LEGAL AND POLITICAL SCIENCE

CARTEL AGREEMENTS

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ABSTRACT

This article points out the aim and purpose of the competition law in the European Union. Competition law is one of the most crucial and essential part of law that has to be implemented properly to support and ensure smooth functioning of the economy in the state. At the same time, brief explanation of the most anticompetitive agreements such as called "Cartel Agreements" are being described in the article. It is worth to point out the most important and restrictive types of agreements in details that can be seen on the market and within the European Union, that definitely needs special attention by the relevant competition authorities of the Member States.

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Introduction. Competition is a one of the most important and fundamental mechanisms of the economy, which is considered to be an essential factor for economic growth and prosperity. The primary goal of competition law is to remedy some of the situations in which the free market system collapse, simultaneously it has to ensure effectiveness of competition, prohibit any kind of agreements restricting free trade or competition between companies. It helps consumers get a good price and encourages firms to innovate by reducing slack; putting downward pressure on costs, it is a central driver for a productivity growth in the economy. Article 101 (81EC) of the treaty on the functioning of the European Union prohibits cartels and other agreements that could disrupt free competition and sets it out in following terms: "All agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the internal market, and in particular those, which directly or indirectly fix prices, limit or control production, share markets or sources supply"[1]. One of the most contentious and important aspects of competition law and policy in Europe and even beyond in recent years has been the regulation of what are now described as cartel violations[2]. Nowadays cartel agreements are becoming more and more problematic and breaking up this kind of unlawful agreement is a crucial part of the competition policy in most countries. Cartel is an explicit agreement among group of legally and economically independent companies or firms to fix prices limit supply, cooperation and competition, to restrict output and to raise prices of the product in order to make a profit[3]. Adam Smith had quoted that "people of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a

[1] The Treaty on the Functioning of the European Union, Art.101(81 EC)
[2] Christopher Harding and Julian Joshua, *Regulating Cartels in Europe*, (Second edition,2010) 1
[3] Simon Bishop and Mike Walker, *The Economics of EC Competition Law, (*University edn, Thomson Reuters Limited, 2010) 163

conspiracy against the public, or some contrivance to raise prices."[1] In general, cartels are not economically stable and don't last for a long time, as the studies have discovered that the mean duration of cartels is from 5 to 8 years.

Types of Cartel Agreements. There are various types of cartel agreements to which competition can be restricted through: 1) price-fixing; 2) Market Sharing; 3) Collective Boycotts; 4) Exchange of Information; 5) Bid Rigging[2]; Price-fixing is an illegal agreement between companies in order to maximum or minimum prices to sell or buy goods. Mostly it leads to high prices to gain profits. This benefits all businesses or individuals that are on the same side of the market, but companies also try to fix the common target price that can be advantageous for them. There have been a lot of cases concerning price fixing between companies, but firstly only one case will be pointed out in order to have an idea how price fixing occurs between different firms. In 2007 The European Commission imposed a fine to Heineken Company (€219.3m), Grolsch (€31.65m) and Bavaria (€22.85m) for creating a cartel agreement on price fixing. These companies controlled 95% of the Dutch market and tried to carve up markets among themselves. Companies tried to fix prices, remain high positions in market restricting competition and were fined for such collusion[3].

Market Sharing is agreement between companies by which competitors divide up a market, customers, territories or the products and agree not to enter each other's territory. Market Sharing agreements are particularly restrictive of competition and contrary to the benefit of single market. Agreements for the purpose of market-sharing are generally based on the principle of mutual respect of the national markets of each member state for the benefit of producers resident there.[4] The case between *SAS/Maersk* gives an idea of market sharing agreement. The market sharing agreement was from 1998 to 2001, the companies agreed on the monopolization by SAS of the Copenhagen-Stockholm route, harming more than million passengers. The illegal activity included SAS paying money to Maersk Company in order to get the specific route. Commission imposed fines of €52.5 million for market sharing in the air transport sector.[5]

Collective Boycotts is considered to be one of the most damaging, corruptive violations of competition law. It includes refusal by a group of competitors to deal with one or more customers or suppliers which is not part of "them"[6]. Collective boycott might also include refusal to supply some customers in order to make Competitor Company adopt a certain course of conduct. Such practices violate competition policy and breaches article 81(1). These kinds of cartel agreement cases are few, but one of the most famous cases is about Netherlands insurance company, which tried to prohibit its members from concluding re-insurance contracts with non-members. This type of action was considered as restriction of competition and Commission asked the association to change the rule.

Exchange of information between companies regarding on production, prices charged, capacity, confidential information concerning the identity and solvency of costumers and conditions applied to them may exist and take place within cartels, which does prohibit article 81 of EC[7]. It does play role of ancillary to other per se violations such as price fixing or market sharing. It can be divided in two categories: 1) exchanging information that support collusive practices such as price fixing; 2) Exchanging information that are not coupled with other collusive behavior, which will still infringe Article 81 (1), if it restricts the competition[8]. The debate on the exchange of the information between competitors under EC competition law is still one of the most controversial of the last years. The leading case on the exchange of information remains UK Agricultural Tractor Registration Exchange case, where eight manufacturers and importers of tractors exchanged information identifying volume of retail sales and market shares[9]. Commission concluded that a detailed exchange of sensitive information in a market, which is not exposed to other competitors, increases the likelihood of collusive outcomes on the market and infringes Article 81 of EC.

[1] Cartels, Jeffrey M. Perloff, *cartels: bad and ubiquitous*, P.1
[2] Van Bael and Bellis, *Competition Law of the European Union*, (Fifth Edition, 2005) 344
[3] Eur-lex.europa.eu, official journal, case Bavaria v European Commission, OJ 2011, C226/23
[4] Commission's 1st Report on Competition Policy (Commission, 1971), para.2.
[5] Alison Jones and Brenda Sufrin, *EU Competition Law*, (Fourth Edition, 2011) 812
[6] Van Bael and Bellis, *Competition Law of the European Community*, (Fifth Edition, 2005) 378
[7] Faull and Nikpay, *The EC Law of Competition*, (Second Edition, 2007) 772
[8] Van Bael and Bellis, *Competition Law of the European Community*, (Fifth Edition, 2005) 382
[9] Eur-lex.europa.eu, official journal, case UK Agricultural Tractor Registration Exchange, OJ 1992 L68/19

Bid Rigging occurs when companies collude on the bids and decides beforehand who should win the tender; instead of participate in real competition. Bid rigging almost always results in restricting competition, harming economy and is considered as violation of Competition law. There are different types of bid rigging practices: 1) Cover bidding; 2) Bid suppression; 3) Bid rotation; 4) Market allocation[1].

Obviously cartel agreements are becoming one of the biggest problems of competition policy and it is important to concentrate more on price fixing and market sharing agreements afterwards and illustrate how it is becoming problematic and the most common ways to restrict and violate competition.

The two most common types of cartel agreements. The most obvious type of price-fixing is between companies when they fix sale prices and increase profits.[2]. One of the biggest price fixing agreements could be seen in the case of *Elevators and Escalators,* where infringements were committed in one, several or All of the MS concerned (Belgium, Germany, Luxembourg, Netherlands).[3] Parties agreed to fix prices, agreed not to compete with each other and exchanged confidential information as well. As we see this is the case involving different types of illegal agreements that's why Commission imposed fine of 990 million euros on four groups of companies for infringing Article 81 (1) of the EC treaty by creating cartels for the installation and maintenance of elevators and escalators. In the case of *Cartonboard*[4]*,* where one of the biggest fine was given to majority producers of Cartonboard made up a scheme, which involved not only price fixing, but market sharing, exchanging information and limiting production as well. They tried to benefit by managing price comparing to other Member State and increasing number of customers, leaving them without other alternative sources. This agreement did not harm only customers but trade between Member States as well. Commission fined 19 Undertakings for planning and implementing price increases, as they agreed on regular price, sharing market, planning to restrict competition as setting up common industry plan and exchanging commercial information.

Agreements to implement price increases can be seen in the case of *Rubber Chemicals,* where 3 major producer Flexsys, Bayer, Chemtura and five significant rubber smaller companies agreed to raise price for specific rubber chemicals from 1996 to 2001[5]. They were implementing price increases and its amount focusing on customers' reaction and exchanging on the positions regarding price negotiations with the customers. Investigation started after Flexsys was granted immunity in 2002. Undertakings were fined because of infringing Article 81 (1) of the Treaty and Article 53 of the EEA Agreement, but Commission took into account gravity, its impact on market and duration.

Fixing purchase prices normally infringe Article 81 (1) EC too, because it does restrict the ability of the parties to purchase individually at different prices. In the case of *Italian Raw Tobacco and Raw Tobacco Spain*[6]*,* raw tobacco processors agreed at purchase price, which should be paid to tobacco growers in both countries, such way they managed to align as closely as possible their purchasing prices of tobacco and reduce them, to their own benefit. The commission emphasized that the 'purchase price is a fundamental aspect of the competitive conduct of any undertaking operating in a processing business and is also, by definition, capable of affecting the behavior of the same companies in any other market in which they compete, including downstream markets'[7].

Discounts does play an essential role in price competition, as it entices people to go to special companies and get service or buy a specific product from them. Agreements fixing discounts are prohibited by Article 81 (1). In the case of *FETTCSA* [8](Far East Trade Tariff Charges and Surcharges Agreement) 15 liner shipping companies agreed not to grant discounts. On the meeting held in 1992, parties agreed they would no longer grant discounts off the rates for 'additionals'. Parties claimed that they did not mean to stop offering discounts but to stop charge 'net all-in' rates. In the decision Commission stated that an agreement not to grant discounts reduces the ability of lines to compete with regard to final price charged to shippers, it does affect overall price and all this amounts to a restriction of price competition. Commission

[1] OECD Guidelines for Fighting Bid Rigging in Public Procurement, p.2
[2] John M. Connor, *Global Price Fixing,* (Kluwer Academic Publishers, USA, 2001) 21
[3] Eur-lex.europa.eu, official journal, case Elevators and Escalators, OJ 2008 C75/19
[4] Eur-lex.europa.eu, official journal, case Cartonboard, OJ 1994 L 243/1
[5] Eur-lex.europa.eu, official journal, case Rubber Chemicals, OJ L353/50
[6] Eur-lex.europa.eu, official journal, case Raw Tobacco Italy, OJ 2006 L353/45
[7] Van Bael and Bellis, *Competition Law of the European Community*, (Fifth Edition, 2005) 355
[8] Eur-lex.europa.eu, official journal, case FETTCSA, OJ 2000 L 268/1

decided that Undertakings agreed such provision constituted an infringement of the Article 81 (1) of the EC Treaty and fined fifteen liner shipping company.

Resale price maintenance is dealt with within the framework of Article 81 (1) EC, because it generally concerns multilateral behavior by undertakings. An agreement between companies concerning a common resale policy is also chastened by the Commission. In Case VBBB/VBVB, decision has met a lot of criticism because many MS supported the use of RPM in the market. Two associations had agreed that books could not be sold in Belgium or the Netherlands at a price below fixed price set by the publishers. Parties claimed that RPM scheme was done in order to improve production and distribution of goods, but Commission considered that "any objective advantages which might derive from the agreement are outweighed by its disadvantages from the viewpoint of competition".[1]Parties also claimed that RPM scheme did not eliminate competition as not all publishers took part in the collective system, but Commission found this agreement to infringe Article 81.

Delivery charges do play an indispensable role calculating price of product and is an important key element of price competition. Agreements on unfair delivery charges constitute infringement of Competition law. In the case of *Glass Containers,* a system of delivery set up by undertakings was condemned by the Commission. The manufacturers of glass containers adopted free delivery system in June 1966, stating that 'The free delivered price is the price of the goods plus average transport costs. This system makes it easier to sell products[2]'…. This system of delivery charges free applied by the parties to the exclusion of any other price system consists in applying, within a determined area and it does not reflect actual cost of transports of goods from place of origin to destination. It cuts any competitive advantage to other glass container, which can make profits from the proximity to his costumers. It does make only distant costumer in better position as the nearer customer pays higher price. System did not treat all customers in the same way and violated competition between undertakings and the users of glass containers. Commission found 24 undertakings constituting infringements of the provisions of Competition law.

A market sharing agreement in its various forms, which has increasingly attracted the attention of the competition policy, is prohibited by the Article 81. In a market-sharing agreement competitors divide up markets in different ways, such as geographical area, size or type of customer and agree to sell only to their allotted segment of the market. As a result, they restrict competition and don't even compete each other. It involves non-price and quota agreements as well[3]. In the report Irish Competition Authority noted that an alternative to a price-fixing cartel, companies can achieve some effect by dividing up the country between and agree not to sell in each others designated area, which brings us to anticompetitive agreement such as market-sharing. In its fist report on commission policy the commission noted that 'Market sharing agreements are restrictive of competition and contrary to the achievement of a single market."[4] Common types of Market-Sharing are: 1) geographical market-sharing; 2) allocation of customers or products; 3) limitation of products or sources of supply;

Geographical market sharing does obviate the cartel members to monitor, agree and enforce prices collectively, instead of limit their presence to a specific territory. Sometimes this type of market sharing agreement might be used by countries in order to protect their home markets as well. In the case of *E.ON/GDF*[5], the commission imposed fines totaling 1.106 billion euros on E.ON AG (German) and its subsidiary E.ON Ruhrges and GDF Suez SA (France) for market-sharing in breach of the rules on cartels and restrictive business practices, Article 101 of the TFEU. After deciding to build jointly the MEGAL pipeline across Germany to import Russian gas into France and Germany, Companies agreed not to sell gas on each other's home markets. They maintained this market-sharing agreement even after European gas markets were liberalized and did not abandon it at least until 2005. The main subject matter of the commission decision was the agreement for concerted practice not to enter each others market. Introducing with the first gas Directive[6], companies still met regularly and discussed implementation of the agreement. This anticompetitive agreement helped companies to

[1] Eur-lex.europa.eu, official journal, case VBBB/VBVB, OJ 1982 L54/36
[2] Eur-lex.europa.eu, official journal, case Glass Containers, OJ 1974 L160/1
[3] S.P.S Chauhan*, Microeconomics,* (*Part II, 2009)97*
[4] Ivo Van Bael, Jean-Francois Bellis, *Competition Law of the European Community*, (Third Edition, 2005) 812
[5] Eur-lex.europa.eu, official journal, case E. ON/GDF, OJ 2009, C248/5
[6] Directive 98/30/EC of the European Parliament and of the Council of 22 June 1998 concerning common rules for the internal market in natural gas

maintain strong positions on gas markets. Having such kind of agreement, the commission found that parties conduct continued infringement and restriction of competition by violating Article 81. The commission denied parties claims on the basis that both companies were perfectly aware that they were infringing competition law and could not invoke any uncertainty. Determining final amount of the fine, the commission took into consideration nature of the infringement, the combined market share and the geographical scope as well and it totally reached to EUR 1.106 billion as case reflected the very large size of the market affected by the agreement and duration of it.

Article 81 (1) (b) EC expressly prohibits any kind of agreements that limit or control production, markets or investment. Since the price of a product is a function of output and demand, a restriction in output by producers will affect prices. It is not surprising that parties also agree to limit production in order to support their price objectives. This kind of agreement allocating production quotas among competitor firms has been condemned by the community.[1]Market sharing can also take the form of customer specific measures. This may consist of allocating them and dividing them between companies. Mostly competitors try to agree to keep their own customers, constituent infringement of Article 81 of EC. In the case of *Flood Flavour Enhancers*[2], there was an agreement outlining customer allocation between four undertakings. Participants in cartel agreement not only allocated the customers, but they also fixed prices and implemented price increases as well. Procedure against anticompetitive agreement started on 9 September 1999, when Japanese company Takeda filed an application pursuant to the commission notice on the non-imposition or reduction of fines in cartel case by informing the commission about existing cartel. Members met and discussed general trends on the nucleotides market, share information on prices and discussed allocation between the manufacturers. During 1990 the European market was largely made up of three large industrial users, which together accounted around 50% of nucleotide demand in Europe. In this case, agreement involved customer allocation, as Takeda and Ajinomoto agreed not to sell to each other's respective European customers, in order to protect their sales. They also had an agreement with Korean competitors to buy nucleotides from them, in exchange of Korean firms would not sell product to the European "big three." As we see customer allocation scheme lead to the allocation of markets on a worldwide and restricted their individual commercial conduct. This agreement had the object and effect of restricting competition in the community, infringing Article 81 of EC. As competition law also prohibits control of investment, in the case of *French beer*[3], which concerns the sales of beer in France in trade sector, was so called "armistice" agreement, with the aim of establishing equilibrium in the market between 2 companies. They wanted to control acquisition of wholesalers, balance distribution and agreed to a temporary acquisition stop, balancing volume of beer distributed through the network of each party and balancing of the volume of beer brands. As the aim of agreement was to prevent, restrict or distort competition within market by having anticompetitive actions, the commission concluded that it was infringing Article 81 of EC. As cartels are becoming problematic, that's why it should be more interesting to talk about on new settlement procedure, introduced by the commission in order to fight against them by saving up time during investigation and making cartel members to collaborate getting 10% reduction of final fines. It is a new tool for cutting up cartel agreements and trying to eradicate such kind of anticompetitive agreements between companies.

Conclusions. Cartel Agreements are one of the most restrictive agreements for the market and the competition. Anticompetitive agreements play an enormous role in distorting and restricting the free competition on the market. It is obvious that competition authorities of the member states or any state should fight against such restrictive agreements to support economic growth of the country and further development.

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