Policy Position

07 / 2009

TRANSPARENCY INTERNATIONAL
the global coalition against corruption


© iStock

Countering Cartels to End Corruption and Protect the Consumer

Cartels are illegal and costly. They inflate prices for consumers, exact an economic toll on countries and undermine the integrity of companies. Cartels can form in any sector, ranging from health care and transport, to construction and telecommunications. They leave no industry untouched or consumer unburdened. When companies engage in collusion by conspiring to fix prices, markets become inefficient and consumers bear unjustified price hikes that can reach up to 100 per cent.

Cartels destabilise the business environment, generating moral ambiguity, illegality and a climate of corruption. Collusion paves the way for a corporate culture that supports corrupt acts such as the bribery of officials or the creation of slush funds. Secret agreements to fix prices might entail the buying-off of public officials, the manipulation of public procurement processes, or bid-rigging. When these activities become exposed, both consumer trust and business reputation are destroyed.

In the face of such risks, companies must prohibit cartel activities with the same vigour used to combat other forms of corruption. To effectively combat cartels, antitrust and anti-corruption authorities should find new opportunities for collaboration and employ a host of tools that both create incentives for disclosure of cartel activity and apply severe penalties for those who continue to collude.

Table of Contents

What is Collusion?

According to the *TI Anti-Corruption Plain Language Guide*, 'collusion' is "a secret agreement between parties, in the public and/or private sector, to conspire to commit actions aimed to deceive or commit fraud with the objective of illicit financial gain. The parties involved often are referred to as 'cartels'."[5]

The Reach of Cartels in Various Sectors

It seems that no industry is free from collusion. Consumers have been overcharged on products including thermal fax paper (10 per cent overcharge), vitamins (35 per cent overcharge) and stainless steel (100 per cent overcharge). A glimpse at some recent cases demonstrates the reach and impact of cartels.[6]

Construction: In 2007 four companies were fined for rigging bids for procurement contracts, fixing prices and exchanging confidential information in order to control the elevator and escalator market in four European countries. Because escalators and lifts are maintained by the companies that install them, the impact of this cartel may be felt for a further twenty-to-fifty years.[7]

Health: A review of World Bank-funded projects in the Indian health sector found that four European chemical companies allegedly participated in a cartel from 1999-2004 during which time identical bids were submitted to provide anti-malarial insecticide for a US$ 114 million health project. As many as 18 out of 21 awarded contracts in the programme may have been affected by the cartel activity.[7]

Media: In 2007 the Hungarian Competition Authority revealed a cartel agreement between two dominant newspaper distribution companies that led to one agreeing not to enter the market where the other one was active. As the two companies represented a near monopoly of the industry, the arrangement effectively cut out any other competition.

1. A globally damaging practice

Globalised cartel activity has assumed renewed prominence over the last three decades, aided by advances in international communication and supply chains. Even the most trusted household brands, from Bayer to Intel, have been found and fined for participating in price-fixing.[1]

Between 1990 and 2005, 283 private international cartels were exposed. These cartels enjoyed aggregate sales topping US$ 1 trillion and overcharged consumers more than US$ 300 billion.[2] Unfortunately, these figures likely represent a mere fraction of the total economic drain cartels exert on consumers. Estimates suggest that perhaps only one in every six cartels is ever detected.[3]

With weaker antitrust laws and fewer resources for enforcement than industrialised nations, developing countries are especially hard hit by both domestic and international cartels. These countries seem to have received little support from industrialised nations to protect themselves from price-fixing: a 2005 study found that 51 countries, the majority of which belong to the Organisation for Economic Co-operation and Development (OECD), have regulatory frameworks that either explicitly or implicitly tolerate cartels which engage in price-fixing outside national borders and export their illegal practices abroad.

Shortcomings in both domestic and international cartel enforcement have resulted, for example, in Latin America and Asia experiencing higher overcharges from global cartel networks than North America or Europe. By one estimate, just 19 industries involved in international price-fixing schemes were found to have cost developing countries — as a result of inflated prices for key imports — the equivalent of at least 15 per cent of what they had received in foreign aid. With the majority of cartels evading detection, it has been suggested that the economic losses for developing countries could approach or exceed the total amount received through international development assistance.[4]

2. Towards collaborative and innovative solutions

Like bribery, cartels flout the rule of law, undermine standards of business ethics and breed a corporate culture of reckless opportunism. Collusion relies on systematic forms of illegality and deception (e.g. the use of hidden budgets, covert communication or the exchange of confidential information by companies or rogue employees) and opens the door for further corrupt activity.

Dismantling both cartels and the channels for private sector corruption requires greater coordination between antitrust institutions and the anti-corruption movement. As antitrust regulators share information on corporate violators, anti-corruption authorities can be warned early of potential offenders and vice versa. For example, a firm's attempt to bribe officials to obtain a public tender may be a sign of other corrupt activity by the offending company or point to possible collusion in the wider marketplace.

Enhanced communication between anti-corruption and competition authorities also creates opportunities for mutual learning on effective enforcement strategies. With a growing set of innovative tools to confront cartels, competition regulators have particularly valuable strategies and experiences that could be adapted to anti-corruption efforts.

Governments are allowing increased leniency for company self-reporting of cartel activity. From lower fines to full amnesty, such leniency has allowed the European Commission to take action on over 100 companies and collect almost € 3 billion in fines in 2002 and 2003 alone. Monetary rewards have also been used, as in the United States and United Kingdom, to motivate potential whistleblowers to disclose cartels. An additional policy lever has been to make participation in a cartel a crime punishable by imprisonment and/or fines. This increasingly common practice has already been adopted by countries including France, Germany, Ireland, Japan, the UK and the US.

Despite these and other efforts by various governments, enforcement gaps remain. As recently as 2007, median cartel penalties were believed to recoup only around 20 per cent of the estimated overcharges and repeat offenses were common.

Deterring cartels is not simply a question of strengthening legal enforcement and corporate governance. The essential role of civil society should be reinforced through greater collaboration between the anti-corruption movement and consumer groups. Consumer advocates have a long history of mobilising the public and undertaking targeted research to improve antitrust regulation. Governance advocates complement these efforts with substantial expertise and awareness-raising on topics including corruption and corporate integrity. Consolidating the efforts of both movements will enhance knowledge and create opportunities to confront corruption and cartels, holistically and sustainably.

3. Responses

Actions against cartels must be integrated as a critical component within wider efforts to reduce corruption in all areas of business. To achieve this end, TI recommends the following policy responses:

Businesses must:

Strengthen compliance and adopt a zero-tolerance policy towards cartels.

- Price-fixing and collusion must be unequivocally condemned by business. To be sustainable, internal compliance measures to stop cartels must be established.

Encourage employee engagement and provide whistleblower protection.

- Companies must introduce whistleblower clauses that actively encourage employees to report suspected wrongdoing and ensure employees' protection in the work place.

Regulators and governments must:

Refine and expand the use of promising enforcement tools.

- Regulators should continue to use financial and criminal penalties to deter cartels, while creating incentives in the form of leniency or rewards to encourage disclosure.

What are the Fines?

In November 2008 the European Commission imposed over € 1.3 billion in fines on four companies that produced car glass for approximately 90 per cent of the European Economic Area's market. The Antitrust Commission found the companies to have illicitly discussed target prices, market share and customer allocation between 1998 and 2003. The fine is the highest ever imposed by the European Commission.[9]

What are the Jail Sentences?

In April 2009 the US Department of Justice (DOJ) moved forward in an ongoing investigation into price-fixing of LCD television panels. Four companies and nine individuals were charged. In addition to fines totalling US$ 616 million, four executives received prison sentences.[10]

In a second ongoing investigation, the DOJ announced that 15 airlines from all over the world and four airline executives pleaded guilty, or agreed to plead guilty, to charges of price-fixing cargo rates to and from the United States. Aggregate fines totalled US$ 1.6 billion and the four executives were given jail time for their involvement.[11]

This policy position draws on the TI Global Corruption Report 2009: Corruption and the Private Sector. It is one of four papers based on the Report. The others cover corporate integrity, regulatory policies and corporate lobbying. All facts and figures, unless otherwise stated, are cited from the Report.

The GCR 2009 brings together more than 80 leading experts and practitioners to explore a wide range of corruption risks in and solutions for the private sector. To learn more, see: www.transparency.org/publications/gcr.

To purchase this and other GCRs in the series, visit Cambridge University Press at www.cup.cam.ac.uk.

TRANSPARENCY INTERNATIONAL

Telephone

+49-30-343820 -0

Fax

+49-30-347039 -12

International Secretariat

Alt-Moabit 96

10559 Berlin

Germany

PRINTED ON RECYCLED PAPER

TRANSPARENCY INTERNATIONAL
the global coalition against corruption

- Competition authorities should develop innovative methods to discourage cartels, for example, by removing companies convicted of cartel activity from ethical indices or investment funds.
- In the field of public procurement, governments can explore opportunities to establish anti-cartel coalitions that commit suppliers to high standards of integrity and honesty.

Coordinate between regulatory bodies, across sectors and internationally.

- Anti-corruption and anti-competition authorities must seek out opportunities for mutual learning and create effective systems to share information on offending companies. Coordination must transcend national borders.

Civil society, citizens and consumers must:

Mobilise consumer action and forge coalitions.

- Consumers can harness their purchasing power and organise collectively to send a strong signal that collusion will not be tolerated.
- Consumer advocates and corporate governance groups will pack a stronger punch by sharing knowledge and collaborating on campaign efforts to generate public awareness of the costly impacts of cartels.

Monitor cartel activity as part of overall company assessments.

- Tracking cartel involvement and corrupt activity as a pillar of corporate responsibility sends a clear message that such behaviour is as illegal, unfair and unacceptable as inappropriate social, environmental or economic actions taken by a company.

References:

[1] For Bayer, see: 'Bayer pays $33 M to settle price fixing case', Pittsburgh Business Times, 30 September 2004. www.bizjournals.com/pittsburgh/stories/2004/09/27/daily39.html. For Intel, see: Fu Yun Chee and David Lawsky, 'EU hands down record antitrust fine to Intel', Reuters, 13 May 2009. www.reuters.com/article/topNews/idUSTRE54C1SO20090513.

[2] Of the 283 private international cartels uncovered between 1990 to 2005, more than half were found to be repeat offenders.

[3] OECD, Hard Core Cartels: Recent Progress and Challenges Ahead (Paris: OECD, 2003).

[4] M. Levenstein, L. Oswald and V. Suslow, 'International Price-fixing Cartels and Developing Countries: A Discussion of Effects and Policy Remedies', Working Paper no. 53 (Amherst, MA: Political Economy Research Institute, University of Massachusetts, 2003).

[5] Transparency International, 'The Anti-Corruption Plain Language Guide' (Berlin, TI, July 2009).

[6] European Commission, 'Competition: Commission fines members of lifts and escalators cartels over €990 million', Press release, 21 February 2007.

[7] M. Voith, 'Collusion Alleged among Pyrethroid Makers', Chemical & Engineering News, 24 January 2008.

[8] K. Hetényi and F. Urlesberger, 'Hungary: The Amendment is Pending', International Financial Law Review, 1 October 2008.

[9] European Commission, 'Antitrust: Commission fines car glass producers over €1.3 billion for market sharing cartel', Press release, 12 November 2008.

[10] US Department of Justice, 'Korean executive agrees to plead guilty and serve one year in prison for participation in LCD price-fixing conspiracy', Press release, 29 April 2009.

[11] US Department of Justice, 'Dutch airline executive agrees to plead guilty for fixing prices on air cargo shipments', Press release, 29 April 2009.

Transparency International (TI) is the civil society organisation leading the global fight against corruption. Through more than 90 chapters worldwide and an international secretariat in Berlin, Germany, TI raises awareness of the damaging effects of corruption, and works with partners in government, business and civil society to develop and implement effective measures to tackle it. For more information go to: www.transparency.org

ISSN 1998-6432