

Enforcement Issues in Antitrust and Merger Review

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European Competition Amsterdam Seminar
Amsterdam, June 5, 2008



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1. Managerial Incentives in Antitrust Enforcement

- Design of compliance programs – avoidance
 - Dark side of incentive compensation
 - Forensic cartel audits
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- Incentives to set priorities in enforcement
 - Information to target sanctions at individuals
 - Asymmetry in plea bargaining negotiations





PRICE FIXING, BID RIGGING, AND MARKET ALLOCATION SCHEMES: WHAT THEY ARE AND WHAT TO LOOK FOR

An Antitrust Primer

This primer briefly describes the most common antitrust violations and outlines those conditions and events that indicate anticompetitive collusion.

Introduction

American consumers have the right to expect the benefits of free and open competition — the best goods and services at the lowest prices. Public and private organizations often rely on a competitive bidding process to achieve that end. The competitive process only works, however, when competitors set prices honestly and independently. When competitors collude, prices are inflated and the customer is cheated. Price fixing, bid rigging, and other forms of collusion are illegal and are subject to criminal prosecution by the

Federal Antitrust Enforcement

Enacted in 1890, the Sherman Act is among our country's most important and enduring pieces of economic legislation. The Sherman Act prohibits any agreement among competitors to fix prices, rig bids, or engage in other anticompetitive activity. Criminal prosecution of Sherman Act violations is the responsibility of the Antitrust Division of the United States Department of Justice.

Violation of the Sherman Act is a felony punishable by a fine of up to \$10 million for corporations, and a fine of up to \$350,000 or 3



Detecting Bid Rigging, Price Fixing, And Other Types Of Collusion

Bids

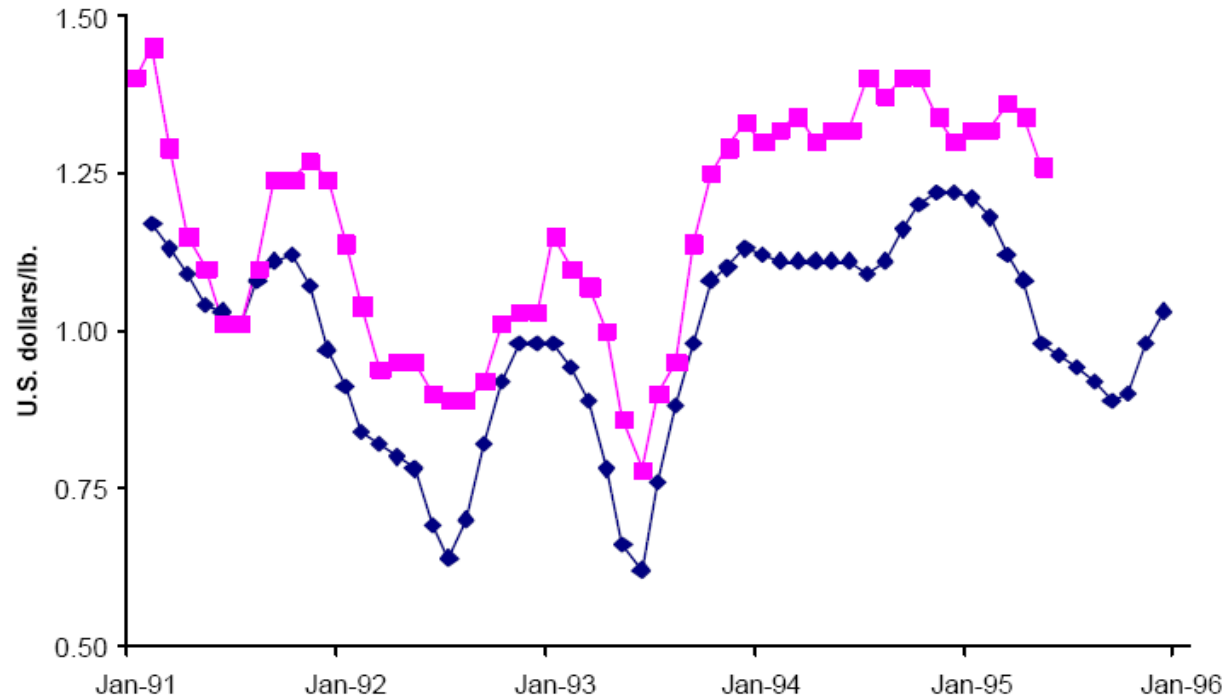
- A company appears to be bidding substantially higher on some bids than on other bids, with no apparent cost differences to account for the disparity.
- Bid prices drop whenever a new or infrequent bidder submits a bid.

Prices

- Identical prices may indicate a price-fixing conspiracy, especially when:
 - Prices stay identical for long periods of time.
 - Prices previously were different.
 - Price increases do not appear to be supported by increased costs.



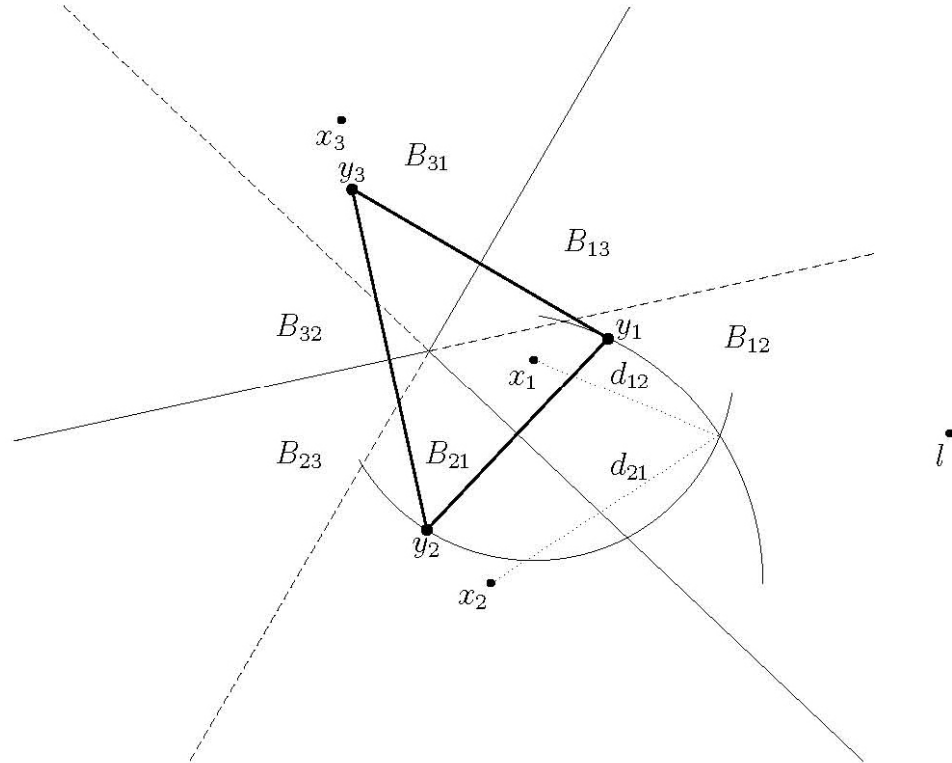
Figure 1. Lysine Transaction Prices, U.S. and EU Markets, 1991-1996.



Source: Connor (2007)



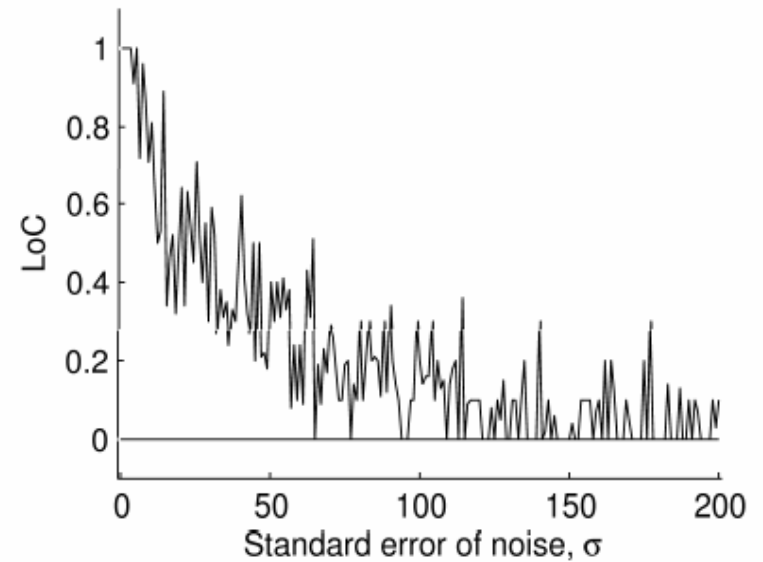
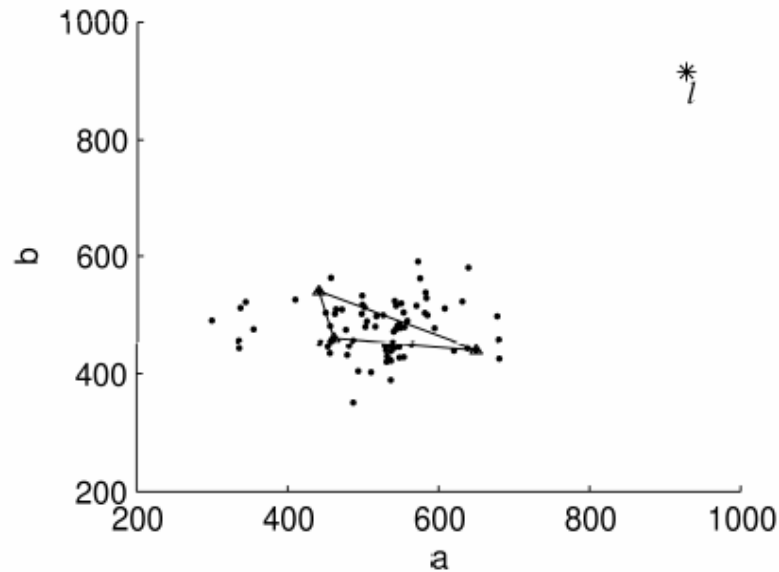
Bird's-eye view of basing-point pricing



Source: Schinkel and Bos (2008)



Testing for collusive basing-point pricing



Source: Schinkel and Bos (2008)



2. Private Litigation for Antitrust Damages

- Commission's recent White Paper quite considerate
- Damages are typically dispersed in the chain
- Upstream damages so far little acknowledged

- Risk of undisclosed settlements with direct purchasers

- Antitrust damages often multi-dimensional:
 - Non-linear pricing and pay-back schemes
 - Unexploited scale economies
 - Restricted entry
 - (Poor quality and little R&D)



Damages tend to get dispersed in the chain of production

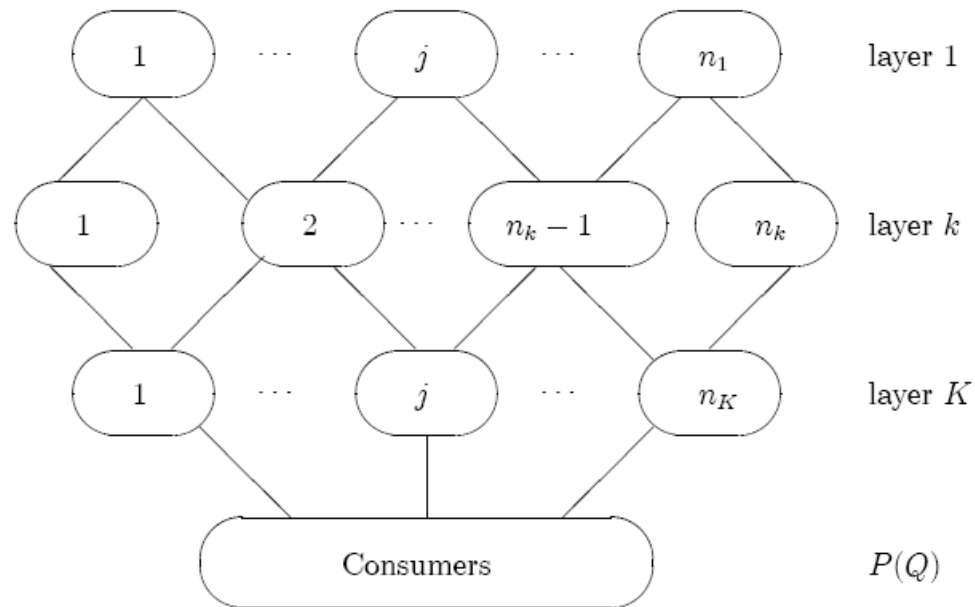


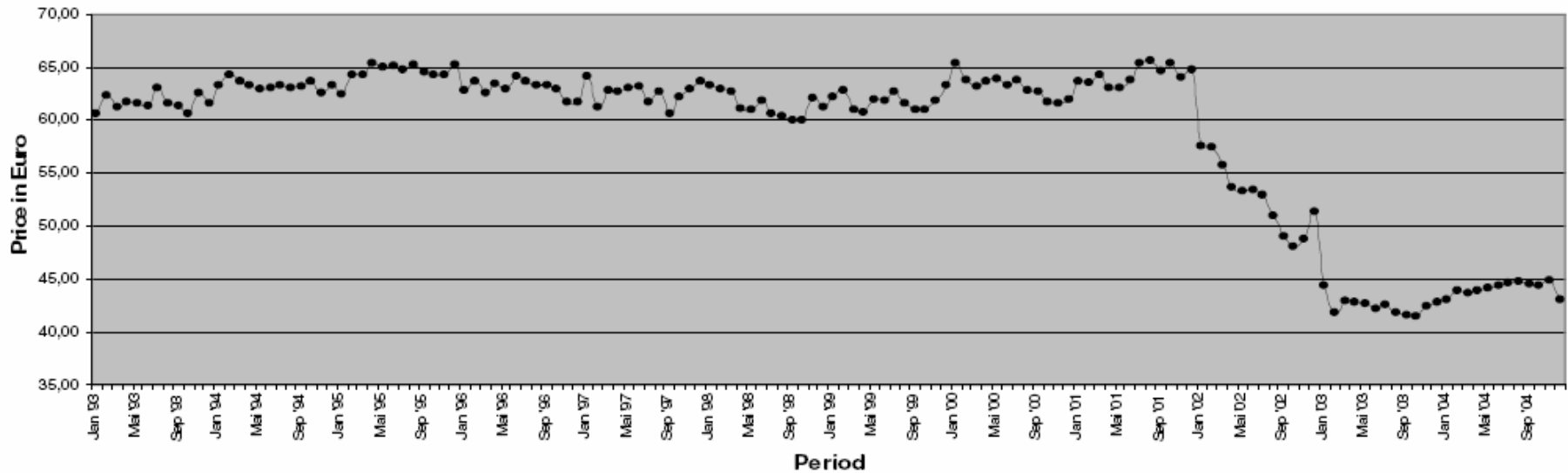
Figure 1: A vertical chain of production.

Source: Han, Schinkel and Tuinstra (2008)



Unit prices net of non-linear pricing parts

Price development (weighted average price)
Freight included in prices



Source: CDC, Classen (2007)



3. Quantifying Efficiency Defenses in Merger Control

“The Commission considers any substantiated efficiency claim in the overall assessment of the merger. It may decide that, as a consequence of the efficiencies that the merger brings about, there are no grounds for declaring the merger incompatible with the common market pursuant to Article 2(3) of the Merger Regulation. This will be the case when the Commission is in a position to conclude on the basis of sufficient evidence that the efficiencies generated by the merger are likely to enhance the ability and incentive of the merged entity to act pro-competitively for the benefit of consumers, thereby counteracting the adverse effects on competition which the merger might otherwise have.” (Commission of the European Communities, 2004, Paragraph 77)



The Werden-Froeb-Index

- Compensating marginal cost reductions (CMCRs)

$$WFI = \frac{\sum_{i=1}^{n_I} q_i \Delta c_i}{\sum_{i=1}^{n_I} q_i c_i} = \frac{\Delta \mathbf{c} \cdot \mathbf{q}^{(n_I)}}{\mathbf{c} \cdot \mathbf{q}^{(n_I)}},$$

- Quite general
- Low information requirements
- Suitable for a pre-Phase II filter
- Easy to implement



The WFI complements HHI-analysis

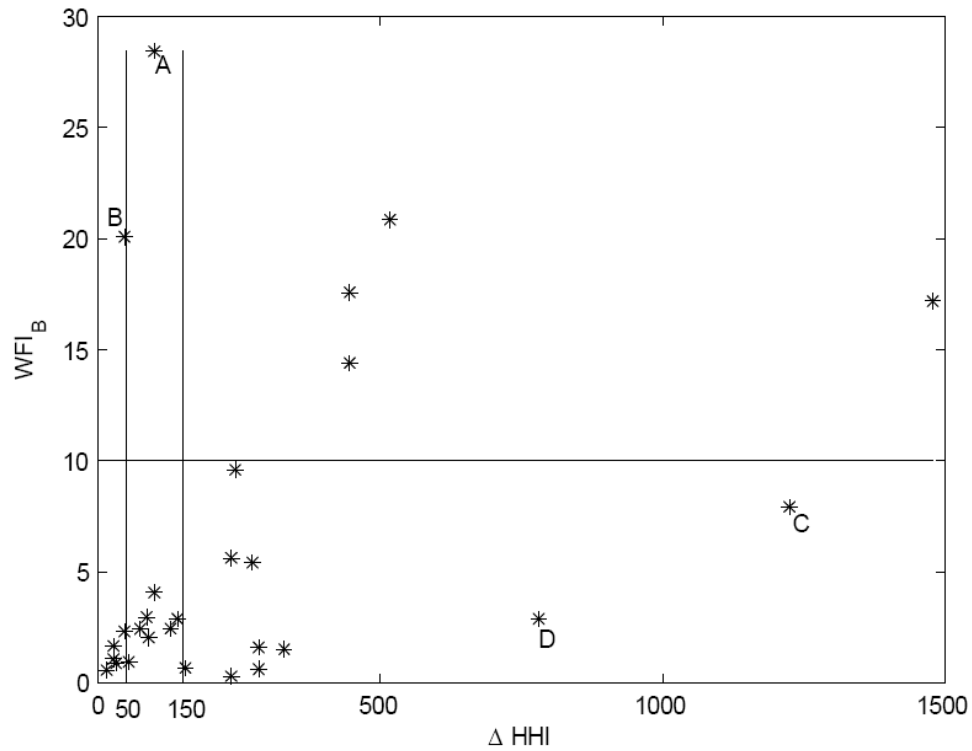


Figure 1: WFI_B versus ΔHHI for representative mergers.



4. Antitrust Fines

- 2006 EC Fining Guidelines
- Deterrence an explicit objective (recitals 30-31)
- Affected value of sales as a base
- Potential for harsh fines – possibly too harsh in cases
- Clear and simple – yet with quite some room for discretion



Implied Fine Formula in 2006 EC Fining Guidelines

$$F = \overbrace{(30\% \times \eta \times n + 25\% \times \kappa)}^{\text{Basic amount}} \times \underbrace{p^a Q^a}_{\text{Value of sales}} \times \underbrace{\theta^a \times \theta^m}_{\text{Adjustments}}$$

$0 < \eta \leq 1$	gravity (recitals 21-23)
n	number of years (recital 24)
$\frac{3}{5} \leq \kappa \leq 1$	'entrance fee' (recital 25)
$1 \leq \theta^a \leq 2$	aggravating circumstances (recital 28)
$0 < \theta^m \leq 1$	mitigating circumstances (recital 29)

Source: Bos and Schinkel (2006)



Some Observations on the Method of Setting Fines

- Some short-cuts – no full effects analysis:
 - Value of sales develops over the business years
 - Sales “indirectly” related to infringement
- 10% maximum (Art.23(2) Regulation 1/2003) *very* often binding
- Maximum protects firms deeply involved in cartel activity
- ‘Antitrust fining-curve’ is inverted U-shape
- Substantial reductions on appeal (25% of fine)



Share of affected value of sales beyond which legal 10% maximum is binding

