

Fighting Cartels: Economic Analysis and the EU Experience

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Outline of the talk

- Economic analysis
 - What is collusion
 - Tacit v. explicit collusion
 - Practices that help firms sustain collusion
 - Policy implications: standard of proof, enforcement
- The European Union experience
 - Legal and institutional framework
 - The case law
 - EU cartel policy in line with economic thinking, but is it enough?

The Economics of Collusion

Antitrust laws prohibit agreements aimed at fixing prices, sharing markets etc.

Rationale: such agreements allow firms to exercise market power they would not have otherwise

Collusion may take different forms, and laws may differ as to what is unlawful, and what is required to prove infringement of the law

Important to understand what is collusion, what helps firms to sustain it, what actions can be taken to fight it

Collusion, I: enforcement

Collusion refers to a situation where firms set prices which are higher than some competitive benchmark

For economists, collusion is an outcome (and ‘collusion’ is not synonym of ‘unlawful cartel’)

What ingredients are necessary to enforce collusion?

Timely detection of deviations from collusive actions

Credible mechanism for the punishment of deviations

Threat of punishment prevents firms from deviating

Examples (explicit agreement not necessary)

Collusion, II: Coordination

Which collusive price? The problem of coordination

Tacit collusion: costly experimentation to coordinate on a collusive outcome, risk of triggering price wars

Explicit collusion: firms coordinate on collusive outcome and avoid problems due to shock adjustments

(Market sharing schemes: possible to adjust to cost and demand shocks without triggering price wars)

Firms will try to talk in order to coordinate!

Factors that facilitate collusion

I. Structural factors

Concentration, entry, symmetry, multi-market contacts, frequency of orders...

Mostly, not manipulable by firms, but:

- Firms might use mergers to have industry conditions more favourable to collusion: importance of joint dominance (coordinated effects) in merger analysis
- Cross-ownership and links with competitors

Facilitating factors, II

II. Price transparency and information exchange

Observability of firms' actions facilitate enforcement

- Exchange of disaggregate information on *past/current* data helps firms to identify and punish deviations

Communication facilitates coordination

- Focal points
- Exchange of information on *future* prices and outputs (private v. public announcements)

Facilitating factors, III

III. Pricing rules and contracts

Meeting-Competition clauses (helps collusion, by eliciting information on rivals and discouraging deviations in the first place)

Resale price maintenance (enhances cartel stability by eliminating variation in retail prices)

Policy: How to detect and fight collusion?

For economists, collusion as an outcome

Both tacit and explicit agreements may sustain collusion

So, why not inferring collusion from market data?

Inferring collusion from data. Problems, I: price levels

Price data availability (list v. effective prices)

Difficult to estimate 'monopoly price' and marginal costs

Where to set the threshold level? (regulation?)

A dangerous principle: firms guilty because able to set a high price... (market power not a problem per se)

Standards of proof, II: data

Inferring collusion from data, II: evolution of prices

Price parallelism: not a proof of collusion (common shocks)

Periods of ‘price wars’ not sufficient condition for collusion either (new capacity, new competitors, demand shocks...)

Which *legal certainty* if firms are found guilty for independent business practices?

Conclusion

Data useful to identify industries to investigate, econometrics for complementary evidence, not proof

Standards of proof, III: hard evidence

Hard evidence only (of communication on prices and/or coordination on facilitating practices) as proof

(focus on observable elements verifiable in courts, to preserve legal certainty: fax, e-mail, phone calls, video etc.)

Too lenient with the firms?

(Since collusion can be reached tacitly, focusing on ‘hard evidence’ amounts to permitting collusion?)

Not necessarily: firms will try to coordinate to avoid costly market experimentation and will leave ‘traces’

More active policies can be used, ex ante and ex post

Ex ante policies to fight collusion

Black list of facilitating practices might deter collusion and free resources for cartel detection

- Private announcements of future prices/outputs
- Exchange of disaggregate current/past information
- Meeting competition, RPM and other clauses, if adopted by coordination
- Cross-ownership among competitors not to be allowed
- Merger control (joint dominance)

Deterrence of collusion: which sanctions? (see below)

Ex post policies to fight collusion

Surprise inspections (also in managers' homes)

Leniency programmes

The US and EU experience:

Leniency must be clear and certain (not discretionary)

Leniency should be extended to firms that report *after* an investigation has started

Fighting Cartels in the EU: the Law

Article 81 of the Treaty: prohibition of agreements and concerted practices that have the object or effect to distort competition, unless they improve goods and promote economic progress (provided consumers gain and agreements are no more restrictive than necessary)

- ‘Concerted practices’: not only agreements may be illegal (definition is deliberately vague)
- ‘by object’: if a cartel (or concerted practice) is found, not necessary to look at its effects
- Cartels are (almost) per se illegal (rare exceptions)

Cartels in the EU: enforcement

European Commission (DG-COMP) is the Competition Authority in the European Union (also, NCAs)

- Administrative system, with Community Courts on appeal
- EC has extensive investigatory powers, including surprise inspections in offices and private homes
- Fining policy (EU – national laws may differ):
 - no criminal penalties (nor sanctions to managers)
 - max fine is 10% of previous year total turnover
 - fines to be fixed according to gravity and duration
 - private actions rare (only non-EU jurisdiction)

Enforcement, II

EC has considerable discretion in giving fines (to a large extent unpredictable; no attempt to estimate damages)

Consensus that EC has increased fines over time, but not clear if enough for them to be a deterrent

- resorting to private actions for damages?
- introducing criminal sanctions? (unlikely)
- focusing on cartels, and leave less important cases to national authorities ('modernisation process')
- but the main novelty has been leniency programmes

Leniency Programmes (LP) in the EU

Main principle: give incentives for violators to report cartels and evidence needed to prove them

First Leniency Notice: 1996

- 75-100% reduction if report before investigation starts
- 50-75% if investigation started but insufficient evidence for initiating the procedure
(in both cases, only if firm is first to report, has ended all cartel activities, and is not ‘instigator’ of cartel)
- 10-50% if cooperation during investigations (e.g., not challenging EC allegations)

Leniency in the EU: 2002 Notice

LP disappointed expectations; problems:

1. EC kept considerable discretion in fines
2. Immunity only if investigation had already begun

February 2002: New Leniency Notice. Immunity is:

- confirmed in writing upon providing evidence
- given also if enough information to launch inspection but not to establish infringement (verifiable?)
- given as long as firm 'has not coerced others' (why?)

[Also, oral leniency procedure not to penalise the applicant in civil actions for damages]

Leniency in the EU: Statistics*

- 80 leniency applications under 1996 Notice (6 years)
 - Mostly, for *reductions* of fines (i.e., after surprise inspections)
- 159 applications under 2002 Notice (3½ years to end Sept. 2005)
 - 80 applications for immunity, of which:
 - 49 conditional immunity decisions (45 for evidence enabling EC to carry out surprise inspection; 4 for allowing it to find infringement)
 - 19 not granted; 12 still under examination
 - 79 applications for reduction of fines (most still being assessed)
- 2002 Leniency Notice seems to uncover many secret cartels, but considerable backlog (also, most firms still appeal in Court)
 - plea bargaining to reduce appeals and speed up procedures?
(main advantage of LP should be to free EC's resources!)

*EC's *Competition Policy Newsletter*, Autumn 2005

Standards of proof in the EU

Parallel behaviour not per se unlawful

- *Wood pulp* (1993): European Court of Justice (partly) annuls EC Decision because:
 - “parallel conduct cannot be regarded as furnishing proof of concertation unless concertation constitutes the only plausible explanation for such conduct”
 - “[Art.81 of the Treaty] does not deprive economic operators of the right to adapt themselves intelligently to the existing and anticipated conduct of their competitors”
- *Dyestuffs* (ECJ, 1972): a case where concertation was only plausible explanation for parallel pricing

Agreements to exchange information

Theory: no problem if information is at the aggregate level, but exchange of firm-level, recent data on prices and sales will facilitate collusion

EU case law (e.g. *UK Agricultural Tractors*): setting up a scheme to monitor each other's sales data is a concerted practice

Hence, an Article 81 infringement is found even absent documentary evidence, if it can be shown that firms have purportedly created an environment where collusion can be more easily sustained

Conclusions

- EU anti-cartel law and policy broadly in line with suggestions from economic thinking
- However, more can probably be done on enforcement:
 - Unclear that fines are large enough to act as a deterrent (also, little evidence that firms and managers are really ‘harmed’ by a negative decision: perhaps because too soft?)
 - If fines were less discretionary, deterrence effect would increase, and there would probably be fewer court appeals, which are inefficient
 - Absence of criminal penalties and (treble) civil damages strengthen the problem