

THE IMPACT OF ANTI-COMPETITIVE CARTEL AGREEMENTS ON CONSUMERS AND THE ECONOMY IN GENERAL

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ABSTRACT

Cartels, the most harmful type of anticompetitive behavior, lead to high prices, lower quantities, and lower variety and innovation with a clear welfare loss. Moreover, they do not offer any economic or social benefit to justify the losses they generate, through their actions they can limit or eliminate part of the competition either on a global, European or national level, for this reason being condemned in all legislation of competition.

Keywords: competition, anti-competitive agreements, secret agreements, cartel, leniency, competitive environment;

INTRODUCTION

Considering the need to create a competitive environment, the Constitution stipulates that Romania's economy is a market economy, based on free initiative and competition.¹ Some authors² claim that "the most important regulatory force of the market economy is competition", representing the engine of operation and the energy of the development of economic activity.

In the legal sense, by competition we understand the confrontation between economic agents with similar or similar activities, exercised in the fields open to the market for winning and preserving clientele, in order to make their own company profitable³.

From an economic point of view, we can say that there is competition if the consumer can choose between several alternatives and can thus choose the one most favorable to his preferences⁴.

Between companies that produce the same goods or offer the same services, there is a permanent struggle to attract customers for the goods and services offered on the market.⁵

In a free market, business is a game where competitors compete, but sometimes businesses can be tempted to avoid this competition and try to set their own rules of the game. Sometimes a large player may try to eliminate its competitors from the market. The European Commission acts as a referee to ensure that all businesses play by the same rules.

¹ I. Didea, *Dreptul european al concurenței*, Editura Universul Juridic, București, 2009, p. 5;

² T. Moșteanu, *Concurența – abordări teoretice și practice*, Ed. Economică, București, 2000, p. 13;

³ O. Căpățână, *Dreptul concurenței comerciale (concurența onestă)*, Ed. Lumina Lex, București, 1992, p. 86, I. Băcanu, „Libera concurență în perioada de tranziție spre economia de piață”, în *Dreptul*, nr.9-12. P. 50;

⁴ T. Moșteanu, *Concurența – abordări teoretice și practice*, Ed. Economică, București, 2000, p. 31;

⁵ S.D. Cărpenaru, *Drept comercial român*, Ediția a VII-a, revăzută și adăugită, Ed. Universul Juridic, București, 2007, p. 112;

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If certain agreements, understandings between enterprises can have beneficial effects on the market, others can negatively influence the competitive process. In fact, reference is made to those anti-competitive practices known as cartels.⁶

Cartels are recognized as the most harmful type of anti-competitive behavior. The protection, maintenance and stimulation of competition and a normal competitive environment is ensured both by domestic legislation⁷ as well as through European legislation⁸, prohibiting any agreements between enterprises, decisions of enterprise associations and concerted practices, which have as their object or have the effect of preventing, restricting or distorting competition.

With few exceptions, by way of derogation from this rule, para. (3) of art. 101 of the TFEU provides that "the prohibition mentioned in par. (1) may be declared inapplicable for all agreements that contribute to the improvement of the production or distribution of goods or to the promotion of technical or economic progress, at the same time ensuring consumers a fair share of the benefit obtained, and that do not impose on the companies in question restrictions that are not indispensable for achieving these objectives and does not offer companies the opportunity to eliminate competition on a significant part of the market of the products in question".

The Competition Council represents the national administrative authority in the field of competition that aims to comply with the legislation in the field of competition, and in case they are violated, the sanctions provided for by law will be applied, thus exercising the coercive force of the state⁹.

The activity of the Competition Council is carried out on two components: a preventive one, for monitoring and supervising the markets, and a corrective one, for sanctioning deviations from normal competitive behavior¹⁰.

In order to discover and stop these anti-competitive practices, the Competition Council launched the leniency policy¹¹- a favorable treatment granted by the Competition Council, according to which the economic agents involved in cartels, who decide to put an end to these illegal practices and provide essential evidence, can benefit from immunity or a reduction of the fine, in the event of the application of a sanction. Thus, companies involved in an anti-competitive practice (agreement or concerted practice), which cooperate with the competition authority in order to discover the respective practice, can benefit from the leniency policy.

The Competition Council applies a policy of leniency under which a participant in such an anti-competitive practice, independently of the other companies involved, cooperates in an investigation carried out by the Competition Council or with a view to its initiation of an investigation, providing voluntarily the information he has about the anti-competitive practice and his role in it and receiving in return immunity from fines or a reduction of the fines that would be imposed for his involvement in that anti-competitive practice.¹²

⁶ http://ec.europa.eu/competition/publications/consumer_ro.pdf

⁷ art.5 paragraph (1) of the Competition Law no. 21/1996, republished, prohibits "any agreements between enterprises, decisions of enterprise associations and concerted practices, which have as their object or have the effect of preventing, restricting or distorting competition on the Romanian market or part of it."

⁸ art. 101 of the Treaty on the Functioning of the European Union (TFEU) which stipulates in paragraph (1) that "any agreements between enterprises, any decisions of associations of enterprises and any concerted practices that may affect trade between member states and are prohibited are incompatible with the internal market which have as object or effect the prevention, restriction or distortion of competition within the common market."

⁹ M. M. Dumitru, *Dreptul concurenței*, Ed. Institutul European Iași, Iași, 2011, p. 97;

¹⁰ <https://www.consiliulconcurentei.ro/despre-noi/descrierea-consiliului-concurentei/rolul/>

¹¹ <http://www.clementa.ro/politica-de-clementa/>

¹² ORDIN nr. 642 din 15 iulie 2019 for the implementation of the Instructions on the conditions and criteria for

General considerations regarding the notion of cartel

Anti-competitive practices or anti-trust law traditionally designates two types of business behavior likely to harm competition: anti-competitive agreements and abuse of a dominant position.¹³

Both European Union regulations and national legislation prohibit anti-competitive agreements, aiming to create an undistorted competitive environment, in which objectives such as: economic progress, stimulation of entrepreneurship and efficiency, promotion of consumer interests, competitiveness of products and services, etc. are pursued.¹⁴

Considering the negative impact on consumers and the economy in general, the most serious forms of anti-competitive agreements that can affect the competitive environment to a greater extent are secret horizontal agreements, cartel-type, aimed at fixing prices, dividing markets, limiting production and distribution, allocation of customers and territories.¹⁵

According to the explanatory dictionary of the Romanian language, the cartel represents a monopolistic union in which several enterprises in the same branch of production conclude an agreement, establishing the prices, the conditions of sale and supply, the terms of payment, the quantity of goods to be produced by each and its divide markets in order to limit or eliminate competition.¹⁶ Such monopolistic unions are prohibited both in Romania and in the European Union.

A cartel is a group of similar, independent businesses that join together to control prices, divide their market, and ultimately limit competition in that market. As a rule, cartels involve secret and at the same time illegal agreements between members, so that the profit is maximum. Participants in a cartel can rely on their market share established by virtue of their understanding with others and do not need to offer new products or quality services at competitive prices. As a result, consumers end up paying more for poorer quality, ultimately being the most affected by this type of deal.¹⁷

According to the Organization for Economic Co-operation and Development (OECD), a cartel is "an anti-competitive agreement, a concerted anti-competitive practice between competitors to fix prices, manipulate tenders, establish restrictions on production or share market shares or geographic markets by allocating customers, suppliers, territories or business types"¹⁸. This definition is given, more specifically, to a "hardcore" type cartel agreement (eng. "hardcore cartel"), respectively to those forms of cartel that are perceived to determine the most anti-competitive effects.

A company's choice to participate in a cartel has strong strategic implications. Thus, although it represents a "distorting" form of strategy - in the sense that the objective of a cartel is the exact opposite of what the company's strategy should aim at - cartels remain a form of cooperation of a strategic nature, which has effects on the company's competitive position on market.

To identify cartel participants, investigators consider the following factors¹⁹:

- the most important competitors on the respective market;
- the goods or services concerned;

the application of the leniency policy, published in MONITORUL OFICIAL nr. 631 din 30 iulie 2019

¹³ G. Coman, *Concurența în dreptul intern și european*, Editura Hamangiu, București, 2011, p. 173;

¹⁴ L. Maiorean, *Dreptul concurenței comerciale*. Curs universitar, Ed. Cermaprint, București, 2009, p.21;

¹⁵ R.D. Vidican, *The importance of analyzing the main anti-competitive practices in view of creating an undistorted competitive environment*, AGORA International Journal of Juridical Sciences, No. 1 (2022), p.70;

¹⁶ <http://dexonline.ro/definitie/cartel>

¹⁷ Politica UE în domeniul concurenței și consumatorul, Ghid european, Direcția Generală pentru Concurență a Comisiei Europene

¹⁸ <http://www.oecd.org/daf/competition/98765440.pdf>

¹⁹ International Competition Network, *Anti-Cartel Enforcement Manual. Chapter 5 – Investigative strategy*, p. 7, www.internationalcompetitionnetwork.org .

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- the degree of consumer dependence on the products or services of the companies that form the cartel;
- the price formation mechanism.

The European Commission believes that it must be very strict with cartels, especially after the introduction of the single currency, because the positive effects of the economic and monetary union - the increase in price transparency within the Union and, consequently, the intensification of competition for the benefit of users, not to be removed by agreements between enterprises. They will be tempted to avoid confrontation on the market by artificially setting the level of the selling price or other commercial conditions, which may lead in the long term to the undermining of the economic and monetary union. Neelie Kroes emphasized in this sense that "cartel-type behavior is illegal, unjustified and unfair, regardless of its size, the nature or the purpose of the affected business"²⁰.

In conclusion, the cartel represents a cooperation for obtaining higher profits and for decreasing the degree of business risk. The gains can be huge as we saw in the 1970s when the Organization of the Petroleum Exporting Countries (OPEC) cut production, raising the price of oil, which led to the creation of enormous wealth in the oil exporting countries.

Analysis of cartel agreements

Due to the couple of low quantities/excessive prices with which they operate, the cartels represent the greatest danger, being considered to directly harm the buyers. They also have an indirect destructive effect, in the sense that, by reducing competition, the efficiency of the participants decreases, which becomes the premise of price increases above the level of real competition.

Both theory and practice show that a cartel is an unstable form of cooperation. If a cartel is profitable in the long run for all its members, then they merge into one large enterprise. The cartel thus disappears in this merger. However, if for one or more members the joint action does not prove too profitable, an independent action will, in most cases, destroy the cartel. It is possible that one of the companies forming the cartel, due to its independence, may want to receive a higher production share. The other companies will oppose this request. In this sense, Professor L. Benham affirmed²¹: "the companies that produced a relatively important part of the production quantity in the past will demand the same part in the future. Expanding businesses (due to more effective management, for example) will demand a larger share than they have obtained in the past."

George Stigler suggested that although oligopolists want to maximize joint profits through their union, asymmetric information creates the opportunity to betray the agreement.

If the cartel brings in unusual monopoly profits, firms and producers outside the branch will enter this area of production to benefit from these profits. And if a major competitor emerges and challenges the cartel, it may disappear. It should not be forgotten that the formation of a cartel is prohibited by law in most countries.

The impact of cartel agreements

Evenett, citing several sources, estimates that, on average, the existence of a cartel increases prices by about 20-40% compared to prices in the case of a competitive situation²².

²⁰ Neelie Kroes, membră a Comisiei Europene, însărcinată cu politica de concurență, The First Hundred Days, comunicare susținută cu ocazia „Forumului Internațional privind legislația europeană de concurență”, Bruxelles, 7 aprilie 2005

²¹ L. Benham, Economics, Ed. Pitman Publishing Co, New York, 1941, pg. 232;

²² Evenett, Simon J. – 'Can Developing Economies Benefit from WTO Negotiations on Binding Disciplines for Hard Core Cartels' ,Aussen, June 2003, 58, 2.

In the case of the cartel on the citric acid market, the former EU competition commissioner, Mario Monti, estimated that the price increase was 50%.

This increase in prices, however, makes that market more attractive for producers who are not members of the cartel ("outsiders"). Thus, a "successful" cartel makes the sector more attractive, which attracts other producers - usually foreign - to the respective market (the so-called "price umbrella" effect, created by a cartel-type agreement). Thus, the hypothesis is confirmed that a cartel can only be effective in the medium and long term as a result of the existence of barriers to the entry of new competitors on the respective market.

The main criteria by which the cartels allocated market shares to their members are:

- past market shares. Thus, the cartel is "a picture" of the competitive situation at a given moment on a market. From this point of view, any development on the market that causes a change in competitive conditions (dynamic factor) acts to increase the cartel's instability to the extent that some members of the cartel will consider that the new situation in the sector entitles them to a market share / higher production.

- production capacity from the moment the cartel agreement was concluded. This criterion creates low motivations for the subsequent profitability of the cartel members' activity (which can possibly be achieved by reducing the production capacity in the case of an oversupplied market) and even motivates the cartel member producers to make investments in expanding their production capacity, although this does not it is argued by the reality of the market.

Producers, to the extent that the only criterion on the basis of which market shares are allocated to them is physical production capacity, will do everything to expand this capacity, regardless of whether it is explainable from an economic point of view. Thus, the companies within a cartel become less dependent on consumers/customers for their activity as they become dependent on their bargaining power within the cartel.

Cartels can have other negative economic effects besides the misallocation of resources (effects on economic efficiency): a cartel shields its members from exposure to market forces, resulting in reduced pressure on cost control and innovation.

These effects on productive and dynamic efficiency are more difficult to measure and, as a result, the competition authorities must focus on the illegal profits obtained by cartel operators, which are easier to calculate.

There is another equally important reason for focusing the analysis on the cartel's gains, which relates to sanctions. Their purpose, in the context of cartels, is to prevent their appearance on the market. An optimal sanction should ensure that the operators of a possible cartel cannot expect to gain from it, as they would lose the profits they would have earned from the illegal behavior as a result of the sanctions.

But calculating the profit of a cartel is also difficult, and the simplest form of calculation can be approximated by multiplying the price increase resulting from the agreement in the form of a cartel with the amount of sales (in units) subject to the agreement (ie the trade affected). It is difficult to determine the competitive price or, in other words, the reference price for calculating the illegal price increase. A "benchmark" price can be used, determined by examining several markets where there is no collusion.

The impact of the cartels is very broad, but difficult to quantify. The data collected following an OECD study, regarding the magnitude of damage caused by cartels worldwide, allowed the following conclusion to be drawn: "the damage caused by cartels is much higher than originally thought, exceeding the equivalent of billions of dollars per year"²³.

²³ OCDE, Report on the nature and Impact of Hard Core cartels and Sanctions against Cartels under national Competition Law, pg. 5, disponibil pe internet la: <http://www.oecd.org/dataoecd/16/20/2081831.pdf>

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Although it is very difficult to calculate the effects of a cartel, there are many reasons why it must be done, including the need to inform consumers and the competition authorities about the importance of implementing an aggressive program against this practice, the need to rehabilitate consumers who have suffered from following these effects and the application by governments of the necessary sanctions.

Conclusions

Current modernism emphasizes the explosive development of relations between enterprises, classified as cooperative relations. Thus, we are increasingly talking about strategic alliances, joint ventures or even cartels. If a few decades ago, the state was the one who initiated certain forms of economic cooperation, now we notice that businesses are the ones who initiate such agreements.

In the typology of competition restrictions, agreements between companies in the form of secret agreements constitute the most harmful form. These concerted practices often group together an important number of economic operators, within a sector of activity, and therefore have a very strong effect on the markets in question. The existence of a cartel denotes major managerial deficiencies that represent impediments to efficient, productive and profitable growth for the enterprise and the economy, it blurs the phenomenon of the emergence of new products, preventing the development of more efficient production processes. In addition, they almost always aim to fix sales prices leading to the prevention of competition.

The lack of competition caused by the existence of such cartels also causes a lack of interest on the part of the producers regarding the quality of the product on the market, the quality-price ratio being forgotten in the conditions of a profit ensured in the shadow of the cartel. Those who pay the prices of such cartels are the consumers who are thus forced to pay higher prices for low quality products, thus not having the option to choose.

Among the main negative effects of anti-competitive agreements, we mention: the artificial limitation of competition, the increase of prices, the decrease in the quality of products or services offered to consumers, the reduction of supply, the avoidance of constraints that generate innovation.

In the long term the effects generated by cartels are even more dangerous than those in the medium and short term. Affecting the real competition in the market, the cartels, once formed, tend to attract more and more economic agents, who find it increasingly difficult and practically impossible to face the competition of the cartels. By practically regimenting themselves in these cartels, in order to avoid the direct effects of competition, economic agents lead to the creation, in the long term, of an unstable industrial branch, coordinated by non-economic principles, an artificial industrial branch, which no longer maintains contact with economic reality.

Thus, we gradually reach a decrease in productivity, an artificial maintenance of prices much higher than they would have been in reality if they had been formed by achieving the macroeconomic balance between demand and supply, as well as a stagnation of the process of technological innovation. Precisely for these reasons, finding, accusing and punishing these secret agreements and implicitly the economic agents who were behind them, is one of the central elements of the competition policy of the European Commission.

In conclusion, cartels are considered the worst forms of anti-competitive agreements, considering the negative impact on consumers and the economy in general and the evidence of their existence being difficult to formulate precisely because of the secret nature of the agreement.

Competition often forces players in international and national markets to reach agreements that do not benefit consumers and harm the economy. Many of the commercial

policies of large companies, however, focus on the creation and exploitation of real competition, which causes economic agents to focus on consumers, more precisely on their needs, trying to satisfy them as best as possible by offering differentiated products or services from those of the other competitors. This presupposes the adoption of a certain competitive behavior, behavior that manifests itself in the competitive relations existing in a field of activity or in a market.

Competition is an effective means to eliminate surplus profits made by some economic agents, to allocate resources for certain uses necessary for society, to determine enterprises to produce quality goods at low costs and in the quantities desired by consumers, to stimulate the introduction technological innovations. Therefore, competition must be seen as a dynamic process with beneficial effects on the economy as a whole, the undistorted competitive environment being a basic condition for the existence of a functional market economy.

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