# CARTEL ISSUES & CHALLENGES

## CARTEL ENFORCEMENT AND SETTLEMENT

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*Brief of Competition Act, Cartel Issues & its Harm, How it should be detected/investigated by Regulatory Agencies etc.*

***CARTEL*** is a formal agreement among competing firms. It is a formal organization where there is a small number of sellers and usually involve identical products. Cartel members may agree on such matters as price fixing, total industry output, market shares, allocation of customers, allocation of territories, bid rigging, establishment of common sales agencies, and the division of profits or combination of these. The aim of such collusion (also called the cartel agreement) is to increase individual members' profits by reducing competition.[1]

One can distinguish private cartels from public cartels. In the public cartel a government is involved to enforce the cartel agreement, and the government's sovereignty shields such cartels from legal actions. Inversely, private cartels are subject to legal liability under the anti-trust laws now found in nearly every nation of the world. Furthermore, the purpose of private cartels is to benefit only those individuals who constitute it, public cartels, in theory, work to pass on benefits to the populace as a whole.

Competition laws often forbid private cartels. Identifying and breaking up cartels is an important part of the competition policy in most countries, although proving the existence of a cartel is rarely easy, as firms are usually not so careless as to put collusion agreements on paper.

The term **Cartel** originated for alliances of enterprises roughly around 1880 in Germany. The name was imported into the Anglosphere during the 1930s. Before this, other, less precise terms were common to denominate cartels, for instance: association, combination, combine or pool. In the 1940s the name cartel got an Anti-German bias, being the economic system of the enemy. Cartels were the economic structure the American antitrust campaign struggled to ban globally.

A distinction is sometimes drawn between public and private cartels, though there is no evidence that public cartels are less harmful to the general good, and being government backed, they are much more effective and, hence, potentially harmful. In the case of public

[1] Some provisions of this Article have been taken from Statutory Enactments & related practices and remaining are views expressed by the Author on the basis of his practical exposure .

cartels, the government may establish and enforce the rules relating to prices, output and other such matters.

Export cartels and shipping conferences are examples of public cartels. In many countries, depression cartels have been permitted in industries deemed to be requiring price and production stability and/or to permit rationalization of industry structure and excess capacity. In Japan for example, such arrangements have been permitted in the steel, aluminum smelting, ship building and various chemical industries.

Public cartels were also permitted in the United States during the Great Depression in the 1930s and continued to exist for some time after World War II in industries such as coal mining and oil production. Cartels also played an extensive role in the German economy during the inter-war period. International commodity agreements covering products such as coffee, sugar, tin and more recently oil (OPEC) are examples of international cartels with publicly entailed agreements between different national governments. Crisis cartels have also been organized by governments for various industries or products in different countries in order to fix prices and ration production and distribution in periods of acute shortages.

In contrast, private cartels entail an agreement on terms and conditions that provide members mutual advantage, but that are not known or likely to be detected by outside parties. Private cartels in most jurisdictions are viewed as violating antitrust laws. Cartel enforcement is the core priority of anti-trust laws, it is vital that the Competition Laws involve effective and speedy cartel enforcement. No aspect of anti-trust enforcement is more important than the fight against cartels.

There is no denying fact that cartels inflicts tremendous harm on economy of any nation and the said conduct of cartelists could not bring any efficiency in the trade & commerce and should not be justified on any ground whatsoever. Time and again various Courts described: collusive behavior of Business Houses as "the supreme evil of antitrust." All the business activities of the trade & commerce including mergers, amalgamations etc. should be analytically evaluated in order to assess the effects of the said mergers & amalgamations and the said activities must promote the healthy competition vis-à-vis which could substantially lessen the competition or create a monopoly. Though it is often difficult to reveal the difference between good, hard competition and anticompetitive conduct, but the Competition Laws should be equipped to challenge conduct that is harmful to competition.

There is now significant global consensus that cartel enforcement deserves our most focused attention. Especially for countries, that have taken up antitrust enforcement relatively recently, there can be no sounder way to develop a strong competition culture than to place primary emphasis on cartel enforcement, through which Consumers will benefit. Businesses that rely upon commodity inputs will benefit. Taxpayers and governments will benefit when bid-rigging is curtailed with effective regulations.

## 1. IMPORTANCE OF HEALTHY COMPETITION

Healthy competition in markets leads to efficiency, encourages innovation, improves quality, boosts choice, reduces costs which subsequently increases the operation efficiency of the business units interalia resulting in reduction of prices of goods and services for the masses. It also ensures availability of goods and services in abundance of acceptable quality with specified standards at affordable price. It is also a driving force for building up the competitiveness of the domestic industry: businesses that do not face competition at home are less likely to be globally competitive. There are lots of examples available in our domestic industry which confirms, if the respective Industry/ Corporate is not competitive in India then, that respective Industry/ Corporate could not be competitive in global arena too and slowly that respective Industry/ Corporate would be forced to be wiped out from the market.

Competition ensures freedom of trade and prevents abuse of economic power and thereby promotes economic democracy. Thus, competition in markets is benign for consumers, business houses and economy as a whole. Past examples of license raj and negligible competition is still alive in the human memory where consumers were paying the exorbitant price for the various products and that too with no surety of supply of products on time viz. delayed delivery and huge bookings of Bajaj Scooters and Maruti Cars in seventies and eighties is still fresh on human memory box.

The absence of fair and free competition, however, eludes the stakeholders from the benefits of competition. The need to sustain fair and free competition has persuaded countries to either enact their competition law or to modernize their existing competition law and to revamp Competition Authorities.

## 2. BRIEF OF THE COMPETITION ACT

In line with international trend and to cope with changing realities, India reviewed the Monopolies and Restrictive Trade Practices Act, 1969 and has enacted the Competition Act, 2002. The Central Government has also established the Competition Commission of India in November 2003. The duties of the Commission are: -

a) to eliminate practices having adverse effect on competition;

b) to promote and sustain competition; and

c) to protect the interests of consumers and ensure freedom of trade carried on by other participants, in markets in India.

One of the core enforcement areas of the Act on its being made effective is "Prohibition of Anti-Competitive Agreements" having appreciable adverse effect on competition (AAEC) in markets, in India". The AAEC is a key factor before an agreement is dubbed as 'anticompetitive agreement' and declared void. 'Agreement' includes any arrangement or understanding or action in concert :-

i) whether or not such arrangement, understanding or action is formal or in writing; or

ii) whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings.

Thus, 'agreement' need not be in writing, not necessarily to be legally enforceable and an arrangement or understanding is as good as a formal written agreement. The necessity to include any arrangement or understanding within the purview of an agreement has been aptly described by Lord Denning in the case of RRTA v. W.H.Smith and Sons Ltd.,namely:

*"People who combine together to keep up prices do not shout it from the housetops. They keep it quiet. They make their own arrangements in the cellar where no one can see. They will not put anything into writing nor even into words. A nod or wink will do. Parliament as well is aware of this. So it included not only an 'agreement' properly so called, but any 'arrangement', however informal"*

## 3. ANTI COMPETITIVE AGREEMENTS:

The "anti-competitive agreements" as per the Act, are of two kinds; namely

**(i)** those agreements which are presumed to have appreciable adverse effect on competition (AAEC). These primarily include:

a) directly or indirectly determines purchase or sale prices;

(b) limits or controls production, supply, markets, technical development, investment or provision of services;

(c) shares the market or source of production or provision of services by way of allocation of geographical area of market, or type of goods or services, or number of customers in the market or any other similar way;

(d) directly or indirectly results in bid rigging or collusive bidding, shall be presumed to have an appreciable adverse effect on competition

**(ii)** those agreements which shall in contravention of Section 3(1) of the Competition Act, 2002, if such agreement causes or is likely to cause an appreciable adverse effect on competition in India. These include tie-in arrangements, exclusive supply agreement, exclusive distribution agreement, refusal to deal and re-sale price maintenance.

'Cartels' are included in the category of agreements, which are presumed to have appreciable adverse effect on competition. The term 'Cartel' is explicitly defined in the Act as:-

*"Cartel includes an association of producers, sellers, distributors, traders or service providers who, by agreement amongst themselves, limit, control or attempt to control the production, distribution, sale or price of, or , trade in goods or provision of service."*

The three ingredients to constitute 'Cartel' are:-

(a) an agreement which includes arrangement or understanding;

(b) agreement is amongst producers, sellers, distributors, traders or service providers i.e. parties are engaged in identical or similar trade of goods or provision of service, and

(c) agreement aims to limit, control or attempt to control the production, distribution, sale or price of, or, trade in goods or provision of services.

Ideally, competition law seeks to promote, maintain and sustain competition in market being beneficial to various stakeholders in society. In case of 'Cartel', competitors agree not to compete on price, product, customers etc. since in the case of a Cartel, direct competitors agree to forego competition and opt for collusion, the consumers and business houses lose the benefits of competition. Thus, cartels are prima-facie harmful to trade and commerce.

Further, competitors know that such an agreement is unlawful and it compels them to keep such agreement secretive and resultantly it is invariably not reduced to writing and it is often found to be in the form of arrangement or understanding. Moreover, the best evidence against 'Cartel' is usually in possession of the charged parties, which are not likely to easily part with and make available to the investigator or enquiring authority.

These compulsions seem to have persuaded the law makers to prescribe that 'Cartel' is presumed to have AAEC.

## 4. WHAT MAKES IT CONDUCIVE TO CARTELIZE:

A group of companies or countries which collectively attempt to affect market prices by controlling production and marketing. Small number of firms in an industry, high concentration, barriers to entry, low technological advancement, identical products, strong

ability of competing firms to exchange information on price and other terms of sale, uniformity in cost or efficiency, severe punishment which can be inflicted on the cheater, and effective trade association etc. make it conducive for firms to cartelize and to continue as such on a long term basis. The less fear of detection and punishment also encourages firms to cartelize.

## 5. DAMAGE CAUSED BY CARTELS

There is worldwide recognition and consensus that Cartels harm consumers and damage economies. Fighting cartels is one of the most important areas of activity of any competition authority and a clear priority of the Commission. Cartels are cancers on the open market economy, which forms the very basis of our Community. By destroying competition they cause serious harm to our economies and consumers. In the long run cartels also undermine the competitiveness of the industry involved, because they eliminate the pressure from competition to innovate and achieve cost efficiencies.

Recent anti-cartel actions of the Commission and other competition authorities clearly demonstrate that in spite of our efforts cartels continue to exist. Moreover, since by nature cartels are secret and therefore difficult to uncover, it is likely that what we are seeing is only the tip of the iceberg. In the words of Adam Smith there is a "tendency for competitors to conspire". This tendency is of course driven by the increased profits that follow from colluding rather than competing. The Regulatory Agencies can only reverse this tendency through tough enforcement that creates effective deterrence. The risk of being uncovered and punished must be higher than the probability of earning extra profits from successful collusion.

In India too, cartels have been alleged in various sectors, namely cement, steel, tyres, soft drinks, soda ash, bulk vitamins, petrol etc. All these tend to raise the price or reduce the choice of consumers. The business houses are affected most by cartels as the cost of procuring inputs is enhanced or choice is restricted making them uncompetitive, unviable or be satisfied with less profits. It is in these backdrops that "Cartels" are considered as most serious competition infringements and supreme evil of antitrust. Infact, Cartels are termed as in violation of competition law. Further, developing countries are affected more either due to absence of competition regime or inadequate capacity to detect, discover and prosecute domestic as well as overseas cartel.

## 6. LENIENCY PROGRAMME:

*An increasing number of Competition Authorities operate leniency programs sometimes also called immunity or amnesty program, as a key tool to detect cartel infringements. In criminal law, there is a provision for pardon, wholly or partly, in respect of offences perpetrated, if the guilty admits the offence and turns as an Approver to bring home the guilt of others.*

One key area in which governments have developed enforcement procedures for the detection of cartels has been the development and use of corporate **Amnesty Policies**. As amnesty policies were developed in multiple jurisdictions, it became clear that unification in effective policies was needed. Over time, we learned that occasionally members of international cartels did not apply for amnesty in one jurisdiction because they had greater exposure in another jurisdiction that did not have a transparent and predictable amnesty policy. Recent convergence in amnesty policies in multiple jurisdictions, however, has led to many simultaneous amnesty applications, which has enhanced enforcement by providing opportunities for coordinated raids, interviews etc.

**The Competition Commision's : Leniency Program cum Amnesty Policy should become the cornerstone of our anti-cartel enforcement program. It has led to the detection and prosecution of more cartels than all of our search warrants, consensual monitoring, and interrogations combined.** Because cartel activities are hatched and carried out in secret, obtaining the cooperation of insiders is the best, and often the only way to crack a cartel. Obtaining the cooperation of knowledgeable insiders at an early stage of an investigation may shorten an investigation by many months, if not years. This saves scarce government resources, leads to the earlier termination of cartels, allows conviction of defendants that might otherwise never be prosecuted, and assists in securing recovery for the victims of the crime.

Through the years, we have faced the deficiencies in our amnesty program and revised it to make it more effective. An increasing number of Competition Authorities operate leniency programs (sometimes also called immunity or amnesty program) as a key tool to detect cartel infringements. In criminal law, there is a provision for pardon, wholly or partly, in respect of offences perpetrated, if the guilty admits the offence and turns as an Approver to bring home the guilt of others.

On the basis of criminal law, when a member of Cartel breaks the rank and make full, true and vital disclosures which results in bursting the 'Cartel', the Commission has been empowered to levy lesser penalty. The scheme is designed to induce member of a Cartel to defect from the Cartel Agreement. The party making disclosure will, however, be subject to other directions of the Commission as per provisions of the Act. The Act does not provide for any incentive to a whistleblower, which can perhaps be considered after sufficient experience in the enforcement of law is gained by the Authority. Clarity, certainty and fairness are critical to make leniency program effective and for this Commission can take suitable measures including formulation of Guidelines etc.

## 7. **EFFECTIVE PENALTY**:

Penalty is key to enforcement and penalty is effective if it is successful in producing a desired or intended result. The "Cease & Desist " order is based on reformative theory which in present time has not been found sufficient to discourage a wrongdoer party to discontinue or not to recur objectionable trade behaviour. Hence, the need to empower the Commission to impose penalty on those found to be contravening the Act, is imperative.

The 'retributive theory' stresses the principle of proportionality (an eye for eye). The 'utilitarian theory' focuses on special deterrence and general deterrence. An economic approach to deterrence assumes that in the area of competition law, the potential offenders conduct a cost-benefit analysis in order to see whether it is worth taking the risk of being caught and punished. Thus, an effective penalty is one that takes into account the financial gains perpetrated by the offence as well as the probability of the detection.

Taking a cue from the economic approach, the Act empowers the Commission, in case of cartel, to impose upon each producer, seller, distributor, trader or service provider included in cartel, various kinds of penalties in accordance with the Chapter VI: Sections 42 to 48 of the Competition Act. In Section 43A of the said Act, penalty which may extend to one percent of the total turnover or the assets is linked with profits made, or turnover of cartel whichever is higher. There will be no incentive to cartelize only if every cartel (be it domestic or international) is detected, prosecuted and penalty is imposed and recovered which is almost unattainable as per global experience. Recognizing that detecting and punishing every cartel is difficult, competition authorities in different jurisdictions supplement and complement penalties with the following:-

(i) imposing penalties on individuals in personal capacity and ensuring that penalties deposited by them are not reimbursed by the defaulting corporate entities;

(ii) Sentencing individuals to prison;

(iii) Declaring directors of errant companies to be disqualified for appointment as 'director' for a specified period, and

(iv) Publishing the order in the media, which seriously damages the reputation of companies found to have 'cartelized'.

**8. Some kinds of Cartels:**

**(I) Cartels in Public & Society Interest , Sovereign Cartels definitely needs special treatment and needs to be exempted from the purview of strict enforcement provisions of Competition Laws:**

(a) As it is universally known, OPEC's objective is to coordinate and unify petroleum policies among the member countries to secure fair and stable prices for petroleum producers, an efficient economic and regular supply of petroleum to consuming nations and a fair return on capital to those investing in the industry. Very few major Sovereign Cartels exist; the most prominent example is OPEC, a cartel which can not be considered illegal because it is made up of sovereign states, not companies, hence need to be protected from the provisions of Competition Laws.

(b) **Levying of Prepayment Charges on the prepayment of amount of Home Loans taken from various service providers in vibrant market :**

Few complaints were made to the Competition Commission of India (CCI) under section 19(1)(a) of Competition Act against 16 banking and non banking financial companies (Banks) for the levying of Prepayment Charges on the prepayment of amount of home loan taken. In their complaints, it was pleaded before the CCI that apart from discontinuing these charges and a detailed investigation by the DG, a fine to be levied on all these Banks upto 10% of their average turnover for the last three preceding financial years.

The Director General (DG) investigated this issue and had summoned 16 Banks including SBI, ICICI, HDFC, PNB and others. The CCI with majority judgment held:

"This is a multi-dimensional case involving macro- economic as well as consumer issues. We have, therefore, identified and determined the issues in this case very carefully within the four walls and boundaries laid down by the Act. It is evident from our analysis and determination of these issues earlier in the order that there is a vibrant market in provision of home loans, with the number of service providers and the variety in products growing consistently and continuously over a period of years. There is no Banks/ Housing Finance Companies (HFC) in the market which can be deemed to be dominant by any of the parameters used for determining dominance. The question of abuse of dominance, therefore, does not arise. It is equally clear that there is no agreement amongst the various service providers i.e. the banks/HFCs, nor is there any uniform practice being followed by them. They are operating as competitors in a vibrant competitive market. Neither the violation of Section 3 or Section 4 of the Act has been established, nor is there any evidence whatsoever of an appreciable adverse effect on competition in the home loan market in India in this context".

The said CCI's majority judgment is encouraging because it demonstrates a sound understanding of the principles of competition law. The order shows that the CCI is unafraid to take decisions that might be unpopular or be considered anti-consumer, as long as these

decisions are well-reasoned, founded in competition law and arrived at after a detailed consideration of the evidence on record. This decision therefore sends a positive message to business and industry that the CCI will take decisions keeping in mind the larger macroeconomic consequences of their orders, and the "aam aadmi" rhetoric of the CCI will not automatically translate into pro-consumer decisions when the same are not merited.

The decision reinforces the fact that the CCI should be, and is, focused only on competition law concerns and does not wish to take on the role of a price regulator or step on the turf of other regulators, such as, the Reserve Bank of India, or Consumer Courts. This should also help allay some of the concerns of the banking sector who have been clamouring for an exemption from the applicability of the Competition Act to their sector, at least for mergers and acquisitions.

Ultimately, these type of cartels of Prepayment Charges on the prepayment of amount of home loan taken levied by various service providers viz. Banks/ HFCs in vibrant market should be outside the purview of penal provisions of Competition Laws.

But, recently again the Indian Regulator: Reserve Bank of India is making elaborate provisions with Indian Banking Industry that Prepayment Charges on the prepayment or foreclosure of amount of home loan should be discontinued and not imposed on the consumers of Home Loan in future.

**(II) Cartels in Consumer Industries**

In number of FMCGs and principal companies that comprises of soft drinks, toiletries, multiplexes, cement, grain, meat, dairy and other food production items, and the processing and distribution system of food, all the way to the supermarket, very little of these products moves on the face of the earth without the undeclared cartel having a hand in it.

These kinds of cartels of need an appropriate action from the Regulatory Agencies in accordance with the provisions of Competition Laws.

## 9. DETECTING CARTELS

The fight against Cartel is legally and practically a demanding task as:-

Cartels being secretive and therefore the cartelists use to conceal it, which necessitates the Competition Authorities to undertake great efforts to detect concealed cartels through extraordinary powers and skill to collect sufficient evidence to make a viable case against uncooperative defendants cum cartelists. These Cartels are conspiracies and to destabilize them, Competition Authority needs to heavily bank upon "Leniency Programme" or to encourage and motivate whistleblowers. Overseas cartels are always subject to territorial restraint and constraint in the investigation and enforcement. In order to penalize the cartel conduct, Competition Authority need to have high standard of proof and procedure.

Cartel busting requires certain specialist skills which differ from the skills required for investigation and prosecution of other infringements of competition law. In case of cartels the focus lies on proving the existence of the arrangement itself rather than demonstrating its impact on the market in economic terms. An increasing number of Competition Authorities, therefore, have set up special cartels branches and the motivation to do so is to develop centres of excellence with respect to expertise required in organizing search and raids, interviewing witnesses, covert surveillance beside successful implementation of leniency programmes. There is an obvious need for intensive & extensive coordination and cooperation with other

specialized agencies such as sector specific regulatory authorities, tax authorities, police, and ministries dealing with corporate bodies.

Under the Act, the Commission, in discharge of its functions has been vested with powers as are in a Civil Court which inter-alia includes; namely –

(a) summoning and enforcing the attendance of any person and examining him on oath;

(b) requiring the discovery and production of documents;

(c) receiving evidence on affidavits; and

(d) issuing commissions for the examination of witnesses or documents

The Director General including any person investigating under his authority is also having powers inter-alia include –

i) production of documents and evidence in the custody of body corporate/other bodies corporate, and

ii) search of place or places and seizure of documents with the approval of the First Class Magistrate/Presidency Magistrate, having jurisdiction, when there is reasonable ground to believe that books, papers or documents may be destroyed, mutilated, altered, falsified or secreted.

Organizing 'search, seizure, raids' is a science as well as an art and its efficacy and success hinges upon constitution of team, coordination with other agencies and if it is made unannounced and is without mandate of a Court. Further since evidence is increasingly stored electronically, the availability of IT skill is also essential requirement to achieve success out of searches etc. Thus, the need for and usefulness of requisite capacity building to undertake "Search and Seizure" is inevitable to make meaningful use of these provisions in detecting 'Cartels'. It may need reliance on circumstantial evidence.

## 10. CONCLUSION

The availability of explicit definition of 'Cartel', incorporation of a leniency programme for a member of a cartel to defect, the power to impose deterrent penalty linked with profits or turnover on each member, explicit provisions to exercise jurisdiction in respect of overseas acts having adverse effects on competition in India coupled with provisions to enter into cooperation agreement with contemporary overseas competition agencies along with efforts to build strong competition culture including encouragement to public to submit information by ensuring confidentiality, coordination with Government Departments & sectoral regulators and by stressing the need for strong sanctions in view of irredeemable harms caused, the Competition Commission will be able to effectively combat domestic as well as cross border cartels.

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