant. It was observed in the Order that even the undertakings having smaller market shares are able to sustain their business irrespective of increase of cost or other factors primarily because of the captive nature of Urea fertilizer market, however in our view it is important to distinguish that the previous matter related to the alleged practice of "Tie-Ins" where the captive market was

[10] http://www.thefreedictionary.com/captive+market
[11] http://thelawdictionary.org/captive-market/

determined broadly to establish the dominant position of the undertakings in relation to the alleged violation under section 3(2)(c) of the Act i.e. 'tie-in'. Since the allegation in the ER is of 'unreasonable price increase' dominance here, may require consideration of certain aspects in the context of 'unreasonable price increase', instead to the broad reliance on 'captive market' as held in the previous Order and we would, therefore, look into the ability of the undertakings to behave to an appreciable extent independently of competitors, customers, consumers and suppliers as also alleged in the ER and SCN.

290. The Commission discussed the definition of Section 2 (1) (e) in one of its earlier orders pertaining to Karachi Stock Exchange (Guarantee) Limited in the matter of abuse of dominance where it interpreted that section 2 (1) (e) has two parts. The first part of the provision relates to the deeming clause where a dominant position of an undertaking can only be deemed to exist if upon analysis of pertinent factors it is found that an undertaking can behave independently of its competitors, consumers etc to an appreciable extent.

291. The second part of the provision provides that if an undertaking's share of the relevant market exceeds 40%, it shall be presumed to have a 'dominant position'.

292. In applying section 2(1)(e) we need to examine the situation of each of the undertakings in the relevant market to assess whether the undertaking was in a position to behave independent of its competitors, customers (who in this case are dealers), consumers (who are in fact farmers) and could independently set prices having market power to sustain price above competitive levels to indulge in the alleged practice of unreasonable price increases as alleged in the ER and SCN. As for the aspect related to independent of suppliers, the same is not applicable because of the absence of an upstream market.

293. A more comprehensive test is provided for determining dominance in EU which was relied upon by FFC during the hearing. We note that it has some of the overlapping considerations as envisaged under our law. As per this test in EU, the following criteria is laid down

a. position of competitors- this is similar to ability to act independent of competitors to an appreciable extent under the Act.
b. Threats of future expansion for entry is an additional factor provided in the EU law to deal with potential competitors
c. Counter veiling buying power is similar to the requirement of having the ability to act independently from consumers and customers under the Act.

In its guidelines, OFT also primarily considers restraints arising out of existing and potential competition and any countervailing buyer power to determine the dominance of an undertaking in a market.

Before applying the above, for assessing whether the undertakings are dominant we consider it appropriate to deliberate on the following objections raised with respect to the 'concept' of captive market.

294. As per DHFL's Submission the market of Urea cannot be termed as captive due to the data given in the ER itself. The tables in the ER reveal that there were substantial opening inventories during Rabi 2010-11 and Kharif 2011 thus implying a surfeit of Urea in the market. A similar concern is raised by PAFL that maintains that since GOP is also a supplier of Urea and does that at comparable rates Urea is never short in the market in fact there are unsold inventories at the end of a season.

295. In this regard one thing is settled that the supply of Urea available as a result of imports is not a permanent feature. As admitted by FFC and some of the other undertakings, GOP is intimated time and again to carry out timely imports. The GOP only imports to cover for any estimated shortage in the market. An examination of the following tables reveal that if the GOP did not carry out imports there would be no inventories left at the end of a season. The decreasing trend in inventories during a season also reveals that whatever inventories left over in one season are sold in the next season and similarly the cycle of GOP imports is repeated again when the production and available inventories are found to be insufficient to cater to the existing demand. Imports correspond to estimated shortage and do not exist at all times which gives a monopoly power to the

undertakings in respect of selling their product. Therefore, these grounds do not seem relevant.

Table 1

Urea supply/demand during Rabbi 2010-11							
							('000 tonnes)
Description	**October**	**November**	**December**	**January**	**February**	**March**	**Total**
Opening Inventory	774	781	350	166	115	53	774
Imported Supplies	-	-		-	-	148	148
Domestic Production	430	453	433	342	351	379	2389
Total Availability	1205	1234	783	508	466	580	3311
Offtake	427	879	626	394	413	421	3160
Adjustment (+/-)	4	-5	9	-	-	-2	6
Estimated Balance	781	350	166	115	53	157	157
Source: NFDC							

Table 2

Urea supply/demand during Kahriff 2010-11							
							('000 tonnes)
Description	**April***	**May***	**June***	**July***	**August***	**September****	**Total**
Opening Inventory	163	120	89	73	76	101	163
Imported Supplies	89	4	-	52	82	117	344
Domestic Production	360	445	477	438	484	472	2676
Total Availability	612	569	566	563	642	690	3183
Offtake	487	473	494	482	556	524	3016
Write off/on	-5	-7	-	-5	15	-3	-5
Estimated Inventory	120	89	73	76	101	163	163
***Actuals**							
Source: NFDC							

FFC:

296. From the financial accounts of FFC that it shared with the Bench, its share in the relevant market in terms of production comes out to 48% in 2011. Thus by mere virtue of having a market share above 40% the Bench finds FFC to be falling in the purview of legal presumption of having a dominant position in the relevant market.

297. Even if one was to go beyond the test of a market share threshold, the first component of the deeming provision is independence from competitors to an appreciable extent. Corresponding to this is the first component of EU's test regarding restraints arising out of competing undertakings (market position of competitors).

298. To argue that it does face competitive pressure, FFC maintains that it is a mere price follower and when EFL which is the price leader, raises price, FFC has to follow suit. When considering that FFC has undeniably a leading share in the market in terms of its production and importantly greater than EFL which has been initiating the price increases and whom FFC purports to have been following, this argument does not seem to hold weight. In this regard, the following definition of 'price leadership' would provide further help in clarifying the concept.

> *When a firm that is the leader in its sector determines the price of goods or services. Price leadership can leave the leader's rivals with little choice but to follow its lead and match these prices if they are to hold onto their market share. Alternatively competitors may also choose to lower their prices in the hope of gaining market share as discounters.*[12]

299. This definition emphasizes that undertakings follow the lead of price leader with respect to pricing in order to hold on to their market shares. It is further elaborated that markets where price changes carried out by the market leader have to be followed by competitors with lesser market power are those where not doing so has the potential to ignite a price war. In such price wars the undisputed market leaders who have significant advantage over their competitors in terms of economies of scale relentlessly employ operational efficiencies to significantly cut

[12] http://www.investopedia.com/terms/p/price-leadership.asp#ixzz2BzLaVOHt

down their prices which force their rivals to absorb heavy losses and some may even be forced to exit if this trend continues. To avoid this scenario firms have no option but to follow the market leader. In our considered view, no such predicament existed for FFC.

300. All the Urea produced in totality in Pakistan whether by FFC or any other manufacturing concern is completely in demand in the country as customers of Urea are those farmers whose livelihood depends on agriculture and their demand exceeds the production in the country. Thus it is beyond question that by driving down its prices any of the competitors can steal away from the market share of other operating concerns. In this regard FFC is no different. However, FFC's current market share is under no threat by price maneuverings of its competitors and when seen in the right context it certainly had no pressure to be a 'price follower'; rather it chose to do so in exercise of its discretion .

301. In our considered view, the particular nature of the relevant market puts some of the manufacturers in command with respect to their ability to increase price at will without the threat of any present or potential counter competitive measures. If EFL with a market share of only 26% has the ability to initiate price changes in the relevant market, FFC with a much higher market share would certainly have the clout to influence the price change whether it initiates or follows. It is therefore, considered view of the bench that FFC holds a dominant position independent of its competitors to an appreciable extent.

302. It needs to be emphasized that the first limb of the test i.e. ability to act independent of competitors, is very critical as it highlights the aspect of the undertaking having market power; which is of material significance in relation to 'price increases' The term market power is defined as under.

> *A company's ability to manipulate price by influencing an item's supply, demand or both. A company with market power would be able to affect price to its benefit. Firms with market power are said to be "price makers" as they are able to set the price for an item while maintaining market share.*

Generally, market power refers to the amount of influence that a firm has on the industry in which it operates. (emphasis added)[13]

303. FFC's argument that it faces competitive pressure from the GOP is also misplaced. As observed above, it is reiterated that the GOP imports Urea to cater to its shortage in the market. Unlike the undertakings the GOP has no financial gains to make from this transaction, in fact it is always burdened to make these imports owing to the huge costs it incurs against them. In this regard we draw attention to the following news item.

> *"Committee's meeting remained indecisive with regard to taking a decision on import of Urea and decided to summon the representatives of fertilizer plants on Thursday (today) to hear their viewpoints … According to sources the fertilizer plants will be asked as to how much gas they would need to manufacture 0. 3 millions tons of Urea for Rabi season so that the government is not compelled to import it…. The ECC was informed on October 3 that about 2.745 million tons of fertilizer, including already allowed import of 300,000 tons, would be available for the Rabi 2012-13 crop against an estimated demand of 3.052 million tons and there would be a shortfall of 307,000 tons"*[14]

304. Since GOP purely imports in the context of fulfilling demand that is expected to be unmet through local supply we are not convinced that these imports would exert any competitive pressure on the existing supplies. FFC's submission in this regard is contradicted by none other than FFC's own submissions that Government has to be intimated time and again to make timely imports. It begs the question that if the GOP imports have the effect of exerting a so called competitive pressure on FFC and hurt its interests why would it be so bent upon reminding the GOP to carry it out in a timely manner.

305. Specifically in regard to the submission of some of the undertakings that the imports carried out by GOP in 2012 exerted pressure on prices, the Bench is of the considered view that such an occurrence was more of an exception than the norm

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14 http://www.brecorder.com/top-news/1-front-top-news/87971-plan-to-import-300000-tons-of-Urea-govt-to-hear-fertilizer-sectors-point-of-view-.html

as its parallel does not exist in the past nor has the GOP shown any such intention afterwards, particularly as highlighted in the newspaper excerpt above.

306. From the foregoing the main point that emerges is that the imports carried out by the GOP are geared toward meeting an essential need and not to exert any competitive pressure and that if due to miscalculation of need the Government has made imports in access it is a unique rather than a usual phenomenon. The GOP faces huge costs in importing Urea and offering it at subsidy and it has no interest in importing a minimum unit more of Urea than is absolutely necessary. Thus based on an isolated incident it cannot be concluded by FFC or any other undertakings that it faces competitive pressure due to GOP imports.

307. The second criterion of the test taken from EU pertains to measuring the strength of an undertaking with respect to any potential competitive constraint coming from its existing competitors or potential entrants in the market. This however, is not a requirement under the Act. However, we have examined this aspect for the purposes of clarity only. This essentially entails assessing the strength of an undertaking considering any threat or possibility of future expansion or entry in the market.

308. It is quite evident that in the given period the barriers to entry remained huge in the Urea industry considering the scarce supply of raw material i.e. natural gas and keeping in view the current scenario FFC do not face any potent threat of any potential entrants in the market. With the gas supply so limited there is also no possibility that the existing players would expand, who were in any case not producing to their full capacity. Lastly the Urea industry is a capital intensive industry with the requirement of huge upfront costs. In view of the above, it is our considered view that FFC does not face any threat of future expansion or entry in the relevant market.

309. The last limb of the test employed by the deeming provision of Section 2(1)(e) is whether an undertaking is independent of its consumers to an appreciable extent. This also corresponds to the third and last criteria of the test taken from EU that assesses the threat of an undertaking while considering the negotiating power of the buyers in a particular market.

310. As discussed earlier the primary consumers of Urea are the farmers. According to a world bank report last published in 2012 the population of Pakistan that resides in villages is 63% of the total population[15]. Of the rural population 60% rely directly on agriculture for their livelihood[16]. Urea is a primary input in agriculture and it does not have a substitute in the real sense both in terms of price as well as characteristics as established in one of the earlier orders[17] of the Commission (regarding abuse of dominance by Urea fertilizers). Production figures from the accounts of manufacturers reveal that approximately 5 million tons of Urea was produced in the year 2011. As against this NDFC figures reveal that in the 2010-11 period the Urea offtake was approximately 6.2 million tons. With demand exceeding production by such a considerable margin and the livelihood of almost 38 % Pakistanis depending on agriculture it is evident that these consumers completely rely on all Urea that is produced by the manufacturers plus additional to fulfill their needs. These consumers do not have the option to switch to another fertilizer which would cater to their needs in the same way or do without any fertilizer as it is a required input in agriculture. This puts the consumers of Urea at a very weak bargaining position. Their situation does not afford them the strength to fully protect their rights against the onslaught of raising prices or other such activities in the prevailing situation. In view of the above, we are of the considered view that that the customer or consumers in the relevant market are at a very weak bargaining and in no position to offer any constraint to FFC.

311. Having established the criteria laid down in the deeming provision of Section 2(1)(e) along with a very similar test taken from EU, the bench is of the considered view that independent of the presumption test based on market share under section 2(1)(e) even deeming test factors are satisfied in establishing FFC's dominant position in the relevant market.

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[15] http://www.tradingeconomics.com/pakistan/rural-population-percent-of-total-population-wb-data.html

[16] http://www.finance.gov.pk/survey/chapter_12/02-Agriculture.pdf

[17] http://www.cc.gov.pk/images/Downloads/fertilizer_order_final_draft.pdf

FFBL:

The major contention of FFBL is that it cannot be deemed to be dominant with a market share of less than 10% in terms of its production. As we agree that FFBL would not fall in the legal presumption category, we, therefore, proceed to apply the test laid down in the Act along with additional factor of 'threat of future expansion and entry' under EU law to the case of FFBL and would do so for other undertakings only for purpose of clarity.

312. We'll address each of these parameters in establishing whether FFBL is a dominant Entity.

313. In order to convince the bench that FFBL is not independent of its competitors it argues that FFBL is a mere price follower and has no option but to follow when the market leader raises its price. We would like to examine it from the point whether FFBL enjoys the market power to initiate, influence or exercise price increase independent of its competitors. Despite the fact that FFBL is a subsidiary of FFC and FFC owns a 51% stake in this company in addition to the 17% owned by Fauji Foundation. Also the fact that the Chairman, Chief Executive officer and three other members of the Board of Directors ('BOD') of FFC are also members of the BOD of FFBL. With management shared to this extent at the highest level, a completely independent decision making process without regard to the other's interest seems unlikely especially when the CEO has the authority to make the most important management decisions including those related to pricing.

314. The purpose of management of a company is to maximize the shareholders' wealth. With the directorates of the two companies linked the chief executive officers represented on each others board it does not take much of thinking that the economic interests of the two companies are intertwined.

315. FFBL also uses the marketing and distribution network of FFC. Since marketing and distribution is a purely management function and there is the aspect of synergies and cost effectiveness in having one network, the notion that FFBL and FFC have economic interests that are intertwined is further strengthened.

316. Lastly FFBL uses the brand name of FFC “Sona Urea" to sell its products[18]. Brand name is the identity of a product. It is the brand name that differentiates product of one manufacturer from the other. In this case it is the same for both. This implies that all the efforts that are geared toward the sale of Urea in the market are the same for FFC and FFBL. Clearly the relationship is not just limited to the directorate as having a common brand goes much farther than that.

317. With this level of interconnection the power that FFBL projects in the relevant market should not just be seen in respect of its market share. However, in the light of the fact that the association between the two undertakings has not been duly covered in the ER or SCN, we would not be able to establish dominance individually or collectively with FFC on this basis. Other factors i.e. barriers to entry and expansion and countervailing buyer power even though present would not make FFBL a dominant player enjoying market power that confers ability to increase prices independent of its competitors in the given facts on record.

EFL:

318. EFL has neither denied dominance, nor contested ‘captive market’. EFL has submitted that EFL(or perhaps the entire industry) is not necessarily always in a dominant position, in fact in 2012 the EFL was forced to reduce its price, even though it was in extremely dire financial state, because of the Urea imports by GOP had flooded the market and it’s sale had almost stopped. EFL accepts that during late 2010 and 2011 it was the ‘price leader’ and took the initiative to increase prices because it was the most effected and vulnerable of all the Urea producers having invested over USD$1.1 Billion in a new fertilizer plant and seeing massive gas curtailment on that plant.

319. Further, in its written response to the SCN and during the case of hearings EFL maintained that the market for Urea is competitive, which is the reason why it has been currently unable to increase prices despite financial losses. It asserted that the competition comes from not just competing manufacturers but also GOP imports carried out to fill the demand-supply gap in the market. EFL admits that the competitive pressure from GOP was not felt in 2011 but came in the form of

[18] http://www.pakinvestorsguide.com/index.php?topic=151.45

imports in 2012. Due to improved availability of Urea on account of imports in 2012 EFL had to reduce its price by PKR 145/bag despite a weak financial position. Even the GOP had to increase the price of Urea from PKR 1300/bag in 1Q 2012 to PKR 1600/bag as the middleman was taking advantage and selling it for PKR 1500-1550/bag in the market. Due to the fact that Urea is a commodity its price equalizes in the market despite varying profits and cost/bag among manufacturers. Owing to the above factors EFL argues that it can not always act independent of its competitors, customers and consumers.

320. In arguing that EFL cannot always act independent of its competitors etc, it has only been able to present the case where GOP imports in 2012 catering to the shortage in the market were able to exert enough pressure on EFL that it had to reduce its price by PKR 145/bag despite a weak financial position.

321. As established in detail earlier, GOP is not a competitor. As EFL itself admits, GOP imports to fill the demand-supply gap. Due to huge costs of importing GOP is the most unwilling participant, however keeping in mind the local concerns the GOP has to carry out this task in order to satisfy a purely social need.

322. If we look at the relevant period running from December 2010 to December 2011, EFL was able to increase the price of Urea at will. It never felt at threat of losing its market share or any other commercial advantage despite the fact that one of the other manufacturers had a much larger market share than EFL in terms of production. In this period EFL also faced no pressure to reduce its price owing to pressure of GOP imports. GOP imports as also highlighted in most of the manufacturers' responses has not been timely owing to which the dynamics of a 'captive market' completely kick in, leaving the consumers at the mercy of manufacturers who were able to increase their price of Urea bag from PKR 830/bag to PKR 1580/bag at the detriment of the consumers without any deterrence from any of the competitors or the GOP as alleged. If at all any one was helpless in this situation it was the poor farmers who had no option but to buy Urea at whatever price available in order to cultivate land and earn their livelihood.

323. Owing to this not just the pressure from fellow manufacturers was absent but even the consumers had no bargaining power as they did not have the luxury to switch to any other substitutes or give up Urea. Even if in 2012 the GOP imports did exert some pressure it was a one of its kind instance as explained in detail earlier. GOP's imports have always been need based and never before one finds any instance of such pressure resulting from GOP's imports including the relevant period. It is important to highlight that historically the fertilizer producers have not been able to meet the demand and every year the government has to divert to imports to fill in the demand gap. Government imports were therefore, not a new phenomenon for this market to exert competitive pressure and push up the prices.

324. It is clear that EFL did not feel any competitive pressure from any of its competitors as it was the initiator of price increases during the relevant period. It commands enough market share to compel the market to move in its direction without feeling a counter pressure from other undertakings throughout the relevant period. Therefore, we have no doubt in holding that EFL had the market power which was demonstrated during the period by initiating and leading the price increase.

325. The **countervailing power of the consumers** is almost non-existent in the relevant market as detailed earlier. In light of the above the Bench finds EFL to have satisfied all the conditions pertaining to the deeming provision of Section 2(1)(e) of the Act and hence deems it to hold dominant position in the relevant market. Even the **threat of entry and expansion** is low in the industry as explained earlier owing to huge capital costs and the prevailing circumstances.

DHFL, AGL, FFL and PAFL:

326. The market shares of DHFL, AGL, FFL and PAFL are 4%, 4.3%, 8.6% and 0.56% respectively in terms of their production in the relevant period as seen in the following table. Individually none of the undertakings exceed a market share of 9% hence the legal presumption of dominance under the Act would not apply. It is also worth noting that the combined market shares of these undertakings is even significantly less than that of EFL. However in applying the behavioral test we will look at the three conditions i.e. independence from competitors, buyer's

countervailing power and barriers to entry. As regards the factors of Countervailing buyer power and barriers to entry, these are common for all the undertakings operating in the industry. Therefore, the critical requirement in these cases that needs to be seen is the whether these undertakings had the 'market power' giving them the ability to act independent of their competitors with respect to increase in prices.

Table 3: Market Shares 2011 – Based on Actual Production

Company	Actual Production (Tons)	Market Shares
FFC	2,396,160	48%
FFBL	433,165	9%
EFL	1,279,000	26%
PAFL	28,000	1%
FFL	427,000	9%
AGL	217,000	4%
DHFL	200,000	4%
Total	**4,980,325**	**100%**

The table below shows that the total production of DHFL, FFL, PAFL and AGL combined is slightly less than the difference between the total Urea produced by FFC and EFL in 2011 and the production they could have achieved had their plants operated at their maximum capacity (assume to be 100% for all plants except FFC). The actual Urea produced by these undertakings amounts to approximately 48% of the capacity unutilized by FFC and EFL together. In our view this shows that in the situation prevailing during the relevant period, had the supply collectively made by these plants been withdrawn from the relevant market, and presumably some or all of their raw material resources diverted to other plants(mainly FFC and EFL), both, could have made up for the withdrawn supply. While this may be a hypothetical and collective scenario for these undertakings it at least substantiates that individually none of them had the market power to initiate or influence price increase. Therefore, we find merit in the argument asserted by these undertakings that they did not enjoy the market power to behave independent of competitors as alleged in the ER and SCN. In other words their

presence in the market at least individually does not impose any significant competitive restraint to affect the market power enjoyed by FFC and EFL.

Table 4: Production Analysis for 2011

Company	Production Capacity	Actual Production	Difference
	----------Tons----------		
FFC	2,490,000	2,400,000	90,000
EFL	2,275,000	1,279,000	996,000
Total <A>	**4,765,000**	**3,679,000**	**1,086,000**
PAFL	92,400	28,000	64,400
FFL	500,000	427,000	73,000
AGL	346,500	217,000	129,500
DHFL	445,500	200,000	245,500
Total <B>	**1,384,400**	**872,000**	**512,400**

327. In the context of 'unreasonable price increase' when the ability to act independent of competitors cannot be established vis-à-vis these undertakings, we do not deem it relevant to address other submissions taken by these undertakings. This is so because before the abuse is established, dominance is a pre requisite for the alleged contravention under section 3 of the Act. As for the association of DHFL and EFL which in any event appears to be less intertwined than FFC and FFBL the same, not being duly addressed in ER and SCN cannot be scrutinized and taken into consideration at this stage. In view of the foregoing, findings in relation to DHFL, FFL, PAFL and AGL holding individually a dominant position in the ER is not upheld.

328. In view of the foregoing what is left to be determined now is the principle issue about the abuse of dominant position by each of the two undertakings who are found individually dominant i.e FFC and EFL.

329. In view of the contentions of FFC and EFL before the Bench we now proceed to address this issue.

UNREASONABLE PRICE INCREASE:

330. At the outset, we would like to deal with the objection taken by the counsel of FFC and some other parties that in terms of clause 'a' of sub- section (3) of section 3 of the Act the 'unreasonable increases in price' has to be read conjunctive with the conditions of *'limiting production, sales'* as both are linked with the word 'and' in the said clause. While in view of settled principles of interpretation there is no hard and fast rule and the word 'and' has also been interpreted to mean as 'or', we consider it appropriate to refer to the concept of 'excessive pricing' in EU and other jurisdictions, which is akin to the concept of 'unreasonable price increase'; to review as to what constitutes its prerequisites. This is for the reason that in the submissions made during the course of hearing the reliance was primarily placed on this concept as understood in EU. We have no doubt that 'excessive pricing' corresponds to the term 'unreasonable price increase' under the Act. We, therefore, consider it relevant to refer as to how the term excessive pricing has been defined or interpreted in other jurisdictions.

331. The 'Organization of Economic Cooperation and Development (OECD)' defines 'Excessive Pricing' as follows:

> *Excess prices refer to prices set significantly above competitive levels as a result of monopoly or market power.*[19]

332. Excessive pricing has also been defined by the EU Court of Justice in United Brands Case[20] in the following manner:

> *"[c]harging a price which is excessive because it has no reasonable relation to the economic value of the product supplied.."*

333. While competition laws are far from being all alike, they typically have provisions prohibiting price fixing and other forms of cartels, as well as measures to tackle abuses of dominance or market power by the dominant undertakings or attempts by undertakings to monopolize markets.

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[19] OECD Glossary of Statistical Terms available at: http://stats.oecd.org/glossary/detail.asp?ID=3211

[20] Judgment of the Court of 14-02-1978, United Brands Company and United Brands Continental BV v Commission of the European Communities. - Chiquita Bananas. - Case 27/76 [ECR 1978 Page 00207]

334. Here it will be pertinent to highlight that in many competition law jurisdictions, the exploitative abuse such as 'excessive pricing' is not prohibited. Only in few jurisdictions, legally 'excessive pricing' is prohibited. Some of these jurisdictions deal with the term 'excessive pricing' as follows:

(i). **Albania**: Article 9(2)(a) of the Albanian Law on Protection of Competition identifies unfair prices as one of the main forms of abuse of dominance.[21] According to the competition authority a price is deemed unfair if it is higher than a price in a competitive market.[22]

(ii). **Brazil**: In Brazil Antitrust Law No. 8,884/94, in its Article 20 (III) and Article 21 (XXIV), considers that it is unlawful to charge excessive prices or to increase prices of goods or services in an unjustified manner.

(iii). **European Union**: Article 102(a) of the Treaty on the Functioning of the European Union (TFEU) specifies that imposing unfair purchase or selling prices or other unfair trading conditions either directly or indirectly consists in an abuse of a dominant position. The term "unfair" in turn has been considered by the European Courts and the European Commission to encompass excessive price.[23]

(iv). **Hungary**: Article 21 of the Hungarian Competition Act (similarly to TFEU 102) prohibits the abuse of a dominant position, and explicitly mentions a prohibition to set unfair selling prices. Excessive pricing comes under this heading, and therefore excessive pricing cases are investigated by the Hungarian Competition Authority.

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[21] Law No. 9121 on Protection of Competition of 28.07.2003

[22] Decision No. 59, Para 63

[23] Sirena vs. Eda [1971] ECR 69, according to Gal (2004:358) the first case where monopolistic prices without harm to competition were found abusive; Case 27/76 United Brands vs. Commission [1978] ECR 207; COMP/A 36568/D3 Scandlines Sverige AB vs. Port of Helsingborg and Sundbusserne AS vs. Port of Helsingborg [Jul 23, 2004]

(v). **Korea**: The Monopolies Regulation and Fair Trade Act defines excessive pricing broadly as an act of determining, maintaining or changing prices unreasonably by a market-dominating company.

(vi). **Pakistan**: In Pakistan, under the Act, the corresponding provision dealing with the excessive pricing is as follows:

> **3. Abuse of dominant position. —** (1) No person shall abuse dominant [24]position.
>
> (2) An abuse of dominant position shall be deemed to have been brought about, maintained or continued if it consists of practices which prevent, restrict, reduce, or distort competition in the relevant market.
>
> (3) The expression "practices" referred to in sub section (2) shall include, but are not limited to –
>
> (a) limiting production, sales and unreasonable increases in price or other unfair trading conditions;

(vii). **South Africa**: Under Section 8(a) of the South African Competition Act a dominant undertaking is prohibited from charging an "excessive price to the detriment of consumers".

(viii). **Turkey**: Act on the Protection of Competition No. 4054 (the Competition Act) sets the basic framework in terms of antitrust rules. The provisions of the Competition Act are generally compatible with Articles 101 and 102 of the Treaty on the Functioning of the EU (TFEU) and Merger Regulation of the EU as part of Turkey's aim and commitments towards becoming a member of the EU. Moreover, the principles contained in the case-law of the European Commission, General Court (former Court of First Instance) and the European Court

[24] In terms of Section 2(1)(e) of the Competition Act, "dominant position" of one undertaking or several undertakings in a relevant market shall be deemed to exist if such undertaking or undertakings have the ability to behave to an appreciable extent independently of competitors, customers, consumers and suppliers and the position of an undertaking shall be presumed to be dominant if its share of the relevant market exceeds forty percent;

of Justice are taken into account as precedent in the decisions of the Competition Board, the decision making body of the TCA.

Within this framework, Article 102(a) of the TFEU explicitly prohibits a dominant undertaking from directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions. Although the Competition Act does not overtly cite unfair prices as a form of abuse, it is considered that excessive price is a form of abuse in the decisions of the Competition Board, the decision making body of the TCA.

The review of the aforesaid provisions and the provision under Competition Act, 2010, abundantly reveals that no where 'excessive pricing' or 'unreasonable price increase' is linked with or subject to 'limiting production and sales' and that '*excessive pricing*', '*unfair pricing*', '*unreasonable increase in prices*' are in all the above jurisdictions treated and dealt with independent of any other condition or conduct.

335. In addition to the above, it is also pertinent to mention here that the conduct regarding '*limiting production or sales*' has been mentioned independent of the '*excessive pricing*' conduct.

336. It is our considered view all the cases that FFC discussed in the hearings such as that of NAPP pharmaceuticals, Scandlines vs Port of Heslsenborg or ATR ltd vs BHB are instances where the increase in price was not an outcome of limiting production or sales and yet proceedings were initiated against them. The Bench interprets it no differently. In the NAPP case the regulator and subsequent courts found it to have abused its dominant position by charging excessive prices to the community segment. Hence there is an inherent nexus between distortion of competition and price hike where the latter leads to prima facie unreasonable price increases.

337. Keeping in view the treatment of 'excessive pricing' in the competition law jurisdictions, we now draw attention to the established principles of interpretation of statutes:

338. In a judgment Khadim Hussain and another vs. The Additional District Judge, Faisalabad and others, **PLD 1990 SC 632**, the Hon ‘able Supreme Court observed as follows:

> *“From the above-cited cases and the passage from the well-known treatises on the Interpretation of Statutes, it is evident that the words "and" and "or" are interchangeable and the word "and" can be construed as "or" and vice versa if the change is necessary to effectuate The obvious intention of the law- maker or the statutory rules framer.”*

339. In the judgment of *‘Younus and 9 others vs. Pakistan State Oil Co. Ltd.’*, cited as **PLD 1988 Karachi 338**, the Hon ‘able Sindh High Court at Karachi observed as follows:

> *“…[words] ‘or’ and ‘and’ are interchangeable and much depends on the context in which these words are used and the intention with which they are used…”*

340. In the case of Vidyacharan Shuka V. Khub Chand Baghal and others (AIR 1964 SC 1099) the Supreme Court held that

> *‘And’ …..…in order that the second part might be held to be independent of the first part it should by itself be complete and be capable of operating independently.…..…*
> *Similarly it was held*[25]

341. In view of the above, there is no doubt in our mind that ‘*limiting production or sales’* independently qualify as anti competitive practices, therefore, there is no need to club it with ‘unreasonable price increase’. Each one of the practices in fact is illustrations of unfair trading conditions. Therefore, the word ‘and’ in the said context will be read as ‘or’. This view also finds support if we look at the provisions of section 4 of the Act where ‘fixing or setting the quantity of production or sales in any manner’ is independently and distinctly prohibited under clause ‘c’ sub section (2) of section 4 of the Act.

[25] AIR 1959 SC 198

342. Various Urea manufacturers in response to the SCN and in hearing have argued that the case of excessive pricing is not fit for intervention by the Commission because the EU has itself approached these cases with hesitation and where they have, it has been cases, where excessive prices amounted to an obstacle to parallel imports, left a substantial share of market unsatisfied and other such factors. In this regard it would be useful to look at the work of competition experts who have dealt with this aspect. Some of the parties also contended that it is beyond the Commission's jurisdiction to intervene in this matter arguing that as per the court's judgment in the matter of **DG Khan Cement Company Ltd vs Monopoly Control Authority (MCA)** it was held that MCA is not a price regulator and that although the powers of the Commission have been extended beyond MCA but the principle applied in the Judgment still applies to it. It also contends that in the light of that a nexus between pricing and distortion in competition must be established.

343. The Bench does not find merit in this reliance as the above cited case had distinguishing facts and does not apply to the Commission the same way as to the MCA. In DG Khan Cement case the Honorable Court observed that MCA had no basis what so ever on which it could contend that there has been a planned or systematic increase in prices and it was insufficient to simply rely on price increase itself for establishing the existence of a 'cartel'. In the aforementioned DG Khan Cement case, price of cement was fixed at PKR 60 per bag by the MCA in its impugned order and DG Cement was directed to reduce price to a level fixed by it. The Honorable Lahore High Court in its judgment held that the Monopoly Authority is not a price regulator and does not have the power to determine the prices. Importantly, unlike MCA, in the case of Commission section 3(3)(a) of the Act expressly stipulates 'unreasonable price increase by a dominant party as an abuse and thus a contravention under the Act.

344. We are cognizant of Commission's role that it is not a price regulator. It is the behavioural aspect which the Commission is entrusted to regulate. In the present case, the Commission is empowered under the Act to regulate the anti-competitive behaviour by preventing abuse of exploitative, excessive or unreasonable price increase and inclusion of such aspect in the statute is in sync with the global

trends. The ultimate goal of competition law is welfare of consumer and protecting consumers from anti competitive behavior.

345. As for the objection pertaining to the applicability of the Price Control and Prevention of Profiteering and Hoarding Act, 1977 is concerned, we believe submissions made by EFL in its reply to SCN in para 71 are quite relevant. EFL has submitted that "*while chemical fertilizer is listed as a product whose price can be regulated under the Price Control and Prevention of Profiteering and Hoarding Act, 1977, due to deregulation of the industry and the assurances in the subsequent Fertilizer Policies of 1989 and 2001, the GoP has in fact expressly agreed not to regulate the price of these fertilizer and waived its rights under the Price Control Legislation."*

346. Abovementioned submission by EFL categorically negates the stance taken by other parties that price of fertilizer is fixed under Price Control and Prevention of Profiteering and Hoarding Act, 1977. Furthermore, Competition Act, 2010 does not prohibit high price or determine a fair price but keeps a check on unreasonable increase in price as a form of an unfair trading condition imposed by a dominant undertaking, which is different from the mandate under Price Control and Prevention of Profiteering and Hoarding Act, 1977.

347. Even otherwise, if there are such provisions, the same has to be read subject to Section 59 of the Competition Act, 2010 which confers an overriding effect to the provisions of the Act. Competition Act, 2010 is a special law and Section 59 clearly states that in case any provision in any other law is inconsistent with the provisions of the Competition Act the later shall prevail. Section 59 of the Competition Act, 2010 is reproduced as below:

> ***Act to override other laws.-*** *The provisions of this Act shall have effect notwithstanding anything to the contrary in any other law for the time being in force.*

348. Moreover, without prejudice to what is observed or stated above, we note that there are also a number of instances where competition authorities in EU and UK

have intervened in matters relating to excessive pricing. In this regard it will be helpful to look at the following.

349. Dr Massimo Motta is a known competition expert on abuse of dominance. We find it useful to refer to one of his papers[26] wherein it has been discussed how an anti-trust authority should screen out cases in the decision regarding intervening in a case of alleged excessive pricing.

350. The listed proposed tests for intervention by anti-trust authorities suggested therein varied from very strict ones to as lenient as 'the mere presence of very high and long lasting barriers to entry and expansion'.

351. 'Excessive Pricing' has been discussed by experts for the following two reasons:

> *"The first one is that the European Commission is reconsidering its policy on Article 82 of the EC Treaty, and although exploitative practices have not been addressed yet in its policy documents, it is well known that the Directorate General for Competition plans to deal with them in the future Guidelines on Article 82 enforcement. "*
>
> *"The second reason is that dissatisfaction with the outcome of the liberalisation process (more particularly with the high level of prices in many recently privatised and de-regulated sectors, as for instance energy), which has taken place in Europe has led many policy-makers – both at the level of Member States and at the EU level – to call for drastic measures of intervention, including structural remedies (for instance unbundling in energy and telecommunications) and price controls."*

352. According to the paper some of the well known objections to intervention by competition authorities in cases of excessive pricing are that:

a. Excessive pricing action may undermine the investment incentives of new entrants
b. It may also undermine the investment incentives of dominant firms
c. It is extremely difficult to ascertain that the price is excessive
d. Price regulation may have a strong 'political dimension' where under the pressure of their electors the politicians may require the administration or independent anti-trust authority to regulate the prices

[26] http://www.barcelonagse.eu/tmp/pdf/motta_excessivepricing.pdf

e. Lastly that US law focuses solely on cases of exclusionary abuse and not exploitative abuses

353. Despite all the challenges associated with intervening in a case of excessive pricing, Motta discusses the biggest pro as follows:

> *"Exploitative abuse is the most direct violation of the consumers' interest that antitrust policy aims to protect and there are some exceptional circumstances where the structure of the market and the institutional design would lead to an excessive price that could only be remedied by competition law."*

354. Thus what is suggested is that competition authorities should intervene in cases of exploitative abuse but only after satisfying certain conditions. In this regard Motta suggests the following screening test in order to identify whether a firm qualifies for such intervention. These conditions are as follows:

a. High and non-transitory entry barriers leading to a super dominant position
b. The super-dominant position is due to current/past exclusive/ special rights or to un-condemned past exclusionary anticompetitive practices
c. No sector-specific regulator has jurisdiction to solve the matters

355. Without treating these conditions as a prerequisite for Commission's interference in such behavioral aspect, even if we take these conditions one by one and analyze one by one to assess how the case of prima facie unreasonable price increase/excessive pricing in the Urea fertilizer industry is fit for intervention by the Commission.

356. First thing to identify is whether there are high and non-transitory barriers leading to a super dominant position. In this regard it would be useful to look at the barriers to entry that exist in the Urea industry.

357. There is no denying of the fact that one of the foremost barriers to entry in the Urea industry is the huge capital cost that is required in establishing a Urea manufacturing plant. One such example is the new plant of EFL established with a total investment of 1.1 bn dollars and having manufacturing capacity of 1.3

Million tons of Urea. Perhaps such huge investment only suits companies who have a reasonable expectation of recovering their investments over a period of time without any significant foreseeable threats. This sector thus provides investment opportunities to only the large groups with financial muscle.

358. Gas is the primary raw material in the production of Urea and gas supply is allotted to various manufacturers based on agreements between national gas providers such as SNGPL and these individual Urea manufacturers. Despite the fact that fertilizer sector has been high on the GOP's priority list it would be practically impossible for any potential entrant to procure gas from the GOP since what is available is not even able to satisfy the needs of the existing players. Furthermore there is no remedy available with the GOP in this respect in the near future.

359. Currently the demand for Urea in the country is estimated to be around 6.3 million tons. The market has already almost reached its current potential in terms of production capacity, since the current players have a combined production capacity of approximately 6.26 million tons.

360. Thus when we look at these three factors combined it becomes clear that with the current scarcity of gas, huge capital costs and no ability of matching the incumbents' economies of scale plus the fact that a new entrant has no chance of stealing any market share from the incumbents, as Urea is a commodity with no room for differentiation and value addition there is absolutely no threat of entry in the Urea industry. This also means that incumbents are under no threat from potential entry and have the status quo secured.

361. The second condition to be satisfied is whether the super dominant position is due to current/past exclusive/special rights or to un-condemned past exclusionary anticompetitive practices.

362. This condition is aimed at eliminating the possibility that the revenues or profits enjoyed by the dominant firm/firms are a result of factors such as risky investment, operational efficiency and innovation.

363. In Motta's words

> *"This second condition is divided in two alternative tests. Under the first limb of the test, the super-dominance should be caused by current or past legal barriers and access in the market has not been granted in a fair and non discriminatory way. Those barriers may be due to the scarcity of indispensable resources (like spectrum for mobile telephony services), to natural monopoly characteristics, or –more critically- to lobbying efforts to get legal protection and create an economically unjustified rent."*

364. In the current scenario, it is the first limb of the test that applies. National gas companies have gas sale agreements with the manufacturers and with the scarcity of gas the GOP has no way of redistributing it to any potential entrant. While the incumbents are ensured gas supply owing to the gas sale agreements, any potential entrants would not have this opportunity. As long as the gas scarcity persists the existing manufacturers will have exclusive rights to its supply and would not have to worry about any potential entrant coming in and affecting their position in the market. This apparent preferred allocation of gas, with no apparent threat of future entry, further strengthens the dominant position of the undertakings already found dominant.

365. The last condition is that no sector specific regulator has the jurisdiction to solve the matters. The prices of fertilizer have been deregulated partially since 1986 and completely since 1993[27]. This has been asserted in the ER and has been agreed to by EFL. FFC's claims that a committee was established under the fertilizer policy 2001 to review fertilizer prices and that it does so, on a regular basis, even if correct, still points to an absence of a regulator having jurisdiction to regulate such behavior in the industry. Actions of manufacturers show that they are free to set their prices without any interference from any regulator and there is no evidence to prove the contrary. Unlike some industries, such as textile, fertilizer sector is not directly managed by Self Regulatory Organizations (SRO). The industry falls directly under the purview of Ministry of Food, Agriculture and Livestock (Minfal). The decisions on the allocation of gas to the firms is decided

[27] https://pakissan.com/english/news/newsDetail.php?newsid=15846

by the Economic Coordination Committee (ECC)[28].This condition therefore stands satisfied.

366. With all of the above conditions satisfied, the case of prima facie 'unreasonable price increase' has been shown to be fit for intervention by the Commission.

367. FFC shared views of an article that competition authorities should ideally refrain from cases of excessive pricing except for where pricing has an **exclusionary effect**. It further maintained that in UK the only case where excessive pricing was found to have taken place was that of NAPP. Excessive pricing is not checked by Competition authorities in the U.S.

368. In our considered view, in the NAPP case mentioned by FFC, the Competition Appeal Tribunal ("CAT") of U.K clearly laid out that ***"Nothing in United Brands suggests that the existence of exclusionary conduct is a prerequisite to a finding that prices are excessive contrary to the Chapter II prohibition."***[29] Hence the existence of exclusionary effect is not necessary in probing into such cases as argued by FFC. Furthermore there are a number of screening tests suggested by various competition experts suggesting when an anti-trust authority should intervene in a case of alleged excessive pricing**.** Even if intervention in such cases has been less owing to challenges associated with it, nevertheless they are dealt with as an important competition issue with strong and direct implications on consumers. Satisfying the conditions laid out in the discussion paper by Motta the Commission finds the case of Urea fit for intervention.

369. As mentioned in the ER and also agreed to by EFL both in its written response and in the hearings that Urea production is a deregulated industry. As per the ER, the factors that indicated the behavior of unreasonable increase in price by the undertakings were (i) Gas curtailment not equally affecting all the undertakings (ii) No notable increase in the price of inputs (iii) Significantly higher profit

[28] http://www.pacra.com.pk/pages/research/web_sector_study/fertilizer/Fertilizer_May11.pdf

[29] www.catribunal.org.uk/files/jdgNapp150102.pdf

margins compared with pre-curtailment times (iv) GOP based subsidy and lastly (v) Lack of meaningful Intervention by the GOP.

370. As per findings of the ER gas curtailment did not affect all the undertakings equally. For instance while EFL's new plant that is on SNGPL network faced gas curtailment its old plant was only slightly affected being supplied by a different gas provider. Similarly FFC's plant was only slightly affected by gas curtailment (something in the range of 7-9%). Thus with this factor not being common in the industry (affecting some but not all) the price increase by all appeared rather unreasonable in terms of ER.

371. The other factor relied on by ER was that the cost of inputs involved in the manufacturing did not increase notably in absolute terms. While gas curtailment affected the production and the cost/bag showed an upward trend owing to lower economies of scale, a point worth noting was whether the upward trend in prices demonstrated a higher magnitude in comparison with the costs.

372. As per ER this is precisely what the increase in gross profit margins revealed when comparing 2010 with 2011. Furthermore the gross profit margin was to neutralize the effect of huge debt obligations that could be peculiar to an undertaking rather than a common issue.

373. In terms of ER, while FFC's gross profit margins increased from 43.6% to 62.2% those of EFL went up from 46.9% to 53.37%. Thus a before and after scenario comparison was employed to assess whether gas curtailment resulted in financial decline or that it instead brought gains to the undertakings.

374. The ER maintains that one significant factor in assessing whether the pricing action carried out by the undertakings was unreasonable, was the subsidy enjoyed by them. While EFL enjoyed a subsidy of PKR 4.5 bn in 2011, FFC's subsidy amounted to approximately PKR 11 bn which is not disputed by any of the undertakings concerned.

375. As for the GOP lacking in its meaningful intervention that may or may not have facilitated the situation, however, it is not the conduct of the undertakings, hence not a factor on part of the undertakings constituting any abuse.

376. While examining these factors in totality, the ER found FFC and EFL along with the undertakings to have abused their dominant positions in contravention of Section 3 of the Act by making unreasonable increase in prices.

377. The bench would now assess the findings of the ER and whether the conclusion drawn from them has merit.

378. The arguments made by each of the manufacturer in their defense as to why their prices are not unreasonable are now analyzed to assess whether they hold ground.

FFC:

379. As per FFC there is no accepted yardstick to measure unreasonableness of price. FFC maintains that the duty of proving a reasonable nexus between the price hike and distortion of competition has not been fulfilled in the ER. While the Commission may look into issues where two or more undertakings agree to fix price to distort competition in a market or individually/collectively limit production to raise prices, it cannot look into price increase that is an outcome of curtailment of gas by the GOP and increase in input costs in the form of GOP levies. As long as there is no relationship between the price and distortion of competition FFC cannot be stopped from making any profit.

380. With regard to whether there is a yardstick to measure reasonableness of price, although a complicated issue, various judgments in respect of cases of excessive pricing have now established criteria or tests for its determination. The following view of CAT in respect of OFT's decision in the matter of NAPP would be very useful in clarifying this:

> *"The fact that the Director has not ... precisely quantified by how much he considers Napp's prices in the community segment to be*

excessive ... does not in our view alter the fact that, measured by a number of different yardsticks which all yield the same result, Napp's prices in the community segment were well above the levels to be expected in conditions of normal competition, during the period of the infringement.[30]"

381. The Judgment by OFT in the matter of NAPP said:

The prices charged by NAPP in the community are excessive. The Director considers that a price is excessive and an abuse if it is above that which would exist in a competitive market and where it is clear that high profits will not stimulate successful new entry within a reasonable period. Therefore, to show that prices are excessive, it must be demonstrated that ***(i) prices are higher than would be expected in a competitive market, and (ii) there is no effective competitor pressure to bring them down to competitive levels, nor is there likely to be.***[31]

382. The judgment of OFT that was upheld in the court of appeals U.K. does indeed mention one such yardstick to measure the reasonableness of prices. As hard as the exercise of satisfying such tests may be, it should not be relied upon as an excuse not to intervene in matters where pricing has a far reaching impact on the well being of consumers.

383. In FFC's case it is our considered view that, had there been competition, FFC would not have increased its profits by more than 100% within one year. Gas curtailment leads to lower production that should translate to lower revenues. However in the case of FFC despite no reduction in costs, the revenue went up so much that the profits doubled. With prevailing crisis and forgone production it would not have been possible for an undertaking to increase profits much less by greater than100% if the dynamics of competition existed in the market.

384. It has been amply established that there is no potent and long lasting competitive pressure faced by the Urea manufacturers from each other. Even the GOP's action of imports in 2012 that exerted pressure on Urea prices as per manufacturers' claim if held to be true, was one of its kind occurrence and cannot be seen as a long lasting check. This is especially true when considering that the GOP is itself short of funds and tries to avoid imports as much as possible.

[30] www.catribunal.org.uk/files/jdgNapp150102.pdf
[31] Ibid

385. It has also been established that the barriers to entry are too high in the Urea industry to enable a new entrant in the market. With the conditions prevailing these barriers are insurmountable. In this light the market shares held by various Urea manufacturers are neither at threat from other manufacturers nor any potential entrants. All these factors are significant in examining how FFC was enabled to increase the price above competitive levels.

386. FFC maintains it is incorrect to say that subsidies are not being passed on to the farmers. It argues that they are being passed on 100% as the prices of International Urea are very high and the subsidy provided to Urea manufacturers is based on international gas prices.

387. The Bench is of the view that it would be unfair to compare international prices of Urea with that produced domestically. The aim of the fertilizer policy is to keep the prices of Urea such that they are affordable by the farmers and not to match international prices. International Urea producers are often Urea exporting entities that do not have the same local concerns as Pakistan. They follow the international demand supply dynamics that are different than those prevailing inside a country. It would perhaps be more reasonable to compare Pakistan with India, where the situation is very similar to Pakistan in terms of local concerns and the aspect of self sufficiency with respect to Urea. As a result of this the Government of India imports Urea to fulfill the unmet demand; however the manufacturers are not allowed to charge the same as international exporters. In fact, to date the Government of India has not allowed any of the manufacturing concerns operating in India to charge more than 12% RoE. In Bangladesh where a state owned entity is responsible for Urea manufacturing even a much lesser after tax RoE is realized. These countries offer a better context to appreciate in terms of local concerns as they are primarily agricultural and know the importance of providing Urea at affordable rates to the consumers and hence serve as more appropriate benchmarks than any of the international exporters of Urea. While subsidies given by the Governments in these countries are direct and much higher than Pakistan, they would not be sufficient in maintaining low prices in of themselves. An important factor behind these prices being of greater utility to the farmers is the

fact that profitability enjoyed by the manufacturers in these market particularly India know bounds.

388. FFC argued that it is not the price leader rather a follower and when EFL raises price it has to follow suit. Gas Curtailment, failure to make timely imports and high price of international Urea all contributed to the high price of Urea. FFC cannot sell for lower as it sells to the dealer who will indulge in black marketing and pocket the difference. The GOP also increased the price of its Urea from PKR 1300 to 1600 for the same reason.

389. The Bench has found that in terms of Urea production the market share of FFC is largest. The manufacturer that has the highest market share after FFC is EFL with a market share of 26%. With the market power of these dominant undertakings under prevailing circumstances both had no threat of undercutting in prices, FFC could not be said to be forced to follow the price patterns of EFL. It had chosen to do so for the reason that it allows it to maximize its profits in the absence of any potent competitive pressure existing in the market.

390. As noted earlier the fertilizer industry in Pakistan has never moved in tandem with international prices now or before. One of the aims of fertilizer policy 2001 is to make Urea available to farmers at affordable prices. Historically the Urea manufacturers have not followed the international trend in prices and the relevant period was no exception. Resulting shortage of Urea from gas curtailment is not a new phenomenon either. Previously the shortage in the market was a result of production capacity lagging behind the demand in the country and presently it's due to gas curtailment. Thus shortage is not a new phenomenon and to remedy the shortage in the market the GOP carries out imports. Similarly all this hue and cry regarding shortage also seems to be exaggerated

391. As per submissions from PAFL there was not a time in the Rabi and Kharif of 2010-11 when the demand exceeded supply once the imports were accounted for. This is also demonstrated in **tables 1 and 2**. Even if we talk about the shortage it needs to be appreciated that it was always a feature of this market and the shortage faced in 2011 was no exception. There was a decrease in output due to gas curtailment but EFL's new plant also went into production during this period.

When looked upon year on year basis the shortage in the market does not exceed 4.32% in 2011 compared with 2010 as seen in the following table.

Table 5: Decrease in Actual Production During 2011

Company	Actual Production 2011	Actual Production 2010	Increase/ (Decrease)
	----------Tons----------		
FFC	2,396,160	2,486,272	(90,112)
FFBL	433,165	524,096	(90,932)
EFL	1,279,378	972,075	307,303
DHFL	200,030	456,192	(256,163)
AGL	216,909	370,062	(153,153)
PAFL	28,182	73,920	(45,738)
FFL	427,000	323,000	104,000
Total	**4,980,823**	**5,205,617**	**(224,794)**
% Age Decrease in Actual Production During 2011			**-4.32%**

With such a little change in the availability of Urea from domestic sources putting all the blame on shortage seems nothing more than an excuse.

392. The dealers as mentioned before may however make use of this situation and sometimes even create artificial shortage in the market or indulge in black marketing but again this cannot be taken as an excuse for Urea manufacturers to resort to unreasonable price increases. The prices set in this fashion by the dealers, a large number of whom are unregistered, is not a natural way of establishing prices in the market. In our considered view, such increase in prices therefore in the instant case, cannot be argued as a result of market forces and further cannot serve as a pretext to engage in unlawful and prohibited behaviour/practices under the Act.

393. FFC also emphasized the importance of external factors in determining the reasonableness of price. FFC discussed the case of Attheraces Ltd (ATR) vs British Horse Racing Board (BHB). ATR Ltd is the business of audio visual media related to British horse racing that bought pre-race data from BHB. BHB demanded 50% of the revenues from ATR's activities. ATR filed a case of excessive charging against BHB in the High Court of Justice Chancery division. While the decision was made in favor of ATR, when this matter entered the court

of appeal the cost plus approach was found insufficient in establishing that the price despite being excessive was unfair and the behavior abusive as 'other benefits' accrued by ATR and not accounted for in the costs were ignored. Thus the Court held that the external factors other than costs have to be figured in to arrive at the right conclusion.

394. Another case in EU is that of Scand lines vs. Port of Helsenborg. The main questions addressed with regard to excessive pricing were whether the price was unfair in of itself or when compared with competing products. Other than the actual costs other costs such as high sunk costs for the port, intangible value of the product, the fact that the land used by the port is very valuable and comparative advantages with respect to other ports were considered.. In this case and other cases Economic value of the product to the consumer was considered. Since no such analysis was carried out in the ER FFC argued that the burden of such proof is on the Commission.

395. It was argued by FFC that the external factors pertaining to FFC are shortage of Urea, opportunity cost since FFC invested money in Urea plants, efficiency of operations and benefit to the farmer or utility derived. The ER did not account for any of these external factors. It further submits that the cost plus approach is a very narrow approach.

396. Taking into consideration the above, the bench is of the considered view that Particularly with respect to the Scandlines vs Port of Helsenborg case it needs to be appreciated that its price or profits did not see a drastic increase suddenly. The price at which Urea was sold in 2010 or in the period before that did account for the sunk cost that went into building the Urea plant by FFC. When manufacturing plants are built financial models determine a rate of return that ensures the manufacturers not only recovery of their initial costs but also profits in the long run. So this cannot be seen as a factor behind pushing the price of Urea to its current level. The same logic can be applied to other opportunity or sunk costs. Besides it must also be kept in mind that in the case of NAPP pharmaceuticals the costs and other external factors such as investment in establishing a business,

efficiency of operations and utility derived were not considered at all while determining excessive pricing.

397. FFC also highlighted that, economic value has been seen as a measure of reasonableness of prices in majority of the EU cases pertaining to excessive pricing. This concept must therefore be understood particularly in respect of Urea.

398. In economics the concept of Economic Value is closely linked to that of Allocative Efficiency. Free markets under perfect competition are allocatively efficient however; taking in view the nature of the Urea industry with demand surpassing supply and no real alternatives available to farmers there is absence of appreciable competitive pressure in the market and hence cannot be termed allocatively efficient.

399. It needs to be appreciated that Pakistan is a unique jurisdiction with a unique situation and circumstances. Its markets are not at the same level of development as Europe or U.S. therefore, local concerns have to be factored in owing to its unique situation and circumstances.

400. A complex product with a high degree of differentiation has a high degree of subjectivity associated with it with respect to its value and perception of its worth changing from person to person. The same cannot be said about a simple product such as an essential commodity with least amount of differentiation and that is of essential use to its buyers. When such is the nature of a product the degree of subjectivity with regards to the value of a product is minimized. We are of the considered view that Urea in terms of its usage and perception when produced by one manufacturer is seen the same as by the other. If at all there is preference for branding its absence would still not curtail or impact the farmers exercising the substitute option. It is certainly not very hard to fathom that Urea being a basic commodity with hardly any differentiation does not invoke varying degree of demand depending on its source; its economic value cannot and should not be linked to complex subjective value judgments. Urea sold by one source does not fetch premium over Urea from another source simply because consumer

perception is more or less the same with respect to this product regardless of its source. Thus unlike the case of United Brands where the Chiquita brand of bananas is viewed by its consumers to be superior or different than non branded bananas or bananas of competing brands the same does not hold true in the case of Urea sold in Pakistan.

401. Finally since Economic value is defined as a measure of the benefit that an economic actor is able to gain from a service the aspect of benefit also needs to be looked at. In wearing upscale branded jeans the benefit may lie in relating one self to a superior and stylish class and being perceived as such whereas, the only utility that a farmer can derive out of Urea is in producing and selling crops in the market. The greater the profit margin a farmer can achieve in selling his crop the more utility he'll derive out of Urea. As per a Nov 21, 2012 report of The News the prices of crops have increased far less in proportion to the cost of inputs required to produce them including the Urea fertilizer.

402. This is primarily where the case of Urea fertilizer deviates from that of United Brands.

403. In the case of United Brands a connection of price of Chiquita bananas had to be established with its economic value owing to the fact Chiquita bananas are not just regular bananas. They are a specific brand of bananas with a peculiar style of growing and taste. Chiquita Bananas also cater to various consumer tastes by offering varieties such as 100% organically grown bananas and their mini version. Chiquita bananas are also 100% Rainforest alliance certified. It is these qualities that differentiate Chiquita bananas from non-branded or even competing brands of bananas. In fact in an independent survey, consumers preferred its taste 2 to 1 over the next leading brand. Keeping in perspective that Chiquita bananas are perceived to be different than their competitors there is that aspect of perception and subjective value assigned to it by the consumers and hence one can gather why a cost plus approach in itself was not held to be sufficient to determine its value.

404. FFC also discussed the case of NAPP that the OFT U.K took cognizance of. NAPP manufactured morphine tablets were sold at a price 90% higher to the community segment when compared with the price charged to hospitals. The case of United Brands was taken as a reference in the case and an analysis involving comparison of prices over time, comparison of prices charged to the hospitals, consumers and exported medicines was employed to arrive at the conclusion that prices were indeed excessive.

405. The Judgment of the CAT laid down the following:

"Measuring whether a price is above the level that would exist in a competitive market is rarely an easy task. The fact that the exercise may be difficult is not, however, a reason for not attempting it. In the present case, ***the methods used by the Director are various comparisons of (i) NAPP's prices with NAPP's costs, (ii) NAPP's prices with the costs of its next most profitable competitor, (iii) NAPP's prices with those of its competitors and (iv) NAPP's prices with prices charged by NAPP in other markets****. Those methods seem to us to be among the approaches that may reasonably be used to establish excessive prices, although there are, no doubt, other methods."*

406. It further emphasized that:

"*the fact that the Director has not chosen to rely on other comparators such as international price comparisons or returns on capital does not in our view lessen the force of the comparators upon which he does rely"*.

407. From this it becomes clear that a method applied in determining excessive price may differ from case to case based on its own peculiarities. Furthermore it is established that it is not the number of comparators that are important as long as the comparisons that are made are sufficient to show that the prices are excessive and they would not be possible to maintain in a competitive market.

408. In our considered view the reliance of the ER on the comparators listed therein adequately substantiate the unreasonable price increase on part of FFC as a dominant undertaking. As per accounts of FFC the Gross profit margin as a percentage of sales for FFC went up from **43.6%** to **62.2%** between 2010 and 2011. Thus we see that the difference between costs and revenue went up significantly in 2011 when compared with pre-curtailment times. Gross profits increased from PKR 19.56 bn in 2010 to 34.35 in 2011 which is an increase by a huge **75.6%**.

409. The profit before interest and tax serves as an important benchmark in comparing profitability between companies in a year as it neutralizes the impact of any debt acquired by them. Profits before interest and tax of FFC increased from approximately 17.4 bn in 2010 to 33.95 bn in 2011 as seen in the following table, which is an increase of a whopping **95%**.

Table 6: Financial Performance and Financial Position Analysis of Dominant Undertakings in Fertilizer Industry

Company	Year	Equity	PBIT*	Increase PBIT	PBT**	% Age in Increase (PBT)	PAT***	Increase PAT	ROE After Tax
		Rs in Million			Rs in Million		Rs in Million		
FFC	2010	15,448	17,397	-	16,310	-	11,029	-	**71.40%**
	2011	23,070	33,952	95%	33,166	103%	22,492	104%	**97.50%**
EFL	2010	13,640	6,557	-	5,206	-	3,730	-	**27.30%**
	2011	18,617	14,521	121%	6,877	32%	4,588	23%	**24.60%**

*** Profit before Interest & Tax**
**** Profit before Tax**
***** Profit after Tax**

410. FFC's profits before tax and after tax were **103%** and **104%** higher respectively (refer to tables 6) when compared with these two metrics in 2010 which is huge considering that FFC's plant also faced gas curtailment although only 13% as per its admission and lower economies of scale. With costs of manufacturing at the same level or a little higher such a situation should indisputably lead to reduction in profits in a competitive industry whereas in this case the profitability figures were so high for FFC that it was listed among the top 25 companies of Karachi stock exchange.

411. As per FFC's accounts it's RoE after tax comes out to **97%** in 2011 up from **71.4%** in 2010 as seen in the table 6. As stated above, India is a country most closely related to Pakistan with regard to the importance of agriculture and Urea,

the condition of its people and the situation of availability of Urea in the country. Urea manufacturers in India are allowed an RoE after tax of no more than 12% after tax. In Bangladesh which is another country similar to Pakistan Urea is manufactured by a nationally controlled entity that enjoys much lesser RoE after tax than India. The RoE after tax of 97% is huge in itself but a comparison with RoEs after tax of manufacturers in similar countries leaves no doubt that it is indeed excessive especially when achieved in times of crisis and not owing to innovation or any extra-ordinary operational efficiency. Had that been the case they would have translated to lower costs rather than increased revenues in the wake of reduced sales and much higher prices.

412. In light of the above comparators and facts specific to this case, the Bench is of a considered view that had competition existed in the Urea industry FFC would not have been able to price as high as it did and earn such high profit margins, RoE after tax compared to pre-curtailment times and manufacturers operating in the neighboring countries with very similar circumstances. Furthermore with no real threat of competition from other manufacturers or any potential entrant regarding maintaining it its market share, It is our considered view that the price charged by FFC in the relevant period was not only above competitive level, it was unfair and unreasonable and thus keeping in view all the facts and circumstances this Bench has no hesitation in holding that the subject price increase in SCN in terms of the ER was rightly found as an abuse of dominant position, individually on part of FFC , under clause (a) of sub- section (3) of section 3 of the Act.

EFL:

413. EFL holds that the Fertilizer industry is not the only one where the prices of gas crisis are being passed on as increases in fuel prices are regularly passed on by the GOP in the form of higher tariffs for electricity, petrol, diesel, CNG etc. The power plants receive higher cost of Diesel in the form of higher tariff payable by Wapda which is then passed on to consumers. In fact, all sectors pass on their cost increases to customers. Frequently the increases are even greater for margin improvement purposes as in Cement, Steel, Plastic and Steel products in line with multiple factors such as international commodity prices, local demand increase,

local inflation margin improvements etc. The Fertilizer sector is no different and therefore the expectation that fertilizer sector will increase price only with respect to gas price increase is unreasonable.

414. In our considered view the comparison made above is not relevant. Sectors such as electricity, petrol, diesel and CNG are regulated sectors. The rates of these products are determined by the GOP. Their price increases reflect direct increase in costs and do not involve complexities such as those found in assessing the effect of gas curtailment. Market conditions vary from industry to industry. Sectors such as cement, steel and plastic do not deal with an essential commodity like Urea and have their own peculiar dynamics. Owing to these reasons the comparison is misplaced.

415. EFL maintains that like other commodities international Urea prices have also exhibited a significant jump over the last four years, however this trend was not matched by the local Urea prices up until 2010 on account of relative stability of input prices and steady supply of gas. Only gas curtailment caused supply shortages putting pressure on EFL and others to increase prices. As pricing is always at margins therefore the entire Urea price moved up due to the differences in impact on Urea producers (with some raising prices and others following). These price rises would have been much lower had the curtailment been equally distributed. These factors have already been addressed in FFC's case.

416. EFL tries to show that Urea is a market driven product by pointing to pricing behavior in 2011 and First Half of financial year 2012. In 2011 GOP imposed gas curtailment on the industry resulting in lower production of Urea. To offset losses Urea manufacturers increased prices and the market moved in tandem.

417. The Bench finds it apparent that it was the nature of the market and lack of competitive pressure that allowed the dominant manufacturers to initiate price increases whether it was to offset losses or in some cases increasing profits. This is important when seen in the context that EFL was not just looking at offsetting losses incurred as a result of gas curtailment but also paying off the heavy debt that it borrowed in order to build its new manufacturing facility that went operational in 2011.

418. EFL argues that prices increased from PKR 830/bag to PKR 1720/bag between November 2010 and July 2012. Gas curtailment, being the greatest contributory in EFL's case, is only 32% of the variables responsible for the increase in price. The remaining 68% is accounted for by GIDC, GST imposed by GOP and inflation driven increase.

419. EFL further argues that prices of other commodities such as cotton and wheat also increased in 2010-11. Based on international demand/supply and other factors, commodity price changes are normal e.g. crude oil prices jumped up 79% in 2009 resulting in significant profit jump for oil related firms. None of these increases were preceded by similar level of increases in their input costs but were primarily driven by supply/demand dynamics.

420. EFL's submission is that unfortunately Fertilizer Industry is the only one being singled out. Even in 2011 when Urea prices increased by 64% after incorporating GST its price differential with the international prices increased to PKR 879/bag as against PKR 493/bag in 2010. Unless the EFL is attempted to sell over the international Urea price how could the question of abuse of dominance arise?

421. The Bench without getting into the accuracy figures considers it relevant to point out that the period addressed by the enquiry was from December 2010 to November 2011. GIDC was imposed in 2012 and is not the subject of this enquiry.

422. EFL has itself mentioned that the increase in prices in various sectors was an outcome of demand/supply and other factors. The Bench is of the view that Urea sector is different in that it is a seller's market with no real substitutes available for the consumers. The normal supply/demand dynamics do not exist in the relevant market as in competitive industries. In this regard a comparison of Urea prices with the average increase of crop prices over the last few years as has also been mentioned above we consider it relevant to draw attention to the following:

As per a business recorder report[32] of November 21, 2012

[32] http://www.brecorder.com/agriculture-a-allied/183/1260244/

> *"The prices of different agricultural inputs have registered an increase of 70 to 100 percent during the last five years as compared to only 40-45 percent increase in prices of various produces, said Hasan Ali Chaniho, Director Farmers Associates Pakistan (FAP) and former Agriculture Minister Sindh here on Tuesday."*

423. As per the above, it appears that, just in year 2011 Urea prices increased by more than 80% as against crop prices that only increased 40-45% over a period of five years. This shows how the marginal utility of using Urea has been reducing over the years particularly in the relevant period as the prices of crops are not increasing to the same extent as the inputs required in producing them.

424. EFL emphasizes that the prices of Urea are not a function of input costs only. High international prices are a reflection of global supply/demand dynamics as well as highly capital intensive nature of the industry which warrants high margins over input costs.

425. The Bench reiterates its view that the supply/demand dynamics, the primary orientation of the manufacturers (exporters as against serving local market), factors such as subsidy on gas, cost structure, nature of consumer in fact everything is too different between an international exporter of Urea and a local manufacturer of the same to warrant a comparison between the two.

426. The Bench does not find this to be the right premise. Take the example of SAFCO and QAFCO that are middle-east based Urea exporting entities with no domestic markets. Unlike them the Urea manufacturers in Pakistan cater to the domestic market. Thus the consumers are completely different in the two markets. They charge prices based on international demand supply dynamics that bear no resemblance to pricing bench marks of agrarian economies with their own peculiar dynamics. As explained earlier EFL increased Urea prices owing to its peculiar circumstances. We have already mentioned that in India, manufacturers are allowed no more than an RoE of 12% despite the capital intensive nature of the industry. The nature of Urea industry was always capital intensive but never

was such a price hike seen in the entire history of Urea production in Pakistan. In fact in our view even the capital intensive nature of an industry would not justify raising of prices above a competitive level.

427. The Bench finds it relevant to mention the case of NAPP pharmaceuticals, where it was argued that "A pharmaceutical company's prices should be judged according to its profits on its portfolio, in order to encourage R&D" on which the CAT commented that:

> *"The need to support R&D is not denied by the Tribunal, but is not accepted by it as a reason for justifying pricing above the competitive level."*

428. EFL argues that the subsidy given by GOP is through differential in feed and fuel gas prices. While the quantum of subsidy of PKR 77 bn is correct, CCP must consider the benefit being provided by the fertilizer industry to the farmers by maintaining a huge differential with international prices. This is despite the 3.95/MMBTU for the gas as against much lower prices in other regions. The industry is under no legal obligation to maintain such a differential and is within its right to sell at import parity price like other industries in Pakistan. In 2011 average price of imported Urea was PKR 2400/bag against the local price of 1,149/bag. With total domestic production of 4,901 m ton, this translates to benefit of PKR 23 bn to the farmers as against 34 bn that is attributable to feed/fuel cost differential.

429. The Bench is of the considered view that the local manufacturers of Urea do not operate in the same conditions as the Urea fertilizer exporter as discussed in detail earlier. If the benchmark used by EFL was reasonable it would have been adopted by regional agro based economies with similar situation as Pakistan, particularly India which very much like Pakistan is not self sufficient in respect of its Urea requirement and faces a heavy financial burden in importing Urea to meet the local demand. Therefore, such yardstick to measure the aspect of passing on the subsidy to the farmers does not seem reasonable.

430. One of the reasons that EFL provides for increasing the price of Urea is that of the dealers, who reap the benefits of shortage in the market by charging high price for Urea. Since EFL has no remedy for this behavior of the dealers it feels justified in

closing in on their prices and those of the dealers. In its defense it says that even GOP increased the price of its imported Urea because the end consumers were not getting the benefit of lower prices owing to the dealers' behavior.

431. We have already sufficiently addressed why the dealer factor does not hold weight as a justification with respect to the undertaking's actions of increasing price and are of the view that if the scenario was such that EFL's new plant had not been built and the gas supplied to it was distributed to other plants on SNGPL that are gas starved there would have been no pretext left for any of the dominant undertakings to jack up prices the way they did other than possibly increasing corresponding to GOP imposed tax.

432. EFL argues that the profitability figures quoted are misleading due to capitalization of massive investment made. The EFL is in great financial distress and has approached its lenders for re-profiling of loans through extension of tenor by around two and a half years. The EFL has taken loans to the tune of PKR 70 Bn which has to be serviced and that it is already in a position where it is not able to do so. Apart from financial charges, principal repayment of long terms should also have been included as costs that need to be recovered.

433. What appears to be the main reason behind the price increases throughout the industry is EFL's investment in its new plant since most of the other plants have fully depreciated their initial investment. Only the absence of competition allowed EFL to keep increasing its price at will .One needs to appreciate that risk of investments have to be weighed and the due diligence requires taking all those factors into account while undertaking may have the liberty to mitigate their losses, they cannot be allowed to indulge into exploitative or unlawful practices by passing the burden to the consumer. The undertakings making long term investments have to allow a long time period to recoup its investment and not to recover its investments through short term measures. Also, it is important to appreciate that the arrangement for financing should be designed in a manner that it should not adversely affect the cash flows of an entity. As in the case of EFL it is facing cash flow problems despite having profitable operations, due to its

financing arrangements which is largely payable in the period of two to five years only as per their own financial statement.

434. EFL argues that its input cost has in fact increased by 93% from PKR 641/bag in 2010 to PKR 1240/bag in 2011. Cash fixed costs per bag increased from PKR 140/bag to 154/bag and financial charges exhibited a whopping increase of 770% as the new plant started incurring financial charges. Therefore it is incorrect to say that input cost did not register any notable increase to warrant increase in prices**.**

435. The Bench has observed that despite a cash fixed cost per bag increase from PKR 140/bag to PKR 154/bag the gross profit margins of EFL showed an increase from 46.9% to 53.4% which shows that its revenues grew much more than the costs to allow for greater profitability over cost.

436. Furthermore, we are of the considered view that it is incorrect to assume that the profitability figures are misleading due to capitalization of massive investments made. The heavy investment made in setting up a plant is always capitalized and never made a part of accounting profits that run from year to year. The heavy debt of 70 bn PKR in respect of the investment EFL made and the terms on which it agreed to pay it back are peculiar to EFL. It is primarily for this reason that financial charges pertaining to EFL experienced an increase of such a high magnitude. In our view, the major onus of the risk associated with EFL's investment was thus affectively passed on to the consumer through price increases in the absence of competitive pressure, with such a low bargaining power the consumer had no choice but to accept his fate and buy this essential commodity despite its plummeting utility that a consumer could derive from the now much more expensive Urea.

437. EFL is of the opinion that abnormal profits should be reflected in a high RoE and that there are many companies with managed RoEs and RoAs(Return on Assets) comparable or better than the EFL's RoE after tax of 24.6%. Furthermore, it submits high RoA or RoE do not imply unfair prices and particularly with respect to the EFL's RoE is not reflective of its worrisome financial position.

438. In India the Government provides enough subsidy to the manufacturers in terms of raw material such that their RoE does not exceed 12%. That has historically been the case. As already emphasized India's situation is very similar to Pakistan and keeping that in perspective the RoE enjoyed by EFL is twice that of an Indian Urea manufacturer. Even in encouraging the expansion that India is looking forward to carry out to lessen its dependence on imports, it is offering RoEs between 12%-20% with 20% being the ceiling to those who would establish new plants. These are future prospects and a 20% ceiling is considered a great enough incentive for firms to enter or expand. Historically RoE figures in India have not exceeded 12%. When EFL's RoE after tax of 25% is seen in this light it appears to be reasonably high.

439. EFL argued that its gross margins have improved for the reason that its gross margins have been taken from published accounts which are missing some key financial events that impacted EFL in 2011. Due to non-availability of gas the EFL was forced to delay commercial production until June 2011 even though it achieved production in Dec, 2010. All costs including financial charges, cash costs etc were capitalized and EFL did not start booking the depreciation up until June 2011. If not for the accounting standards the EFL's net profit margin would have been 6% vs 15% in 2011. The EFL's cash generation in 2011 was barely enough to meet its debt obligation. Had it not increased prices it would have faced a cash deficit of PKR 8.6 bn.

440. As per note 2.1.1 of the financial statements of EFL Corporation Limited they are prepared in accordance with the requirements of the Companies Ordinance, 1984, directives issued by the SECP and the approved financial reporting standards as applicable in Pakistan.

441. According to the definition[33] of matching principle of accounting it is:

> *"A fundamental concept of accrual basis accounting that offsets revenue against expenses on the basis of their cause-and-effect relationship. It states that, in*

[33] http://www.businessdictionary.com/definition/matching-principle.html

measuring net income for an accounting period, the costs incurred in that period should be matched against the revenue generated in the same period."

442. So as per above principle it is normal to book depreciation, finance expense and other expenses in the period during which related revenue is booked. If the costs are not accounted for in the first half of 2011 nor are the revenues associated with it, hence the only appropriate measure of determining profitability of a plant would be to consider the costs and revenue incurred by the new plant after commencement of its commercial operation date as accurately reflected in the audited accounts of the undertaking.

443. EFL submits as a further proof that in 2012, it is facing a difficult financial situation contrary to the allegation of abnormal profitability growth achieved through price hikes. During the first half of 2012 the EFL suffered an estimated pre-tax loss of PKR 2.5 bn when Urea price per bag was PKR 1544 owing to availability of gas for only 45 days. EFL's profit for first half of 2010 was PKR 2 bn.With regard to the above submission it needs to be appreciated that the period covered by the ER is between December 2010 and November 2011 and what concerns the Bench is the pricing actions carried out by the undertaking during that period and for reasons already stated the focus has to remain within those parameters.

444. As per EFL, the profits after tax for 2011 after adjusting for capitalized costs (from Jan to June 2011) were only PKR 1.7 bn which is 54.5% decline compared with 2010. This decline should be seen in the context that the EFL took loans of more than PKR 70 bn for the new plant and servicing of these loans necessitated substantial increase in profitability and cash generation.

445. In this regard the Bench is of the view that as per accounting standards it is not appropriate to account for costs where the matching revenues are not accounted for. The only correct measure of the profitability of a plant is when it has commenced commercial operation as shown in the audited financials of the undertaking. With respect to the audited financial statement of EFL during the year 2011 its profits after tax actually increased from PKR 3.73 bn to PKR 4.59 bn representing an overall increase of approximately **23%**.

446. We find merit in the reliance placed by ER on Gross profit margin which is a measure that involves cost of goods sold and do not involve costs such as financial charges. This is a standard measure that neutralizes the peculiar situation faced by EFL as a result of its massive investment and resulting debt service obligations. The Bench observes that the Gross profit margin for EFL did in fact go up from 47% in 2010 to 53% in 2011 as calculated from the figures provided in the audited financial statement of EFL. The total production by EFL went up from 0.97 metric tons to 1.28 metric tons which is an increase in production of **31.6%** while in comparison the Gross profits increased from PKR 8.9 bn to PKR 16.7bn from 2010 to 2011 which is an increase in Gross profit by almost **88%**. Even if one is to take on face value the gross profits of PKR 16.1 bn that EFL claims would have resulted had its costs related to the first half of 2011 not been capitalized, it is an increase by **81%** compared to the gross profits in 2010. Such a high increase in gross profit despite an increase in cost of production from 10.12 bn to 14.62 bn which is approximately **44.5**% cannot be attributed merely to increased production but primarily to the unreasonable increase in price as a result of which the value of net sales went up from 19.02 bn in 2010 to 31.35 bn in 2011 which is an approximately **65%** increase.

447. The profit before interest and tax is treated as an important benchmark in comparing profitability of different companies in a year as it neutralized the impact of any debts acquired by them. The Profit before interest and tax of EFL increased from approximately 6.6 bn in 2010 to 14.5 bn in 2011 which is an increase of **121%** as seen in table 6. It is important to note that EFL's Profit before interest and tax increased by 121% against FFC's increase of the same of 95%. This implies that if the interest or debt obligation were taken out of the picture, this price increase would have translated into enormously high after tax profits for EFL as they have for FFC.

448. The Bench is of the view that if the market for Urea was competitive with excess capacity relative to demand in place EFL's competitors vying for greater share in the market pie and not facing the same costs as EFL would have undercut any attempt by EFL to raise prices which would have forced EFL not to increase prices much beyond the GST imposed by the GOP.

449. EFL submits that prices of Urea in Pakistan are far below international prices and they are higher when compared with India, Bangladesh and Sri Lanka because the governments there offer much greater subsidy than the subsidy through lower gas prices in Pakistan. EFL has repeatedly maintained that if the continuous gas supply is ensured to its plants, it will reduce its prices to give even further benefit to the farmers.

450. In the **OFT** judgment with respect to **NAPP** it was held that:

> *"to show that prices are excessive, it must be demonstrated that*
>
> *a. Prices are higher than would be expected in a competitive market, and*
> *b. There is no effective competitive pressure to bring them down to competitive levels, nor is there likely to be."*

451. The Bench considers that a (i) high after tax RoE (ii) the huge increase in gross profits in 2011 when compared with 2010; was only made possible due to the absence of any appreciable competitive pressure While the net profit margins of EFL may have plummeted during the relevant period when compared with 2010 it does not lead to the conclusion that the prices were not above competitive level.

452. In this regard it will be helpful to look at the case of **Belko** where The Competition Board in Turkey analysed cost-price relationship and ruled that

> *" … while, along with high prices, a large margin between the sale price and the total cost (excessive profit) could be considered a sign of excessive pricing, monopolistic pricing is also possible in situations where the profit margin turns out low or even negative due to establishment of real or fictitious costs in excessively large magnitudes (along with prices set at relatively high levels).*"

453. In view of the above, we find that in the absence of any competitive pressure in the relevant market, EFL was able to raise its price above a level that a competitive market would have allowed and that cannot be termed as just or fair. As observed earlier, EFL did not face any existing or potential threat of competition in the relevant market due to insurmountable entry barriers. The Bench therefore, holds that the conditions set in the NAPP case by OFT are

fulfilled by the pricing actions carried out by EFL during the relevant period and hereby holds EFL to have individually abused its dominant position in the relevant period through unreasonable price increase which in terms of Clause (a), Subsection (3) of Section 3 of the Act and thus hereby upholds the findings of the ER in this regard.

454. In view of the foregoing we hereby hold and deem EFL to have abused its dominant position in the relevant period by charging an unreasonable price in the relevant market in violation of section 3 of the Act.

Collective Dominance:

455. The Act lays down the definition of ' Individual Dominance' and 'Collective Dominance' in section 2(1)(e) as follows:

> *"dominant position" of one undertaking or several undertakings in a relevant market shall be deemed to exist if such undertaking or undertakings have the ability to behave to an appreciable extent independently of competitors, customers, consumers and suppliers and the position of an undertaking shall be presumed to be dominant if its share of the relevant market exceeds 40%"*

456. Thus as per the Act if several undertakings together can act to an appreciable extent independent of their competitors, consumers and suppliers they shall be deemed to be collectively dominant.

457. In the ER the following arguments and reasoning was given to determine the existence of collective dominance in the fertilizer industry:

> *"Taking all the above factors into account, it appears that the price increase of this magnitude representing 86% increase from PKR.850 per bag to PKR.1580 per bag by all the manufacturers at the same time was unjustified and unreasonable and prima facie makes out a case of individual and collective abuse of dominance on part of each of Urea manufactures. Where factors such as Economies of scale, operation efficiency, innovation and impact of gas curtailment varied from one Urea producers to the other, they increased prices at the same rate and at same time. This increase is unmatched in any other period of Pakistan's history. The manufacturers have not been able to provide any convincing reasons or justifications for simultaneous increase in*

prices of Urea fertilizers without any significant increase in their cost of production. The simultaneous and coherent increases in prices of Urea in the absence of an objective justification by the industry players indicate some formal or informal understanding between Urea producers. Even if one is to assume that such an understanding is non-existent it is worth noting that FFC and FFBL[34] group and DHCL[35] and Engro group collectively hold 84% (including its new plant) of the total Urea market. Analysis of the price increase patterns indicate that ECPL is always the price leader despite having lesser market share when compared with FFC & FFBL. Generally these two players appear to dictate the Urea price in the country and both have benefited tremendously by the recent price hike as detailed in the profitability analysis. Such situation further supports and strengthens the aspects of abuse of 'Collective Dominance' in the Urea market in Pakistan.

Individual undertakings can be collectively dominant if they are participants in a tight oligopoly and act in unison. To be more precise, a dominant position is held collectively when legally independent undertakings are linked in such a way that they adopt a common policy on the market. The links may be structural or economic but they make the undertakings to adopt the same policy on the market without ever explicitly agreeing on a particular practice/conduct."

Following characteristics are considered as essentials for existence of collective dominance:

A few large producers occupy the market, as is the case in Urea fertilizer market where there are a total of 7 producers and if we consider the producers of the same group as one, there are only 3 producers in the relevant market.

Either these few companies offer homogenous, or standardized, products OR offer different products and place an emphasis on non-price competition, such as advertising. – This condition also appears to be met by Urea producers as Urea fertilizer is a homogeneous product.

As stated in earlier part of the report, Urea producers have always increased prices in parallel manner and irrespective of their individual market shares, production capacity, input costs, economies of scales etc they have increased prices in a coherent fashion, so the Urea market appears to satisfy this condition as well.

Relatively high entry barriers – huge initial investment and scare resource of natural gas as a key input appear to make entry barriers relatively high in Urea market.

[34] FFBL is a subsidiary of FFC which hold its 51% shareholding. Fauji Foundation, the ultimate holding company of FFBL also holds 17.29%.
[35] DHCL and its associates hold majority stake in ECPL.

> *Section 2 (1) (e) of Act provides a deeming provision for collective dominance of several undertakings. Dominant position of several undertakings in a relevant market shall be deemed to exist if such undertakings have ability to behave to an appreciable extent independently of competitors, customers and suppliers and the position of an undertaking shall be presumed to be dominant if its share of the relevant market exceeds forty percent.*

In view of above discussion, Urea fertilizer market appears to satisfy all the four conditions for existence of 'Collective Dominance'."

458. Party wise Arguments raised by the Urea manufacturers with respect to 'Collective Dominance' and the Commission's view on them are as under:

SUBMISSION MADE BY THE UNDERTAKINGS OBJECTING COLLECTIVE DOMINANCE:

459. It has been contended by the parties that the Act does not use the expression 'Collective Dominance'. 'Collective Dominance' is a concept taken from European jurisprudence and must be understood in the same context. It is well settled that price parallelism among undertakings on its own is not sufficient evidence to establish 'Collective Dominance' as it is a recognized feature of oligopolies. This features stems from the interdependence undertakings have in an Oligopoly. We must record our appreciation for the assistance rendered by all counsels on this issue and particularly by the counsel of DHFL who very ably and comprehensively assisted this Bench in the determination of 'collective dominance'.

460. The European Court of Justice (ECJ) is clear that price parallelism alone is insufficient to constitute anti-competitive conduct. This is evident from the **Wood Pulp case** and **Hoffman-la Roche**.

461. In Wood Pulp the ECJ annulled much of Commission's decision finding that the Commission did not appreciate that the behavior of undertakings was a consequence of the non-collusive interdependence that existed in an oligopolistic market.

462. In Hoffman-la Roche ECJ rejected the idea of parallel courses of conduct constituting a dominant position stating that such conduct is peculiar to oligopolies.

463. The Commission would like to apprise here that even though the term collective dominance is not mentioned in the Act, the concept is in fact covered under section 2(1)(e) along with individual dominance.

464. Under the ER dominance was perceived to exist among the manufacturers in a collective sense not purely based on the fact that their prices moved in tandem but on the basis that they had a common economic interest in increasing prices owing to the absence of competition.

465. The parties hold that as per description in the ER, Urea market in Pakistan is characterized as an oligopoly, Parallelism of conduct may therefore be most inevitable in this market. The Criteria for determining whether undertakings enjoy 'Collective Dominance' requires the establishment of 'economic links' or more recently 'connecting factors' between undertakings.

466. Recently in **Compagnie Maritime Belge Transporters** it was held that it must be ascertained whether economic links exist among undertakings that enable them to act independently of their competitors and consumers. It further held that the existence of a collectively dominant position may flow from the nature and terms of an agreement, the way it is implemented and consequently from **links and factors which give rise to a connection between undertakings** which result from it.

467. Nevertheless the existence of an agreement or of other links in law is not indispensable to finding of a collectively dominant position as such finding may be based on other connecting factors and would depend on an economic assessment and particularly **assessment of the structure of the market** in question.

468. It is argued that the ambiguity in the terms **'economic links'** and **'connecting factors'** is one of the difficulties in applying the test. The allusion by the ECJ in **Compagnie** to the 'structure of the market' as a connecting factor implies certain

stringent condition that need to exist in an oligopoly for finding a collectively dominant position. These conditions have been clearly laid out in **Airtours** and subsequently in **Laurent Piau**:

a. Each member of the dominant oligopoly must have the ability to monitor other members for compliance with common policy.

b. Some form of credible deterrent mechanism in case deviation by an oligopoly member is detected to sustain tacit coordination over time.

c. Foreseeable reaction of current and future competitors and consumers must not jeopardize the results expected from the common policy.

469. The difficulty in ascertaining the meaning of 'economic links' and 'connecting factors' can only be understood by examining the situations in which EU jurisprudence has found 'Collective Dominance' to exist in practice. 'Collective Dominance' has only ever been found when certain explicit consensual arrangement existed between independent undertakings. For Example in:

a. **Compagnie Belge** undertakings were members of a shipping conference;

b. **TACA** undertakings had contractual links with each other and were members of a liner conference which contained common pricing provisions;

c. **Italian Flat Glass** undertakings were found to have formed a cartel;

d. **Almelo** undertakings were members of a trading association;

e. **Wouters** undertakings were contractually linked through their membership in an association although ECJ did not think these links were close enough to establish 'Collective Dominance';

f. **Laurent Piau** undertakings were members of an association with legally binding rules as to members' transactions.

470. In the absence of such evidence EU jurisprudence has been unable to assert 'Collective Dominance' between undertakings. It is small wonder that this is the

case as commentators have argued that collusion is unsustainable without some form of communication between undertakings. The ER and SCN do not refer to any evidence of communication between the fertilizer manufacturers except price parallelism which as mentioned before is legally incapable of supporting a finding of 'Collective Dominance'. It was argued by the parties that the ER and SCN do not describe how the relevant characteristics of the 'structure of the market' are met in the instant case in particular the second requirement of a credible deterrent mechanism. Further there is no allegation in the ER or SCN that price parallelism occurred as an outcome of some communication between the fertilizer manufacturers.

471. Where the ER lays out the characteristics considered essential for the existence of collective dominance, the characteristics it notes are really those of an oligopolistic market (Paragraph 87 of the ER).

472. Furthermore, it was submitted by the parties that this idea also finds resonance in Anti-trust jurisprudence of the US. Even more pertinent is that this aspect of antitrust jurisprudence has received endorsement by the higher judiciary in Pakistan as well as MRTP (Control and Prevention) Ordinance 1970.

473. Oligopolies, price parallelism or coordinated effects are not treated as being anti-competitive in the absence of **'plus factors'**. The **US Supreme Court's treatment** of such coordination is as follows:

> *'Tacit Collusion, sometimes called oligopolistic price coordination or conscious parallelism, describes the process, not itself unlawful, by which firms in a concentrated market might in effect share monopoly power, setting their prices at a profit maximizing, supra competitive levels by recognizing their shared economic interests and their interdependence with respect to price and output decisions.'*

474. In **D.G. Khan Cement**, Justice Saqib Nisar after citing several US decisions summarized the legal position as follows:

> *a. Parallel business behavior or conscious parallelism is not in itself sufficient to indirectly establish an agreement in violation of the Sherman Act. Parallel business behavior is all the more possible in the case of standardized products where it is expected that prices will*

ordinarily tend to move in parallel. Furthermore in a concentrated market where there are relatively few sellers, conscious parallelism is also to be expected.

b. If there are certain factors, referred to as 'plus' factors, in addition to and over and above, parallel business behavior, then a presumption arises that there has been unlawful price fixing and in such a situation, a violation of the Sherman Act can be indirectly inferred. The 'plus' factors may include evidence demonstrating that the conspirators acted contrary to their economic interests and were motivated to enter into a price fixing conspiracy. The nature of a ***'plus' factor*** *must be such that it tends to exclude the possibility that the alleged conspirators acted independently.*

c. If parallel business behavior and ***'plus' factors*** *are found to exist, the alleged conspirators can nonetheless rebut the inference of collusion by presenting evidence establishing that it could not reasonably be concluded that they entered into a price fixing conspiracy.*

475. Like economic links or connecting factors in EU jurisprudence **'plus factors'** is the extra proof required to conclude that parallel conduct is anti-competitive. US courts often describe conspiratorial motivation and acts against self-interest as evidence of plus factors. While the Supreme Court has not recounted a list of plus factors, numerous plus factors such as 'motive to conspire', 'opportunity to conspire', 'high level of inter-firm communications', 'irrational acts or acts contrary to a defendant's economic interest, but rational if the alleged agreement existed and departure from normal business practices, have been considered by other circuits.

476. The burden of proof for establishing these factors lies with the body alleging anti-competitive conduct. With the establishment of plus factors only a presumption of anti-competitive behavior arises meaning thereby that there undertakings involved are free to present evidence to rebut that presumption.

477. There is a significant body of evidence under EU, US and Pakistani law that has settled the need of persuasive plus factors for undertakings to have 'Collective Dominance'.

478. We also consider it relevant to address the Intervener's arguments offered in this regard.

479. It was argued that the most difficult to prove is existence of the second condition that says that there should be a deterrent mechanism in place to punish an oligopoly member who deviates from the common policy. While it is not worth the while for any manufacturer to follow any other policy but price increase due to the fact that it is a sellers' market there is no evidence to shows that there is a pre-agreed mechanism among the members to correct the behavior of a member who deviates from this policy. Although in the current scenario a deterrent mechanism does not have to be in place owing to the fact that increasing prices and subsequently profits is an incentive enough itself; this proves as a deterrence. We are of the considered view that the above stated structure of market while may be present has not been addressed in the ER. Evidence on existence of any physical indication of this structure is missing in the market and based on that alone this Bench cannot find the undertakings exercised collective dominance.

480. However, upon review of the cases cited above and the principles relied upon the Bench is of the considered view that the ER is deficient in addressing the requisites of collective dominance against all subject undertakings, while alleging in the SCN the alleged contravention. We have no doubt in holding that the concept of 'collective dominance' is very much envisaged in the definition of 'dominant position' itself. However, the ER does not sufficiently address the evidence of 'economic links' and as for structural links which may appear to exist in two instances i.e. FFC and FFBL and EFL and DHFL(no matter how diluted); in the absence of same being addressed specifically in the ER, these cannot be taken into consideration at this stage and there is no doubt that mere price parallelism without discussing the plus factors through substantiation of economic or structural links would not constitute abuse of dominance collectively on part of the subject undertakings. We find merit in the submissions of DHFL and others and hereby hold the findings of the ER on the aspect of abuse of dominance collectively on part of all the undertakings concerned, as untenable.

REMEDIES:

481. The Bench finds and holds both FFC and EFL to have abused their dominant position individually by raising the prices of Urea unreasonably above competitive levels. We must bear in mind the obligation attached to dominant undertakings as highlighted in ECR 1983 Pg NO. 03461; NV Nederlandsche Banden Industrie Michelin v Commission of the European Communities wherein it was observed:

> *"10. A finding that an undertaking has a dominant position is not in itself a recrimination but simply means that, irrespective of the reasons for which it has such a position, the undertaking concerned has a special responsibility not to allow its conduct to impair genuine undistorted competition on the common market."*

482. In determining the quantum of penalty, taking into all factors available on record, including the accounting comparators, in particular, the facts that: the subsidies given by GOP and availed by FFC alone is around PKR 11 billion and that availed by EFL is around PKR 4.5 billion in a period of one year, given the nature of the product i.e. Urea being the essential commodity and the significance it holds for Pakistan's economy; we are of the considered view that the subject price increase of the product in question i.e. Urea is by all means astronomical, unfair and unreasonable. Therefore, such violation makes it a just and fit case for imposition of a maximum penalty. In fact the harm done to the consumers is far more than what could be translated into deterrence through such imposition, but we are constrained by the maximum penalty envisaged under the Act. Accordingly, the Bench hereby imposes a penalty equivalent to 10% of each of the undertakings turnover in 2011; a sum that amounts to PKR 3.14 billion in case of EFL and PKR 5.5 billion in case of FFC - each held liable to pay the penalty for abusing its dominant position in violation of Section 3(3) (a) of the Act.

483. Furthermore, we deem it important to advise Securities and Exchange Commission of Pakistan (SECP) that in order to ensure transparency in a sector which is heavily subsidized, forensic cost audits pertaining to all the manufacturers operating in the Urea market has become critical and must be carried out by independent auditors and the information so obtained is to be

submitted to the relevant departments of the Federal and Provincial Governments along with the Commission.

484. Also, appreciating the fact that Agriculture plays an extremely important role in the country's economy, in feeding its population and in providing livelihood to a very large percentage of the population; we are of the considered view that the Government of Pakistan needs to evolve a mechanism whereby the subsidy (if any) should be envisaged to target the farmers directly as farmers are the end consumers and are intended to be the eventual beneficiaries of such subsidy and one of the principle objectives of the existing fertilizer policy of GOP is to make Urea available at affordable prices.

(Rahat Kaunain Hassan)
Chairperson

(Abdul Ghaffar)
Member

Islamabad, the March 29, 2013.