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Cartel in Indian Market –An Overview

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INTRODUCTION

"Competition is not only the basis of protection to the consumer, but is the incentive to progress."

When a layman thinks of competition, he or she probably has one of two images in mind. The first is a sporting event, in which two evenly matched opponents, play a spirited, but closely contested, match like the recent Champions League Match between Real Madrid and Manchester United. The second is a market that resembles a scrum in a rugby match with numerous firms scrambling for every scrap of business — the more numerous, the more competitive.

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Competition is a vital element in the lives of consumers. For the consumers, competition in the economy is a crucial factor in determining benefits, appropriate prices and the variety of choice to choose from. The aims of competition or antitrust laws are to ensure that consumers pay the most efficient price coupled with the highest quality of goods and services they consume. When there are activities which hamper the competition, the consumers are the very first party which gets affected and then comes the economy of a nation.

CARTELS

One way to hamper the competition and creating monopoly in the market is forming cartels. Cartels have got adverse effect on competition. It hampers promotion and sustenance of competition in markets. It fails to protect the interests of consumers and restricts the freedom of trade carried out by other participants present in the market. It gives the parties to the agreement an undue benefit which helps them to dictate different variables of the market.

Cartel – the English word seems to have first come into common use by mainstream economists – Alfred Marshall's Principles of Economics. Economists borrowed the term and ascribed to cartels behavior that was antithetical to efficient competition. By analogy the word Cartel was used by German economists to signify a coalition that brought together hostile political parties. Later on, this term came to mean an arrangement of business rivals for the purpose of regulating prices or output in the industry. Cartel is the term which the Americans referred as 'Trusts' or 'Combinations'. As per the Oxford English Dictionary the word Cartel was first used in English in 1902 in the Business sense to refer to what were formerly called "producers syndicates" or "trusts" in the sugar or steel industry.

INDIAN LAWS

In India, The Competition Act, 2002, as amended by the Competition (Amendment) Act, 2007, ('the Act') prohibits any agreement which causes, or is likely to cause, appreciable adverse effect on competition in markets in India. Any such agreement is void.

Cartels as defined under the Act, are an explicit or implicit agreements between enterprises (including association of enterprises) not to compete on price, product (including goods and services) or customers but to fix prices, limit production and supply, allocate market share or sales quotas, or engage in collusive bidding or bid-rigging in one or more markets. An important dimension in the definition of a cartel is that it requires an agreement between competing enterprises, not to compete, or to restrict competition.

The objective of a cartel is to raise price above competitive levels, resulting in injury to consumers and to the economy. For the consumers, cartelization results in higher prices, poor quality and less or no choice for goods or/and services. Each and every consequence of cartel is inter related to each other. When we consider cartel decreasing the competition in the market between the suppliers of same or similar commodities in the market, then the quality and price are bound to get affected in a negative way for the consumers.

There are different kinds of cartels, like an international cartel, which is said to exist, when not all of the enterprises in a cartel are based in the same country or when the cartel affects markets of more than one country. Another form of cartel is an import cartel, which comprises enterprises (including an association of enterprises) that get together for the purpose of imports into the country, where as an export cartel is made up of enterprises based in one country with an agreement to cartelize markets in other countries. By working together, the cartel members are able to behave like a monopolist.

These sorts of Cartels not only affect the market of the country they are based but have got the ability to harm to consumers of different nations. Since, formation of cartels is an easy process; these cartels can be formed with ease without any intervention of the national or international laws. As two or more enterprise only have to agree on simple terms to increase the price over a competition level to kill the competition prevailing in the particular market. This can be done through a formal agreement in writing, agreement which is not legally enforceable, or without any agreement in writing.

Agreements between enterprises engaged in identical or similar trade of goods or provision of services (commonly known as horizontal agreements) including cartels, of four types specified in the Act are presumed to have appreciable adverse effect on competition and, therefore, are considered anti-competitive and void according to Indian law. As evident from Section 3, sub section (3) of the Act:

"Any agreement entered into between enterprises or associations of enterprises or persons or associations of persons or between any person and enterprise or practice carried on , or decision taken by, any association of enterprises or association of persons, including cartels, engaged in identical or similar trade of goods or provision of services, which-

(a) directly or indirectly determines purchase or sale prices;

(b) limits or controls production, supply, markets, technical development, investment or provision of services;

(c) shares the market or source of production or provision of services by way of allocation of geographical area of market, or type of goods or services, or number of customers in the market or any other similar way;

(d) directly or indirectly results in bid rigging or collusive bidding, shall be presumed to have an appreciable adverse effect on competition:"

However, horizontal agreements of the above four types entered into by way of joint ventures are not presumed to have appreciable adverse effect on competition and are excluded from the above provisions of section 3, sub section (3) of the Act if they increase efficiency in production, supply, distribution, storage, acquisition or control of goods or provision of services.

The above statement is laid down in the proviso to section 3, sub section (3) of the Act, which is:

"Provided that nothing contained in this sub-section shall apply to any agreement entered into by way of joint ventures if such agreement increases efficiency in production, supply, distribution, storage, acquisition or control of goods or provision of services."

Appreciable adverse effect on competition of other types of agreements i.e. other than those covered by section 3, sub section (3) of the Act, including tie-in arrangement, exclusive supply arrangement, exclusive distribution agreement, refusal to deal and resale price maintenance, commonly known as 'vertical agreements " would not be presumed to have appreciable adverse effect on competition.

So, it is very evident that any agreement which is injurious to the interests of the consumer would be held as illegal and in violation of the Indian law as laid down in the Act. Any agreement which is made for the betterment of the consumers by way of increasing the supply, providing storage facilities for excess goods, bettering the quality of the goods. Hence, any agreement entered by enterprises for this sort of work would not come under the definition of cartel, as these are not injurious for the consumers and the economy of the nation.

CHARACTERISTICS OF CARTELS

Before we understand the common characteristics of cartel in details, this statement gives a summery.

"Cartel behavior attacks the very heart of a "free economy" – the determination of price and output through competition and consumer preferences – diverts resources from their optimal use, and transfers wealth to those engaged in illegal activity.The uncertainty that exists in an oligopoly can lead to collusive behavior by firms. When this happens the existing businesses decide to engage in price fixing agreements or cartels. The aim of this is to maximize joint profits and act as if the market was a pure monopoly, which usually functions in secrecy. The members of a cartel, by and large, seek to camouflage their activities to avoid detection by the Commission. Perpetuation of cartels is ensured through retaliation threats. If any member cheats, the cartel members retaliate through temporary price cuts to take business away or can isolate the cheating member.

Another method, known as compensation scheme, is resorted to in order to discourage cheating. Under this scheme, if the member of a cartel was found to have sold more than its allocated share, it would have to compensate the other members. As a result of which no party to the agreement breaks the cartel. The cartel gives them more profit than being out of it. Some of the conditions that are conducive to cartelization are:

- high concentration – few competitors
- high entry and exit barriers
- homogeneity of the products (similar products)
- similar production costs
- excess capacity
- high dependence of the consumers on the product
- History of collusion.

Along with the above mentioned conditions, for the cartel to work effectively the producers must control supply to maintain an artificially high price. Collusion is easier to achieve when there is relatively small number of firms in the market and a large number of customers, market demands are not too variable and the individual firm's output can be easily monitored by the cartel organization.

Lack of effective competition and proper system to detect the agreements entered by the enterprises plays a very vital part in collusion method being used by the suppliers in a large number. If there is effective competition in the market, cartels would find it difficult to be formed and sustained.

Once established, cartels are difficult to maintain as some economists believe that price-fixing cartels are inherently unstable and that at some point they inevitably come under pressure and finally break down. The problem is that cartel members will be tempted to cheat on their agreement to limit production. By producing more output than it has agreed to produce, a cartel member can increase its share of the cartel's profits. Hence, there is a built-in incentive for each cartel member to cheat. Of course, if all members cheated, the cartel would cease to earn monopoly profits, and there would no longer be any incentive for firms to remain in the cartel.

There are a number of sources of potential instability for price fixing cartel arrangements.

- Falling demand creates tension between firms e.g. during an economic downturn;
- The entry of non-cartel firms into the industry increases market supply and puts downward pressure on the cartel price;
- Exposure of illegal price fixing by the Government or other regulatory agencies causes an arrangement to end;
- Over-production and excess supply by cartel members breaks the price fixing; and
- The Prisoners' Dilemma game suggests that all collusive agreements tend to fall eventually because although price fixing is in the joint interests of all members of a cartel, it is not a profit maximizing equilibrium for each individual firm.

ANTITHETICAL RELATIONSHIP

To Adam Smith, business collusion was an ubiquitous temptation, a 'conspiracy against the public' that was injurious to the workings of a market economy. Collusion has been a mere cooperation for the business leaders to avoid destructive competition that is injurious to their firms and industries. To legal authorities who must implement competition law, collusion is an ongoing problem that lurks among the millions of business transactions occurring each year in a complex developing economy, but is not always easy to find or even define.

History, as well as common sense, tells us that businesses will collude and economic theory teaches us that collusion, especially formal cartels, when it is effective, reduces social welfare.

The main implication of standard cartel theory is that price will be raised above the competitive level. Indeed, most of the literature follows Adam Smith in assuming the sole goal of inter firm cooperation to be a conspiracy against the consumer. More recently, Irwin Stelzer described it as 'a practice without defenders in the economics profession'.

Cartels are the very antithesis of competition, to a successful free market and unfair to the consumers. They allow small and inefficient competitors to join together to enjoy the easy life at the expense of their efficiency, cartels, by definition, have no efficiency-enhancing potential whatsoever.

Conclusion

It is a worldwide accepted notion that cartels have negative effects to the consumers. If we take example of any of the international or national cartels, we can find that the effect of such cartels is an extraordinary price high of the respected goods or services. There are at least 30% to 40% price high occurs due to formation of any cartel. The people have to pay that high amount to avail that respected good or service, though actually that goods cost more less than what the consumers have to pay. So, it is considered as a great detriment to the consumer welfare. For detecting a cartel, the competition authority should have some extraordinary power, .Most of the cartels are formed in secrecy, so the competition authority should posses some special features to detect a cartel, means, they have had something more than what a general investigation agency have.More units of Competition Authority should be formed, with a special wing for cartel detection.More importance should be given to the "leniency programme" and also to the whistle blowing system.Huge penalty should be imposed, with criminalization of the persons involved in a cartel.

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