

Cartelization in the Indian Competitive Market

Lubna Fairoze

Abstract

Competition in markets has slowly been increasing and the same is casting an effect on the Indian as well as international market. Competitors want to scale new heights at a short span of time and hence choose short-cuts to achieve such goals. One such short-cut is cartelization of markets wherein the competitors agree not to compete against each other and agree to work in co-operation with each other thereby leading to unhealthy competition. The same has been discussed extensively under the Competition Act, 2002 in India under Section 2(c). Determination of Cartels is a challenging task for the Competition Commission of India as there is thin line between competition and anti-competitive practices. The anti-competitive nature of cartel agreements has been severely criticized in this article by highlighting the ill-effect of entering into such agreements in the Indian markets. This article discusses the basic features of cartel agreements and the kinds of cartel agreements.

The determination of cartel agreements, the harmful effects of such agreements is also discussed in this article. The need for leniency programmes and the manner in which the Competition Commission of India deals with participants of cartel agreements under the leniency programme has been discussed here. This article further discusses the need of whistle blowers for promoting fair and competitive market in India. The need for criminal liability on par with practices in other countries has been discussed and the same shall have a deterrent effect. This article gives an overview of the cartel agreements that are existent in the market which are causing a negative impact on healthy growth of competition in India. There is a need to curb cartelization in India to gain a good position in the international market and the same is possible through effective implementation of the provisions of Competition Act, 2002.

Introduction

Competition in markets promotes efficiency, encourages innovation, improves quality, boosts choice, reduces costs and also leads to lower prices of goods and services. Competition further encourages freedom of trade and prevents abuse of economic power and thereby promotes economic democracy. Competition espouses the fundamental right to practice any trade and business guaranteed under the Constitution of India.

Anti-competitive practices such as cartels are impediments which curb the competition in Indian markets. The Supreme Court of USA has referred to cartels as “the supreme evil of anti-trust”¹. Sec 2(c) of the Competition Act, 2002 (the Act) states that *"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 services.*

Cartels have been regarded as anti-competitive agreements wherein the competitors enter into collusive agreements in order to control prices, production and supply of goods and services and also control technological advancement in India. Indian markets evidence cartels mainly in the cement, steel, tyre sectors at the domestic level and in petrol, soda ash, bulk vitamins etc at the international level. Cartels tend to increase the price of goods and services and reduce the choice of consumers thereby leading a setback on the consumer's rights and choices.

Under Section 3(3) of the Act, the agreements under which any practice is carried on and under which any decision is taken shall be presumed to have an appreciable adverse effect on competition. Cartels can be at the national level or international level. A cartel can be an export cartel or an import cartel. Cartel agreements may be tie-in agreements, exclusive supply agreements or exclusive distribution agreements or agreements refusing to deal or resale price maintenance which has an appreciable adverse effect on competition. There is a need to curb the cartels by effective implementation of Competition Act, 2002.

¹ Vinod Dhall “*Competition Law Today*”, Oxford University Press, New Delhi (2007)

Basic characteristics of Cartels

- a) Price Fixing : Competitors agree on a pricing structure rather than competing against each other. This is known as price fixing. It is pertinent to mention about the Vitamins Cartel on price fixing by the leading producers of vitamins including Roche AG and BASF of Germany, Rhone-Poulenc of France, Takeda Chemical of Japan formed a cartel dividing up the world market and price fixing for different types of vitamins during the 1990s. The cartel operated for over 10 years and was later prosecuted with the help of Rhone-Poulenc which defected from cartel and cooperated with US authorities. Roche paid fines of US \$ 500 million and total fine collected exceeded US \$ 1 billion in the US alone. The overcharges paid by 90 countries importing vitamins were estimated to the tune of US \$ 2700 million during the 1990s. The analysis also revealed that jurisdictions with weak cartel enforcement regime suffered more. Damage wise, India incurred overcharges of more than US\$ 25 million.
- b) Sharing Markets: Market sharing occurs when competitors agree to divide or allocate customers, suppliers or territories among themselves rather than allowing competitive market forces to work. The Cement cartel practiced by Cement Manufacture's Association (CMA) was brought to the notice of the Competition Commission by Builder's Association of India (BAI) by filing a complaint based on the Sec 19 of the Competition Act of 2002, on 26th July, 2010 against the Cement Manufacturer's Association (CMA) and 11 other major cement manufacturing companies for the alleged violation of the provisions of Section 3 and 4 of the Act (Case 29/2010 before the Competition Commission of India). As per the information in the case before the Competition Commission of India, the Respondent cement manufacturers indulge directly or indirectly into restrictive trade practices in an effort to control the price of cement by limiting the production and indulge in collusive price fixing.

The complainant claims that it is the strategy of the cement companies to divide the territory of India into five zones so as to enable themselves to control the supply and fix high prices. Further the top 11 companies by the virtue of the fact that they collectively hold more than 57% of the market share in India enjoy a position of dominance and arbitrarily increase the price of cement.

The above mentioned case also states that the Builders Association of India has also mentioned that ACC cements and Gujarat Ambuja Cements are the leading cement manufacturers having approximately 21% market share in India. But from Nov 1st, 2009 they have withdrawn the membership from the CMA. But despite having resigned from the membership, ACC and Gujarat Ambuja cement have been successful in keeping their prices per bag similar to that of other cement manufactures. According to the BIA, despite having large capacities, the opposition parties with sole intention to control supply, produce less cement and increase the market price of cement deliberately, the large cement manufacturers have set up the cement manufacturing units at different places in India keeping in view the availability of raw materials, power, coal, etc and accordingly have different costs of production.²

- c) **Bid Rigging** : Bid rigging, also referred to as collusive tendering, occurs when two or more competitors agree that they will not compete genuinely with each other for tenders, allowing one of the cartel members to 'win' the tender. Participants in a bid rigging cartel may take turns to be the 'winner' by agreeing about the way they submit tenders, including some competitors agreeing not to tender. Bid rigging may be cover bidding, bid suppression, bid withdrawal, bid rotation or non-conforming bid.

The competition regulator has imposed Rs 317 Crore in penalties on three companies for collusive bidding to supply aluminium phosphide (ALP) tablets to state-run Food Corporation of India (FCI). After a suo motu probe into the matter by its investigation wing, the Competition Commission of India (CCI) concluded that United Phosphorus Limited (UPL), Excel Crop Care and Sandhya Organics were guilty of the "crudest form of bid rigging" as they repeatedly quoted identical prices for the FCI tenders for ALP tablets during 2002-2009. The anti-competitive agreement among the firms inflated FCI's cost of procuring the tablet used to preserve grains, the CCI noted. The CCI probe also found these companies indulged in collusive bidding in supply of tablets to other government agencies like central and state warehousing corporations.

² Deepika and others, " *Cartel in Cement Industry in India: Is there enough evidence* " (October 2012) <http://amrita.edu/asb/pdfs/workingpaper/Working-Paper-No.133.pdf>

The CCI has imposed penalty of 9 % which was the average turnover of each firm for three years (2008-2011) under the Competition Act, 2002.

- d) Controlling the output or limiting the number of goods and services available to buyers: Output restrictions may also be thought of as supply restrictions. They occur when competitors agree to prevent, restrict or limit the volume or type of particular goods or services available.

Categories Of Cartels

Cartel Members agree on price fixing, total industry output, market shares, allocation of customers, bid-rigging, setting common sale agencies and allocating territories and division of profits or combination of these to gain supernormal profits. Given below are the few types of cartels which are usually practised by enterprises and corporations:³

- a) **Customer Cartels**: Customer cartels allocate customers or suppliers to certain producers.
- b) **Specialization Cartels**: In specialization cartels, members of the cartel assign lines of product or production techniques among themselves. This is basically a non-price oriented strategy involving division of labour.
- c) **Territorial Cartels**: Territorial cartels divide market share by allocating the area geographically.
- d) **Quota Cartels**: Quota Cartels limit the production output of participating members and thus artificially creating supply constraint. This leads to price fluctuations and also excess capacity is left with the firm. However in these cartels, there is greater probability of defection as monitoring is difficult.
- e) **Price Cartels**: In Price Cartels, price is agreed upon among the members and usually an independent agency is created to monitor the compliance of members and hold them accountable.

³<http://www.iitk.ac.in/infoCELL/announce/convention/papers/Industrial%20Economics%20%20Environment,%20CSR-01-Ritu%20Raj%20Arora,%20Runa%20Sarkar.pdf> [retrieved on 25.08.2013]

- f) **Syndicates**: Syndicates usually pose a more united front against firms entering the market and also punish wayward firms.

Cartels under Competition Act, 2002

The Competition Act, 2002 promotes free and fair competition in the markets and cartels are considered as a hindrance to competition. Hence, the Act identifies agreements as cartels, which are executed for fixing of prices, limiting supply of goods or services or technical development, sharing the market and bid rigging. Classes of parties to a cartel agreement under Section 3(3) of the Act are enterprises, association of enterprises, persons or association of persons and they could act in any combination. Cartels result in super-normal profits due to arbitrary and unreasonable pricing of goods and services.

Cartels being the most pernicious form of anti-competitive business agreements may or may not be in writing. Cartels can be an arrangement or understanding and the same is as good as a formal written agreement. Sometimes an agreement may be called apparently by an insignificant name and be in effect of an anti-competitive agreement. What is necessary to examine is the effect of that agreement on competition and not go by its name.

Lord Denning in the case of *RRTA Vs. W.H.Smith and Sons Ltd.*,⁴ inferred that “*People who combine together to keep up the prices do not shout it from the housetops. They keep 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.*”

One of the instances of cartels where there was no agreement in writing is the cartel arrangement that happened at Siem Reap in Cambodia which is a very popular tourist town, which houses the famous Angkor Vat temples. There were three means of transportation from Phnom Penh to Siem Reap – boat, road and air. The competition between boat companies has been intense and the prices came down from US \$ 10 to US \$ 5. The boaters discussed among themselves and resolved that they will charge US \$ 10 from Khmer nationals and US \$ 20-25 from foreigners. They further agreed that they would not compete with each other

⁴ [1969] 3 All ER 1065

and would share their departure schedules. There was no written agreement and only an understanding and it was decided that it constitutes a cartel agreement.

Descrying Cartels

Cartels being anti-competitive practices have to be curbed in order to have a free and fair competition. Competition Authorities have to take measures in order to ascertain and determine cartels. Few aspects of determining cartels may be the following as discussed below:

Evidentiary Proof: The basic problem to establish a Cartel is to bring out the evidentiary proof. Competition authorities require extraordinary skills and talents to collect sufficient evidence against enterprises indulging in and executing cartel agreements. Where one can establish a proof of meeting of minds, the Cartel can be established.⁵ The main focus lies on proving the existence of an agreement or arrangement which has an appreciable adverse effect on competition.

Whistle Blowing: Whistle blowing should be encouraged in enterprises which will facilitate the competition authorities to determine cartels. Whistle blowers should be protected from harassment and victimization at work place. Efforts should be taken to protect their identity so as to enable and encourage other people to reveal any anti-competitive practices of enterprises leading to cartels.

Leniency Programmes: Leniency programmes⁶ shall act as an effective tool for descrying cartels. This scheme induces a member of a cartel to disclose true and vital information which results in busting a cartel. The person making such disclosures will be subjected to lesser punishment by the Commission.

The Commission has notified the Competition Commission of India (Lesser Penalty) Regulations, 2009 laying the process, procedure and methodology for granting leniency to the cartel members who break the ranks of the cartel and become helpful to the Commission and instrumental in busting the alleged cartel.⁷ Further proviso to Section 46 provides for leniency

⁵ Isha Malhotra, Project Report on Price Parallelism and Tacit Collusion with respect to Practices Under Indian Competition Law (retrieved from) <http://cci.gov.in/images/media/ResearchReports/Isha30jan2012.pdf> on 16.07.2013

⁶ Section 47 of the Competition Act, 2002

⁷ For the details of the conditions for lesser penalty please refer to Regulation No. 4 of 2009 dated August 13, 2009 (also available on the CCI website www.cci.gov.in)

programmes. Accordingly, the Commission *may* impose a lesser penalty on a cartel member who makes a “vital disclosure” i.e. information or evidence sufficient to allow the Commission to find *prima facie* that a cartel exists or to help establish the violation of the Competition Act.

Harmful effects of Cartels

Cartels diminish social welfare, create allocative inefficiency, modify output and prices. Cartels are harmful in the long run. Engaging in cartels to avoid the rigours of competition can result in the creation of artificial, uneconomic and unstable industry structures, lower productivity gains or fewer technological improvements and sustained higher prices. Furthermore, the weakening of competition leads to a loss of competitiveness and threatens sustainable employment opportunities.⁸ Prohibition against cartels is a universal component of competition law of most of the countries which is evident from the following reports of various international organisations. The 1998 OECD Recommendation has proclaimed that “Cartels are the most egregious violations of competition law.”⁹

Need for a tougher Anti-Cartel Law

The first question that arises in the domain of cartels is what the general nature and legal basis of cartel prohibition is; civil or criminal? While India and European Union have civil penalties for cartels, UK, Australia and U.S. believe in criminal penalty for the grave offence of cartelization. In fact, Australia has some of the toughest cartel laws in the world and adopted criminal liability on account of the Dawson review of 2003 that suggested criminal sanctions for cartel conduct although subject to resolution of a number of issues.¹⁰

The MRTP Act, 1969 had no provisions regarding the mechanisms for avoiding cartels. Hence the Competition Commission was not empowered to punish the organisations and enterprises indulging in cartels. The MRTP Commission had no provision for avoiding cartels and hence there were trucking cartels which practiced eliminating competition in the market. It was a common scenario in the trucking industry where the freight rates were fixed

⁸ As per EU XXXII Report on Competition Policy-2002.

⁹ Amit Sanduja “*Report on leniency programme : A key to detect cartels*”
http://cci.gov.in/images/media/ResearchReports/leniencyproject_amitsanduja11032008_20080715104637.pdf

¹⁰ Saumya Jhambekar, “*Competition Assesment of Leniency Policies and Introduction to Market System and Amnesty Plus*”
<http://cci.gov.in/images/media/ResearchReports/LeniencyPoliciesIntroductionToMarkerSystemandAmnestyPlus.pdf>

without liberty to the members of the Truck Operators Union to negotiate freight rates individually.

The M.R.T.P. Commission passed 'Cease & Desist' order against Bharatpur Truck Operators Union vide order dated 24.8.1984 in RTP Enquiry No.10/1982, Goods Truck Operators Union, Faridabad vide order dated 13.12.1989 in RTP Enquiry No.13.13.1987 and Rohtak Public Goods Motor Union vide order dated 25.8.1984 in RTP Enquiry No.250/10983. As the MRTP Act was devoid of any penalty provision, no fines could be imposed on the Truck Operators Union which indulged in cartels.

Keeping in mind the hindrance caused in ascertaining cartels and also the absence of penalty provisions in the MRTP Act, provisions were introduced by enacting the Competition Act, 2002 which provides for penalty under Section 27 of the Act. The Commission currently imposes penalty under Section 27 of the Act, based on the profits made or the turnover of cartel, whichever is higher. The Act empowers the Commission to impose upon every producer, seller, distributor, trader or service provider who indulges in cartels, a penalty equivalent to three times of the amount of the profits made out of such agreement by the cartel or 10% of the average of the turnover of the cartel for the last preceding three financial years, whichever is higher.

The Commission under Section 27 of the Act has the power to pass inter alia any or all of the following orders:

- a) direct the parties to a cartel agreement to discontinue and not to re-enter such agreement
- b) direct the enterprises concerned to modify the agreement.
- c) direct the enterprises concerned to abide by such other orders as the Commission may pass and comply with the directions, including payment of costs, if any; and pass such other order or issue such directions as it may deem fit.

The criminal liability structure acts as deterrent but the absence of same in India is a major drawback and hence cartelization is evidently dominant in India. Under the existing penalty regime in India, corporations and enterprises involved in cartels can only be imposed with

pecuniary fines as envisaged in the Act, which most of the enterprises/corporations pay and continue to indulge in cartelization in Indian markets. Penalties fail to act as deterrents to members of cartel.

Australia's recent introduction of criminal penalties for cartel activities has reported an increase in leniency applications ever since the new law came into force. On the contrary, Indian law, in its current form, has not attracted many leniency applications ever since the inception of the Act. There is, therefore, a compelling need to scrutinize the current penalty regime to further deter cartels.

Conclusion

Cartels being anti-competitive agreements are having an adverse effect on competition and this indirectly affects the markets and also the consumers. Though the Competition Act, 2002 contains provisions relating to defining cartels, provisions laying down penalty for organisations indulging in cartels, it is difficult for the Competition Authorities to ascertain cartels. The Competition Authorities are facing difficulties to differentiate between practices that lead to free and fair competition and practices that lead to cartels. The thin line of difference between these aspects is not always clear and hence even though cartels prevail in certain areas, the competition authorities are unable to categorize those practices as cartels. As provided under Section 18 of the Act, it is the duty of the Commission to eliminate practices having adverse effect on competition, promote and sustain competition, protect the interests of consumers and ensure freedom of trade carried on by other participants, in markets in India. The Commission should involve the participation of general public in descrying cartels to avoid cartels effectively. This can be done by creating awareness among the general public and informing them about the authorities before whom such matter can be placed for adjudication.

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