The Competition Authority
An tÚdarás Iomaíochta

DISGUISED CARTELS
Industry Restructuring
(“Crisis Cartels”)

EU-China Competition Week

21 to 24 October 2013

Victoria Balaguer
Case Officer/Lawyer
Irish Competition Authority

Issues to cover

1. Crisis Cartels
   - What are they?
   - Types
   - Government intervention
   - Legal framework: Article 101

2. Agreements to reduce capacity
   - What are they?
   - What is agreed?

3. The *BIDS* case – application of Article 101(1)

4. Application of Article 101(3)

5. Conclusion

1.a Crisis Cartels
What are they?

- Crisis cartels (also know as "*industrial restructuring agreements*") are:

  - agreements among competitors - horizontal agreements

  - to resolve problems arising within a specific industry - mainly excessive production, low prices and overcapacity

  - during a sectoral, national or global economic crisis

1.b Crisis Cartels
Types

- Agreement on a **"fair" price level** to avoid that some companies leave the market.

- Agreements to **restrict sales** or **output**.

  (e.g. by setting production quotas among firms and penalties for overproduction)

- Agreements to **reduce capacity**.

- Agreements to **restrict imports/exports**.

1.c Crisis Cartels
Government intervention

- Governments have created or encouraged the creation of crisis cartels, particularly during previous economic crisis.
- They can:
  - allow or encourage crisis cartels (**direct intervention**)
  - adopt non-economic factors and/or objectives (e.g. social welfare and employment) and expect that they are taken into account by competition agencies when applying competition rules to crisis cartels (**indirect intervention**)
  - amend competition laws

1.c Crisis Cartels
Government intervention

- **Motives** behind a policy towards crisis cartels:
  - Limiting or avoiding employment losses
  - Facilitating rationalisation of a sector with excess capacity
  - Stabilising prices
  - Preserving a proportion of the total market for favoured firms, including domestic firms

1.c Crisis Cartels
Government intervention

- **Crisis cartel in the French beef industry** (2001)
  - agreement to restrict imports and fix minimum prices
  - meeting organised by the French Minister of Agriculture
- **Crisis cartel in the Irish Beef Processing Industry** (2002)
  - agreement to reduce capacity
  - implement the recommendations to reduce capacity identified in a report commissioned by the Irish Government and supported by a task force set up by the Minister of Agriculture and Food

1.c Crisis Cartels
Government intervention

- **Crisis cartel in the fish-farming sector in Greece** (2008)
  - agreement to set prices and restrict sales/output
  - Minister of Agriculture supported the initiatives and took steps to assist the market sector
- **Crisis cartel in the rubber market** (2008)
  - agreement to reduce exports (by limiting production) and fix prices
  - promoted by the Governments of Indonesia, Malaysia and Thailand

1.d Crisis Cartels
Legal framework: Art. 101

Art. 101(1) ⇨ **Prohibition**

- Prohibits agreements that have as their <u>object</u> or <u>effect</u> the restriction, prevention or distortion of competition in the common market, including agreements to:
  - directly or indirectly **fix prices** or any other trading conditions
  - **limit or control production**, markets, technical development, or investment
  - share markets or sources of supply
  - apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage
  - make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which have no connection with the subject of such contracts

1.d Crisis Cartels
Legal framework: Art. 101

Art. 101(3) ⇨ **Exemption**

- Exempts anticompetitive agreements that meet four conditions:
  - contribute to improving the production or distribution of goods or provision of services or to promoting technical or economic progress
  - allow consumers a fair share of the resulting benefit
  - do not impose on the undertakings concerned terms which are not indispensable to the attainment of those objectives
  - do not afford undertakings the possibility of eliminating competition in respect of a substantial part of the products or services in question

1.e Crisis Cartels
Application of Art. 101?

- **YES,** even if there is government intervention.

  The fact that conduct on the part of a company is known, authorised or even encouraged by national authorities has no bearing on the applicability of Art. 101

- Crisis cartels are agreements between competitors and thus fall within the scope of Art. 101.

- Times of economic recession or declining demand do not grant immunity from the application of competition law.

- Recent practice shows that most competition agencies do not follow a flexible approach.

- Crisis cartels must, therefore, be assessed under:

  - Art. 101(1) – prohibition
  - Art. 101(3) – exemption

1.e Crisis Cartels

Application of Art. 101

- 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****"*.

2.a Agreements to reduce capacity
What are they?

- Agreements whereby competing companies within an industry **agree to reduce capacity**.
- One specific type of "*crisis cartels*".
- Entered into in the context of industries suffering from overcapacity problems (sectoral economic crisis):
  - industries experiencing a fall in demand (e.g. recession-induced fall in demand or technological changes)
  - industries where there has been overinvestment for a prolonged period of time (e.g. industries that have received state aids for a long time, or where state control prevented the closure of plants due to social or political factors, such as unemployment)

2.b Agreements to reduce capacity
What is agreed?

- **A reduction of capacity** in one specific industry.

  1) A number of **individual companies leaving the industry** and closing down their production capacity – complete exit of certain players from the market

  2) **Companies reducing part of their own production capacity** by closing down a number of plants or production units – all players stay in the market

- The companies leaving the industry (or companies suffering a reduction of their capacity) are financially compensated.
- A commitment not to increase capacity during the currency of the agreement.
- Restrictions in the use of the dismantled plants.

2.c Agreements to reduce capacity
Application of Art. 101

- In the past, the Commission has looked at agreements to reduce capacity:
  - 1984: *Synthetic Fibres* case - synthetic fibres industry
  - 1994: *Stichting Baksteen* case (known as the *Dutch Bricks* case) - bricks industry

- The Commission considered that these agreements infringed art. 101(1) but could be exempted under art. 101(3)
  - there is very little analysis on the application of art. 101(1)
  - inaccurate statements on the application of art. 101(3)

- **Landmark judgment on the application of Article 101(1) to agreements to reduce capacity:** judgment of the Court of Justice delivered on 20 November 2008 in the *Beef Industry Development Society* case (the *BIDS* case).

3.a The BIDS case
The story of the case

- **1998: the McKinsey Report**
  - Identified significant year round overcapacity in the Irish beef processing industry
  - Recommended the rationalisation of the industry
- **1999: Irish Ministry of Agriculture and Food**
  - Sets up the Beef Task Force which concludes the industry should remove excess capacity
- **2002: the 10 biggest beef processors form BIDS** (an association of beef processing companies)
  - BIDS to take 25% of overcapacity off the market

3.b The BIDS case
The Agreement

- To achieve the reduction of capacity, it was agreed that:
  - Some beef processors would leave the industry (the "*goers*") and some of them would stay (the "*stayers*")
  - The *stayers* would pay levies (€2 and €11) on each head of cattle slaughtered to pay the *goers* for leaving the industry
- Additional restrictions on future activities of the *goers,* their land and equipment:
  - Non-compete clause
  - Decommissioning of the plants
  - Prohibition to use the land for beef processing
  - Equipment sold to *stayers* or purchasers outside Ireland

3.c The BIDS case
Application of Art.101(1)

- Art. 101(1) prohibits agreements that have as their **object** or **effect** the prevention, restriction or distortion of competition.

- Judgment of the Court of Justice:

"In the light of the foregoing considerations, the reply to the question referred must be that ***an agreement with features such as those of the standard form of contract concluded between the 10 principal beef and veal processors in Ireland****, who are members of BIDS,* ***and requiring, among other things, a reduction of the order of 25% in processing capacity****,* ***has as its object*** *the prevention, restriction or distortion of competition within the meaning of Article 81(1) EC"*.

The Competition Authority
An tÚdarás Iomaíochta

3.c The BIDS Case

Application of Art. 101(1)

- The Court of Justice also found that these type of agreements are anticompetitive by object:

  "even supposing it to be established that the parties to an agreement acted without any subjective intention of restricting competition, but ***with the object of remedying the effects of a crisis in their sector*** *[…]"*

- It is not necessary for plaintiff to demonstrate anticompetitive effects.

- The only assessment necessary for such agreement will be an assessment under Art. 101(3) to see whether the conditions necessary for an exemption are satisfied.

The Competition Authority
An tÚdarás Iomaíochta

4.a Application of Art.101(3)

- Art. 101(3) provides for an exemption from the prohibition contained in Art. 101(1) against anticompetitive agreements.

- An agreement must meet four conditions:

  - Generate efficiency gains

  - Benefit consumers

  - Indispensable to achieve the efficiency gains

  - No elimination of competition

4.b Application of Art.101(3)

- The Court of Justice did not deal with the application of Art. 101(3) in the *BIDS* case.

- Where to find guidance?

- Commission´s guidance documents:

  - Commission's "*Guidelines on the application of Article 81(3)* [now Art. 101(3)] *of the Treaty*"

  - Commission written observations submitted to the Irish High Court in the BIDS case ("*amicus curiae*" observations)

4.c Application of Art.101(3)
First condition: efficiency gains

The agreement must generate efficiencies.

- It is necessary to verify:
  - The nature of the claimed efficiencies
  - The link between the agreement and the efficiencies
  - The likelihood and magnitude of each claimed efficiencies
  - How and when each claimed efficiencies would be achieved

- Only inefficient players/plants should exit the market – the agreement should provide sufficient indication of what firms are to reduce capacity or leave the market altogether.

- The companies staying in the industry should not be restricted from increasing output.

4.d Application of Art. 101(3)
Third condition: indispensability

- The overall arrangement (and each individual restriction flowing from the agreement) must be indispensable to achieve the claimed efficiency gains.

- Could market forces solve the problem of overcapacity within a reasonable period of time?

  - Possibly not when there is structural overcapacity

- Are there any other economically practicable and less restrictive means of achieving the efficiencies?

  - e.g. mergers and acquisitions and specialisation agreements

5. Conclusion

- Competition agencies need to be very vigilant – economic crisis may favour cartels.
- Granting immunity to crisis cartels by governments or competition agencies would mark a significant point of departure from prevailing views on cartel enforcement.
- Crisis cartels can avail of the exemption to the prohibition when all the conditions under Art. 101(3) are met.
- Post-BIDS:
  - Crisis cartel in the French beef industry: Judgment of the Court of Justice, 18 December 2008 - breach of Art. 101
  - Baltic Max Feeder Scheme: 26 March 2010, investigation closed
  - Crisis cartel in the Greek fish-farming industry: decision of the Hellenic Competition Commission, 23 June 2010 – breach of Art. 101

Thank you

Questions?