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Crisis Cartels: For Better or For Worse?

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I. INTRODUCTION

Cartels typically involve private agreements that limit quantities sold, thereby effectively raising prices; in turn this transfers income from buyers to sellers and reduces the allocative efficiency of the market mechanism. This market distortion is regarded as so detrimental to the institution of competition and to consumers, that strict enforcement of competition rules against cartels has been a top priority for most competition authorities globally.

The term "crisis cartel" is used in two ways in economic literature. First, it can refer to a cartel that was formed during a severe sectoral, national, or global economic downturn without state permission or legal sanction. A second use of the term "crisis cartel" has been to refer to situations where a government has permitted, even fostered, the formation of a cartel among firms during severe sectoral, national, or global economic downturns, or when national competition law allows for the creation of cartels during such downturns.[2] For antitrust considerations, a crisis is generally defined as a deterioration in economic performance indicators, such as demand, beyond that associated with a typical business cycle downturn. During the last century, such cartels have appeared in times of crisis, with most characteristic examples being the 19th century German crisis, the post-war era Japanese crisis, the U.S. crisis during the great depression of the 1930s, and the East Asian financial crisis in 1998.

Crisis cartels are one of the most challenging issues for competition authorities, who need to strike a balance between strictly antitrust considerations and non-economic government objectives, such as social welfare and survival of entire market sectors. The current global recession has made itself evident also by the reappearance of such cartels, a recent one being the crisis cartel in the fish-farming sector in Greece.

The present article is organized as follows. First, there is a presentation of the facts and the competition assessment of the fish-farming cartel formed between the five strongest market players in Greece. The next section presents the approach adopted by EC case law on crisis cartels, and attempts to evaluate its contemporary relevance to the current recession. Subsequently, the role of competition authorities in times of crisis is examined, followed by the

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[2] OECD, Directorate for Financial and Enterprise Affairs, Competition Committee, Global Forum on Competition, Crisis Cartels, Background Note, Session III, DAF/COMP/GF(2011)6, p. 6 et seq *available at* http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DAF/COMP/GF(2011)6&docLanguage=En

main alternatives to crisis cartels. The next section explains the need for an effects-based approach to crisis cartels, and the last section concludes.

II. HCC DECISION NO. 492/VI/2010

In late 2008, the five strongest fish farming companies in Greece notified to the Hellenic Competition Commission ("HCC"), a Memorandum of Cooperation ("MOC"), the purpose of which was to "mutually exert every possible effort to cope with the crisis in the aquaculture sector." Accordingly, the MOC parties requested the HCC to clear said agreement either pursuant to Art. 11 C.L. 703/77 or pursuant to Art. 1 para. 3 C.L. 703/77 (i.e. the equivalent of Art. 101 para. 3 TFEU).

The parties claimed that excessive production, and a resulting oversupply, of aquaculture products, especially sea bream, from Greek and other Mediterranean companies had occurred due to erred programming, in combination with the general financial crisis. They further claimed that this had caused a severe downturn in the aquaculture sector, which resulted in sales significantly below the average real cost, for a long period of time. As a result, the relevant prices had reached such low levels that, unless promptly reversed, would cause many undertakings to go out of business, since the demand did not increase despite the price reductions.

The MOC in question provided, among others, that the parties would:

a) form a six-member committee by their Managing Directors and/or General Managers aiming at addressing the crisis, with all means permitted by law;

b) determine and effect sales of the desirable quantities of products on a weekly basis, both in total and per company; and

c) determine the range of the desirable sale prices on a weekly basis, both in total and per company, in order to gradually stabilize sale prices at levels coinciding at least with the commonly acceptable threshold of average real cost. Its duration was agreed to be 6 months.

The MOC was notified both to the HCC and the competent of Minister of Agricultural Development and Food, who supported the initiatives of the MOC parties and took steps to assist the market sector also through the Ministry of Economics. To the contrary, however, the HCC initiated an ex officio investigation and subsequently a Statement of Objections, following which HCC Decision No. 492/VI/2010 was issued.

The HCC held that the agreement on the determination of the desirable sales price range on a weekly basis, in total and per company, which primarily aimed at setting such prices at least to the real average cost, directly limited the ability of the parties to determine their sale prices independently and thus violated Article 101 para. 1 TFEU and Article 1 para. 1 C.L. 703/77 (the equivalent of Art. 101 TFEU in Greek Law) by object. The HCC rejected the parties' argument that the term in question did not fix prices but merely set a goal-price and did not therefore violate Article 101 para. 1 TFEU and Article 1 para. 1 C.L. 703/77. The HCC held that, even if this were true, such agreement would still constitute an infringement by object; all the more so, since the regular exchange of information among the MOC parties on the range of each party's desirable sale price, allowed them to monitor and predict the general pricing policy of their competitors.

As to the agreement on the determination and realization of sales at the desirable quantities, on a weekly basis, in total and per company, the HCC held that it directly restricted the ability of the parties to independently determine the level and method of selling (and producing) the relevant products, and thus also violated Article 101 para. 1 TFEU and Article 1 para. 1 C.L. 703/77 by object. Accordingly, the HCC rejected the parties' arguments that the term on limitation of sales did not concern future production but only the existing one, and thus did not violate said articles. Pursuant to the HCC, even if this was the true meaning of the term, it would still constitute an infringement by object and, in any case, such agreement indirectly signalled the need to limit oversupply and thus to limit production in the upstream market. Besides, such limitation of sale quantities was directly connected with the price increase pursued, and thus, the HCC held, it should be appraised within the total plan of the parties to coordinate their business strategy.

The parties argued that even if the MOC fell under Art. 101 para. 1 TFEU and Article 1 para. 1 C.L. 703/77, it nevertheless satisfied the criteria of Art. 101 para. 3 TFEU and Art. 1 para. 3 C.L. 703/77, mainly because it was short-term (6 months) and aimed at normalizing the flow of ready products and reversing sale prices to levels approaching the production cost. The parties also argued that the measures in question also sought to safeguard the reliability of their products, the image of which had significantly deteriorated due to the low sale prices, which falsely signalled bad quality. Finally, the parties supported that if the MOC achieved its short-term goal, it would benefit both competition and consumers, since the chances of viability would increase for more undertakings in the market, and therefore competition and consumer choice would increase in the post-MOC era.

The HCC rejected such arguments, holding that the parties did not present enough evidence to support their claims and that, in any case, the agreement in question primarily aimed at safeguarding the parties' interests and not the consumers'. In particular, the HCC held that the measures taken by the MOC did not aim at addressing a long-term crisis on a permanent basis (restructuring), but merely sought to immediately stabilize/increase prices by controlling the quantities of sea bream sold to the market. Thus, an individual exemption under Art. 101 para. 3 TFEU and Art. 1 para. 3 C.L. 703/77 could not be granted, so much so since the exchange of information on pricing and sales quantities on a weekly basis between the parties constituted a violation of competition rules *per se*, and thus the agreement could not be considered a "necessary" or "proportional" means to achieve the efficiencies sought.

Concluding, the HCC stressed that the obligation of competing undertakings to independently determine their own business policy also covers periods when the supply and demand present cyclical variations, and competitors are not allowed to artificially maintain prices at higher levels through horizontal agreements until the market conditions return to a balance. Pursuant to the HCC, the independent adaption of undertakings to the developing market conditions, even during a financial crisis, is an indispensable element of the competitive procedure and, in any case, the mere existence of crisis in a given market did not suffice to remove the anticompetitive character of an agreement. Taking a rather strict view on crisis cartels, the HCC held that even if the parties to an agreement acted without immediate intention to restrict competition but in order to address the crisis in a particular sector, such reasons are not taken into account for the analysis under Art. 101 para. 1 TFEU and Art. 1 para. 1 C.L. 703/77, since collusive behaviour may impede competition by object, even if it also serves other purposes.

In view of the above, the HCC concluded that there had been a violation of Art. 101 para. 1 TFEU and Art. 1 para. 1 C.L. 703/77 and no exemption could be granted under para. 3 thereof. Thus, it imposed a fine of EUR 273,582 on NIREUS AQUACULTURE S.A., a fine of EUR 146,339 on SELONDA AQUACULTURE S.A., a fine of EUR 119,015 on DIAS AQUACULTURE S.A., a fine of EUR 42,905 on ANDROMEDA FISHFARMING S.A. and a fine of EUR 96,044 on HELLENIC FISHFARMING S.A.

III. THE EC CASE-LAW ON CRISIS CARTELS AND ITS CONTEMPORARY RELEVANCE

The above HCC decision reflects the traditional approach of EC case-law on crisis cartels[3]: the fact that an industry faces a crisis does not mean that undertakings can enter into agreements that restrict competition and claim immunity from Art. 101 TFEU.[4] As the former European Commissioner for Competition Policy, Ms. Neelie Kroes, noted during the current economic crisis: "there may be many temptations in 2009 to cut corners, but encouraging cartelists and others would be guaranteeing disaster. It would drag down recovery, increase consumer harm and create more cartel and cartel cases into the future. No-one wins—today's softness is tomorrow's nightmare.[5]"

Only when the crisis has resulted in a structural, as opposed to cyclical, overcapacity in a given industry can agreements in restraint of competition be condoned, and only if they are aimed solely at achieving a coordinated reduction of overcapacity, and do not otherwise restrict free decision making by the firms involved.[6] In particular, the reorganization must not be achieved by unsuitable means such as price-fixing or quota agreements and, as always, all four conditions of Art. 101 para. 3 TFEU must be satisfied for an exemption to be granted.[7]

The above prerequisites have rarely been satisfied over the past decades; exempting a crisis cartel under Art. 101 para. 3 TFEU is only the exception confirming the rule that anticompetitive agreements between undertakings cannot be tolerated, even in times of crisis. As the General Court noted in the *Imperial Chemicals* case, the poor financial state of a sector not only fails to justify forming a cartel, but also can hardly be regarded an attenuating circumstance, since "as a general rule cartels come into being when a sector encounters problems. If the applicant's reasoning were to be followed, the fine would have to be reduced as a matter of course in virtually all cases."[8]

However consistent the EC case- law on this point is, it has rarely dealt with cases where the crisis in a given market is coupled with such a profound and global financial downturn as the current one. The present economic circumstances, which have led countries such as Greece to the worst financial crisis since the end of World War II, have severely affected many market

[3] Indicatively, ECJ C-209/07, Irish Beef, ECJ C-238/99 P, C-244/99 P, C-245/99 P, C-247/99 P. C-250/99 P to C 252/99 P and C-254/99 P, LVM and other vs Commission, CFI T-217/03 and T-245/03, FNCBV and other vs Commission, Commission Decision COMP/C.38.279/F3, French Beef etc.

[4] RICHARD WHISH, COMPETITION LAW, Sixth Edition, p. 600 et seq. (2008).

[5] SPEECH/09/454 Date: 08/10/2009, Tackling cartels – a never-ending task, available at http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/09/454&format=HTML&aged=1&language=EN&guiLanguage=en

[6] XXiiird Commission Report on Competition Policy, at 84.

[7] *Id*. at 85

[8] Case T-13/89, Imperial Chemical Industries plc v. Commission, [1992] ECR II-1021, para. 372.

sectors with direct consequences on almost every form of business activity, such as fall in demand due to weakening of the buyer power, shortage of working capital, prohibitive lending terms from credit institutions, insolvency of debtors, etc.

Therefore, one could reasonably question whether the dicta of the existing case- law have any contemporary relevance with the current economic and financial circumstances, and, if so, to what degree. Today, a crisis that may strike a certain market sector, —even if it appears to be a case of cyclical overcapacity[9] which cannot, in principle, justify an exemption based on the existing case-law, —cannot be presumed to be overturned by market forces alone, as the latter are almost impossible to interact in the same way as they do under normal market conditions. Besides, the strong interconnection of various sectors of the economy favors "domino effects" in times of recession, whereby a crisis in a given industry may rapidly extend to neighboring markets, even if the latter did not *a priori* appear to be directly affected by the downturn.

In view of these complexities, and especially the extent and intensity of the current economic crisis, the rigid way in which EC case-law has addressed crisis cartels in previous points in time does not seem as efficient, or even appropriate, as it once did.

IV. THE ROLE OF COMPETITION AUTHORITIES DURING TIMES OF CRISIS

In general, when overall demand for a product falls, as normally happens during economic crises, incremental costs tend to rise for market players; therefore, but for the creation of a market allocation cartel, prices may rise even more. Thus it is not obvious what causes more harm to consumers: the exercise of any market power by the cartel, or the higher prices necessary to cover costs associated with competition between firms, in industries where unit costs fall as output rises.[10]

From another standpoint, sometimes crisis and overcapacity in a given industry may have the opposite result price-wise, namely result in sharp reductions, which may be good for the consumers in the short run, but may well undermine the capacity of the industry in long and medium term to invest and undertake R&D, causing consumer harm in the long term.[11] Either way, it is obvious that in times of crisis, consumer welfare is jeopardized irrespective of the price levels formed as a result of the downturn.

Economic theory has sustained that economic crises may often increase the incentive to cartelize.[12] When potential cartelists are faced with the prisoner's dilemma on whether to exit the market or form part of a cartel, they will compare the expected profit from cartelizing, with the expected profit from competing in the absence of a cartel, taking into account that if the cartel profit during the crisis is low, this may limit the maximum fines to be imposed. Subsequently, if

[9] Namely when excess capacity is going up and down over time.

[10] OECD, Directorate for Financial and Enterpise Affairs, Competition Committee, Global Forum on Competition, Crisis Cartels, Background Note, Session III, DAF/COMP/GF, p. 5 (2011).

[11] XXiiird Commission Report on Competition Policy, at 82.

[12] *See indicatively* George J. Stigler, *A Theory of Oligopoly*, 72(1) J. POL. ECON, pp.44-61 (1964) and Janice Rye Kinghorn, *Kartells and Cartel Theory: Evidence from Early 20th Century German Coal, Iron and Steel Industries*, CLIOMETRIC SOCIETY, (1966), *available at*: http://www.cliometrics.org/conferences/ASSA/Jan_96/kinghorn.shtml

they are convinced that the fines imposed during a crisis are less than under normal market conditions, their incentive to cartelize will be increased.[13]

If one accepts said theory (crisis favors cartels), it is obvious that competition authorities need to be very vigilant. But it is not that simple. In times of crisis competition considerations must also take into account non-economic factors and/or objectives often dictated by the government, such as reducing employment losses, facilitating rationalization of a sector with excess capacity, promoting productivity improvements by facilitating cooperation with the workforce, stabilizing prices, and avoiding ruinous competition that denies firms the necessary profits for reinvestment—all while avoiding a widespread backlash against cartel law and their enforcement. In the author's view, this task is so exigent that it cannot be successfully done following the traditional EC case-law on crisis cartels.

V. IF NOT A CARTEL, THEN WHAT?

Despite the aforementioned demand for a more efficient antitrust policy in times of crisis, competition authorities seem reluctant to adopt a more flexible approach to crisis cartels, not only because the rule prohibiting cartels is regarded as the cornerstone of antitrust enforcement, but also because under normal market conditions, cartels seem to be the most prejudicial competition restriction. Besides, a tolerant approach, even in times of crisis, could jeopardize the long established trend towards a strict anti-cartel enforcement, which seems to explain why antitrust authorities do not generally examine the effects of crisis cartels if they contain any "hard-core restrictions," but prefer to promote other means for exiting the crisis.

The most common alternatives to crisis cartels seem to be state bailouts and subsidies to domestic manufacturers, producers, and service providers, granted with the tolerance of or even the explicit approval of the European Commission. Such alternatives, although in principle preferable and less anticompetitive than a cartel, nevertheless contain imperfections.

First, granting state subsidies and bailout schemes inherently distorts competition conditions in a given market, all the more so when the criteria by which these are granted are not transparent, or when there are no guarantees that the benefit of the bailout will be passed on to consumers. Especially during the current crisis, most bailout schemes have been granted to credit institutions, as opposed to other sectors of the economy that might suffer a worse downturn, thereby only partially addressing the general market. Besides, granting subsidies to credit institutions does not seem to benefit the consumer, at least directly, while any pass-on procedure is almost certain to be a very slow one.

Second, there are many jurisdictions, such as Greece, that find themselves in such a deep recession they do not have the financial resources to sustain subsidizations; for such jurisdictions bailout schemes to boost the economy are not an option.

Another alternative promoted by some jurisdictions, such as Jordan, is the establishment of temporary minimum prices for certain goods and services, which seems to grant a presumption of legality to what would be otherwise considered an illicit price-fixing by competitors. Nevertheless, one could object that the state setting a minimum price for goods and services is not necessarily preferable than the market players doing so. Not only is this because

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[13] Margaret Levenstein & Valerie Y. Suslow (2010), *Constant Vigilance: Maintaining Cartel Deterrence During the Great Recession*, 6(2) COMPETITION POL'Y INT'L, pp. 145-162 (Autumn, 2010).

the latter understandably know their market better than the state and could fix the maximum price more effectively, but also because such state intervention creates a hazardous precedent for future state interventions in market sectors that are regulation-free and only subject to the market forces.

Mergers are another alternative often brought forward as a legitimate way to exit a sectoral crisis, presumably because although they attenuate competition between surviving firms, the harm to consumers is often less than that of a crisis cartel that eliminates all competition between rivals. The so-called failing firm defence has been accepted—albeit rarely—by competition authorities as a means to address sectoral crises. In such cases, a merger that would be normally blocked due to its adverse effect on competition is allowed when the acquired firm is actually failing, there is no less anti-competitive alternative offer of purchase, and, absent the merger, the assets to be acquired would exit the market,

Such an alternative, though, also poses problems, both theoretical and practical. First, a merger assessment inevitably entails *ex-ante* and *ex-post* considerations of competition conditions, which, given the prediction factor, inherently contain a degree of uncertainty. Second, such a merger inherently means that the market will have one less player in the post merger era, while another one will enjoy increased market power (the merged entity); hence competition in the market will to some degree be restricted anyway.

From this standpoint, it is not evident why a restructuring agreement which may contain normally "anticompetitive" terms, but can be presumed to achieve a pro-competitive objective in the long-term (the survival of as many competitors as possible), restricts competition more than a merger that will deprive the market of one market player and empower a strong one, all while providing no guarantees (but merely a presumption) that the post-merger competition will be ignited. There does not seem to be an obvious reason why such *ex-ante* and *ex-post* analysis cannot not be conducted *mutatis mutandis* also with regard to crisis cartels, especially when market forces seem unable to ignite competition in the market and the "legitimate alternatives" cannot guarantee an infallible solution thereto.

VI. NEED FOR AN EFFECTS BASED APPROACH

The Commission and the EC Courts have made it clear that an exemption to a crisis cartel can be granted provided, among other conditions, that the agreement does not contain any hard-core restrictions such as price-fixing, as the latter restricts competition by object: "price-fixing and market sharing are certainly not legitimate means of combatting difficult market conditions. Nor are undertakings entitled to flout [EU] competition rules because of alleged overcapacity."[14]

This holds true if one considers the wording of Art. 101 TFEU and the way it is interpreted under normal market conditions, but it may not be so if one considers the object of the agreement in question. As was the case in the Greek fish-farming cartel, often the object of the agreement is not the restriction of competition, but the survival of the parties, which will allow them to continue competing once the crisis is over.

[14] Case C-209/07, Competition Authority v. Beef Industry Development Society Ltd. And Barry Brothers (Carrigmore) Meats Ltd., [2008] ECR I-8637, para. 40.

The effects of such an agreement may be pro- or anticompetitive, but this should be cautiously assessed on a case-by-case basis; excluding such effects analysis altogether and, thus, the right to exemption, because a certain term would be considered "a restriction by object" in normal market conditions, appears too formalistic in times of crisis, where market conditions are distorted anyway. Besides, the essential objective of a typical restructuring agreement among crisis cartel parties is not achieving and sharing monopoly profit and forcing competitors to exit, but dividing loss to prevent exits from the market.

This difference is so crucial that it could itself justify a more lenient Art. 101 TFEU approach, at least before labelling an agreement as a "hard-core restriction" which disqualifies the right to exemption. This is not to say that cartels can never have anticompetitive effects; in fact in many cases they will actually do. But this is an empirical question, which cannot be appropriately answered judging only by the fact that they entail a restriction "by object."

Perhaps the most apparent inefficiency identified in the way Art. 101 para. 3 TFEU is applied on crisis cartels, is the fact that the exemption criteria, developed for tackling business behavior under normal market conditions, are applied in almost the same way to tackle behavior developed under distorted market conditions. Such application of Art. 101 para. 3, though, fails to take into account that in the latter circumstances there are less alternatives—if any—to the anticompetitive behaviour in question. And those that exist mostly depend on external factors, such as the state, rather than on private initiatives.

Whereas under normal market conditions it is almost self-evident that absent the cartel both the market and the consumers would be better off, this does not necessarily hold true with regard to a crisis cartel. In times of crisis, consumer welfare and market conditions are already affected adversely due to the downturn, and absent any intervention to reverse market conditions, consumer harm may increase even more. Therefore, a scheme aiming at reversing market conditions, even if it appears to be an anticompetitive practice, cannot be excluded as an option to raise consumer welfare in the long term more than market forces could alone; but even if it does not, one cannot *a priori* conclude that it will cause more harm to consumers than in the absence thereof.

Hence, there appears to be a need for a more flexible application of Art. 101 para. 3 TFEU by the competition authorities, which should entail an effects-based approach to crisis cartels, even when a restriction would be characterized as a 'restriction by object' under normal market conditions. There is no obvious reason why the *ex-ante* and *ex-post* analysis of the market conducted by competition authorities when assessing a failing firm merger cannot be applied also with regard to the crisis cartel analysis since, in both cases, the market downturn could cause more consumer harm than a business practice which would not be allowed under normal market conditions.

In any case, competition authorities should always consider whether there are indeed any viable alternatives to the crisis cartel, such as state interventions and, if so, whether such alternatives would increase consumer and social welfare more than the proposed cartel and do so at a lower cost. If there is no solid evidence that overall state intervention is preferable than a crisis cartel, after taking into account all costs and benefits, an approval of such a cartel subject to conditions and to periodical review, appears to be preferable than an *a priori* rejection thereof. And even more so when there is no available evidence comparing the effectiveness of crisis cartels

and other forms of state intervention, which could readily justify exclusion of the former and resort to the latter.[15]

VII. CONCLUDING REMARKS

It has been made clear from the above that crisis cartels are a very complex competition issue which cannot be efficiently addressed by formalistic and technocratic approaches adopted to address business behaviors developed under normal market conditions. The EC case-law so far does not appear to have departed from the traditional Art. 101 TFEU approach when appraising crisis cartels, irrespective of the fact that the economic and social circumstances under which crisis cartels were formed in the past seem to have evolved markedly. Unless EC courts and national competition authorities smartly adapt to the present economic circumstances and adopt an effects-based approach backed by sector-specific evidence, it is almost certain that crisis cartels, expected to increase due to the prolonged recession, will uncontrollably develop below the radar screen of competition authorities, to the obvious detriment of the market, competition conditions, and, finally, consumers.

Perhaps the first and rather costless step towards an enforcement reform of Art. 101 para. 3 TFEU on crisis cartels could be a more generous application of the Leniency Notice to members of crisis cartels that come forward, which will not only act as a motive for potential cartelists to unveil, but will also ensure a substantial amount of sector-specific information and evidence which the competition authorities may not otherwise have been able to collect.

However each competition authority chooses to adapt to the evolving economic circumstances, reviewing and appraising the contemporary relevance of the traditional EC case-law before strictly applying it, seems like a good start. Posing the question—whether a crisis cartel is for better or for worse—before considering it anathema, seems like a sign of progress.

[15] OECD, Directorate for Financial and Enterpise Affairs, Competition Committee, Global Forum on Competition, Crisis Cartels, Background Note, Session III, DAF/COMP/GF(2011), p. 33.