



COMPETITION ACT, 2002

AND

SHIPPING LINER CONFERENCES

PRESENTATION

BY

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DISCLAIMER

This presentation is intended to highlight, for discussion purposes, the competition related issues arising from liner conferences.

It does not necessarily reflect the views of the Competition Commission of India.

The presentation is subject to likely amendments in the Competition Act, 2002.

Organization Of The Presentation



1. What is Competition ?
2. Competition Act, 2002
3. Cartels
4. Liner Conferences
5. Adverse Effects of Conferences

What is Competition ?

- Competition refers to economic rivalry amongst enterprises to control **market** for products (goods and services)
- Level of Competition does not depend upon number of players in an industry but on degree of **contestability**
- **Contestability involves ease of entry and exit**
- Concept of relevant market: **Relevant geographical market and relevant product market**



Economics of Competition

- **In the market structure spectrum Competition lies in one extreme and Monopoly at the other extreme**
- **In between are oligopoly and monopolistic competition**
- **Under perfect competition consumer is the king and Consumer surplus is maximised**
- **Monopolist is able to maximise his profits either by limiting production or by dictating price or by both, using his monopoly/market power**
- **This results in deadweight losses**



Economics of Competition

- Competition results in economic efficiency through:
 - Allocative efficiency >> 'pareto optimality'
 - Productive efficiency >> Avoidance of 'X-Inefficiency' (Leibenstein)



Benefits of Competition

Competition in markets:

- ♥ promotes efficiency;
- ♥ leads to higher productivity
- ♥ punishes the laggards;
- ♥ enhances choice, improves quality,
reduces costs;
- ♥ facilitates better governance;

Competition is benign



For consumers:

- lower prices
- improved quality
- better services
- wider choice

For business:

- availability of inputs at competitive price,
- level playing field,
- redressal against denial of market access and other anti-competitive practices

Empirical evidence of benefits

- Australia:
 - Average household income was up by A\$ 7,000/- per annum on account of the competition policy (APC study quoted by OECD).
 - Gains from reform ~ 5.5% of GDP (Paul Crampton, OECD-IADB).
- EU: White Paper on Growth, Competitiveness and Employment, 1993-Ensuring fair competition in market is essential ingredient for enhancing and maintaining competitiveness in economy.
- New Zealand, UK: Pro-competition policy in New Zealand and UK added around 2.5% to their employment rate over 1978-1998 (OECD).
- USA: Fall in prices following deregulation of certain industries.(OECD) In 1990s, competition contributed most to economic growth; raised productivity by 4% p.a. (Paul London).
- **India: Benefits since reforms - increased consumer welfare, enhanced growth, greater competitiveness.**



Competition the key driver



COMPETITION ACT, 2002



Duties of Competition Commission

Competition Act, 2002 notified in Gazette in January, 2003. Preamble's stated objective is to establish the Commission which is to:

- Eliminate practices having adverse effect on competition;
- Promote and sustain competition
- Protect consumers' interests
- Ensure freedom of trade carried on by other participants in markets, in India

[Section 18]



Main Features of Competition Act - 1

With the above objective, the Act:

- Prohibits Anti - Competitive Agreements.
- Prohibits Abuse of Dominant Position.
- Provides for Regulation of Combinations, and
- Enjoins Competition Advocacy

[Sections 3, 4, 5, 6 and 49(3)]



Main features of Competition Act - 2

- **Agreements**

- > **Horizontal Agreements**, including **cartels**

- Four types presumed to have appreciable adverse effect on competition (Similar to per se treatment)*

- Price fixing**

- Bid rigging**

- Quantity limiting**

- Market sharing**

- > **Other horizontal agreements** and **Vertical Agreements**:

- Assessed based on 'rule of reason'*

- Vertical agreements include: Tie in, Refusal to deal, exclusive supply arrangement, exclusive distribution arrangement, resale price maintenance,



Dominance - 1

- Position of strength enjoyed by an enterprise in the **relevant market** which enables it to:
 - Operate independently of competitive forces prevailing in relevant market or
 - Affect its competitors or consumers or the relevant market in its favour
- Ability to prevent effective competition and
- Ability to behave independently of two sets of market actors, namely:
 - Competitors
 - Consumers



Dominance - 2

Factors To Be Considered In Determining

Dominant position linked to a host of factors

- Market share of enterprise
- Size and resources of enterprise
- Size and importance of competitors
- Commercial advantage of enterprise over competitors
- Vertical integration
- Dependence of consumers
- Dominant position as a result of a statute
- Entry barriers
- Countervailing buying power
- Market structure and size of market
- Social obligations and costs
- Contribution to economic development
- Any other factor



Dominance - 3

Abuse Of Dominance

- Imposing **unfair** or **discriminatory price** or **condition** in purchase or sale, including predatory pricing
- Limiting production or scientific development to the prejudice of consumers
- Denial of market access in any manner
- **Conclusion of contract subject to supplementary obligations**
- **Use of position in one relevant market to enter into or protect other relevant market**

Abuses are of two types:

- > Exploitative (predatory pricing, e.g.)
- > Exclusionary
(interference with competitive process)



Remedies

- Cease and desist order
- Specifying future terms and conditions
- Imposition of penalties
- Award of compensation/damages
- Structural remedies include ‘division of enterprise’
- Such other order as may be deemed appropriate by Commission

Combinations -1



- Combination covers
 - ❑ Merger & Amalgamation
 - ❑ Acquisition
 - ❑ Acquiring control
- Any combination which causes or is likely to cause appreciable adverse effect on competition (AAEC) is void



Combinations - 2

Remedy And Order Of The Commission

Competition Commission of India can:

- Approve
- Approve with modifications
- Not approve

If no order within 90 days, the combination is deemed to have been approved.

- Structural as well as behavioural remedies



Competition Advocacy

- **With Government/Regulators**, to promote pro-competition policies, laws, regulations
- **Competition principles interface with policies relating to: disinvestment, concessions, industrial policy, international agreements, entry/exist policies etc.**
- **Public awareness:** with industry, trade associations etc. to strengthen competition culture and improve compliance
- Under Sec 49 Central Government may make references to the CCI on competition policy and law issues. CCI is required to give opinion in 60 days. CCI opinion advisory
- Under Sec 21 statutory authorities may make references to CCI on competition issues. CCI opinion advisory
- DG (Sh) as regulator can also make a reference for an Inquiry (Sec. 19)

Coverage Of The Act



- Government Departments covered (in CA, 2002), except when engaged in discharge of sovereign functions and Currency, Atomic energy, Space and Defence
- Extra-territoriality (Sec. 32)
- Provision to enter into MOUs with foreign competition authorities

CARTELS

What are cartels ?



As per Competition Act, 2002:

- “ Cartel includes an association of producers, sellers, distributors, traders or service providers who, by agreement amongst themselves, limit, control or attempt to control the production, distribution, sale or price of, trade in goods or provision of services” Sec. 2 (c)*
- Cartels are in the nature of prohibited horizontal agreements and are presumed to have appreciable adverse effect on competition

Some Noted Cases Of Cartels In India: Under MRTPA



SODA ASH CARTEL

- In September, 1996, American Natural Soda Ash Corporation (ANSAC) comprising of six American producers of soda ash attempted to ship a consignment of soda ash at cartelized price to India.
- Based on the ANSAC membership agreement, the M.R.T.P. Commission held it as a prima facie cartel and granted interim injunction in exercise of its powers in terms of Section 14 of the M.R.T.P. Act. The Supreme Court, however, overturned the order of the Commission inter alia, on the ground that it did not have authority to prohibit imports

Some Noted Cases Of Cartels In India: Under MRTPA



TRUCKING CARTEL

- Eliminating competition in the market by fixing the freight rates without liberty to the members of the truck operator union to negotiate freight rates individually is common in the trucking industry.
- The M.R.T.P. Commission passed 'Cease & Desist' order against Bharatpur Truck Operators Union, Goods Truck Operators Union, Faridabad, and Rohtak Public Goods Motor Union.
- In the absence of any penalty provision, however, no fines could be imposed.

Detecting Cartels Not Easy



- **Cartels being secretive and cartelists taking pains to conceal it necessitates the Competition Authorities to undertake great efforts to detect concealed cartels;**
- **Competition Authority needs special powers and skill to collect sufficient evidence to mount a viable case against uncooperative defendants;**
- **Cartels are conspiracies and to destabilize them, Competition Authority needs to heavily bank upon “Leniency Programme”**

Detecting Cartels



- **Competition Commission of India (CCI) is empowered to inquire into any anti-competitive agreement, including cartels of the four types, mentioned under Section 3(3) {Section 19 & 26, & 36(2)}**
- **Director General of CCI is empowered to investigate into cartels and has the powers of a Civil Court for summoning and enforcing attendance of any person and examining him on oath; requiring the discovery and production of documents; receiving evidence on affidavits; issuing summons for the examinations of witnesses or documents; requisitioning any public record or document or copy of such record or document from any office. {Section 41(1) & (2)}**

Detecting Cartels



- Director General of CCI has powers as are vested in the 'Inspector' in terms of Section 240 & 240 A of the Companies Act, 1956.
- These powers inter-alia include - production of documents and evidence in the custody of body corporate/other bodies corporate, and search of place or places and seizure of documents with the approval of the First Class Magistrate/Presidency Magistrate, having jurisdiction, when there is reasonable ground to believe that books, papers or documents may be destroyed, mutilated, altered, falsified or secreted. **{Section 41(3)}**

Deterrence & Penalty Against Cartels



- CCI is empowered to pass following orders against anti-competitive agreements including cartels :
- Grant temporary injunction or restraint order – during the pendency of inquiry.
{Section 33(1)}
- Cease and desist order - directing offending parties to a cartel to discontinue and not to repeat such agreements.

Deterrence & Penalty Against Cartels



- **Modification of agreement** - directing offending parties to modify the agreements to the extent and in the manner as may be specified in the order.
- **Payment of costs etc.** – direct the enterprises concerned to abide by such orders as the Commission may pass and comply with the directions, including the payment of costs.
- **Heavy penalty** – imposing on each member of cartel, a monetary penalty equivalent to three times of the amount of profits made out of such agreement by the cartel or 10% of the average of the turnover of the cartel for the last preceding three financial years, whichever is higher. {Section 27(a) (b) (d) (e) & (g)}

Detecting A Cartel – Leniency/ Amnesty Schemes



- **When a member of Cartel breaks the rank and makes full, true and vital disclosures which results in bursting the ‘Cartel’, the Commission has been empowered to levy lesser penalty.**
- **The scheme is designed to induce member of a Cartel to defect from the cartel agreement.**
- **The party making disclosure will, however, be subject to other directions of the Commission as per provisions of the Act.**
- **Clarity, certainty and fairness are critical to make leniency programme effective and for this Commission can take suitable measures including formulation of Guidelines etc.**

{Section 46}

Effectiveness of CCI against Cartels



- **CCI can be effective at addressing cartel menace because of:**
 - **The availability of explicit definition of ‘Cartel’,**
 - **Incorporation of a leniency programme for members of a cartel to defect**
 - **Power to impose deterrent penalty linked with profits or turnover on each member of the cartel**
 - **Explicit provisions to exercise jurisdiction in respect of overseas acts having adverse effects on competition in India coupled with provisions to enter into cooperation agreement with contemporary overseas competition agencies**
 - **Efforts to build strong competition culture including encouragement to public to submit information by ensuring confidentiality,**

Impact Of Cartels - International Context - 1



- **There is worldwide recognition and consensus that Cartels harm consumers and damage economies.**
 - **Japan has estimated that recent cartels raised prices on average by 16.5 percent.**
 - **In Sweden and Finland, competition authorities observed price declines of 20-25 percent following enforcement action against asphalt cartels.**
 - **The football replica kits case in the United Kingdom has resulted in long-term price reduction to the extent of 30 percent following the OFT's enforcement action.**
- *(Source - Hard Core Cartel: Third Report on the implementation of the 1998 recommendation © OECD 2006)*

Impact Of Cartels

International Context - 2



- In Israel, the competition authority observed that prices declined by approximately 40-60 percent after it uncovered a bid rigging cartel among envelope producers.
- Estimates in the United States suggest that some hard core cartels can result in price increases of up to 60 or 70 percent.
- Based on a review of a large number of cartels, it is estimated that the average overcharge is somewhere in the 20–30 percent range, with higher overcharges for international cartels than for domestic cartels.
- *(Source - Hard Core Cartel: Third Report on the implementation of the 1998 recommendation © OECD 2006)*

Cartels

International Cases



COLLUSIVE PRICE FIXING BY BOATERS :

- **Siem Reap in Cambodia is a very popular tourist town, which houses the famous Angkor Vat temples. There are three means of transportation from Phnom Penh to Siem Reap – boat, road and air. The competition between boat companies has been intense and the prices came down from US \$ 10 to US \$ 5. The boaters discussed among themselves and resolved that they will charge US \$ 10 from Khmer nationals and US \$ 20-25 from foreigners.**
- **They further agreed that they would not compete with each other and would share their departure schedules. There was no written agreement and only an understanding and it constitutes a cartel agreement.**

Cartels

International Cases - 2



LYSINE CARTEL

- **Lysine is an amino acid that stimulates growth and results in leaner muscle development in dogs, poultry and fish. It is also mixed with corns and is an input for feed products.**
- **Between 1992 and 1995, five producers belonging to Japan, Korea and US controlling more than 97% of the global capacity engaged in price fixing, allocation of sales quota and monitoring of volume agreements. The DoJ undertook searches with the cooperation of FBI and on the basis of subpoenaed documents together with tape recordings of meeting of the conspirators could make out a strong case of colluding on lysine prices around the world for three years.**

Cartels

International Cases - 3



- **AIRLINES CARTEL**
- **There was allegation that four airline companies had conspired to simultaneously announce in May, 2004 a fuel surcharge in identical amounts in South Africa.**
- **After the investigation, prompted by news reports of the price increase, an airline applied to the Competition Commission for leniency under the Commission's Corporate Leniency Policy.**
- **The applicant cooperated with the Commission and was not cited as a respondent and the Commission recommended a fine up to 10% of the turnover of each of the respondent.**

Vigorous Enforcement Against Cartels



- **OECD Report On Hard Core Cartels - Third Report On The Implementation Of The 1998 Recommendation, 2005 has documented that efforts to fight domestic and international cartels have advanced in many respects**
- **Legislative changes in several member countries have conferred greater investigative powers on competition authorities, authorized stiffer sanctions, and increased the opportunities to effectively cooperate with foreign competition authorities.**

Vigourous Enforcement Against Cartels



- **More competition authorities have created specialized cartel units and/or prioritized the fight against cartels among their activities.**
- **High fines are imposed on a regular basis.**
- **Cooperation has become much more common.**
- **Exchanges of cartel enforcement know-how have intensified.**
- **Much remains to be done.**

SHIPPING CONFERENCES

What is a shipping liner conference ?



- EU Regulation 4056/86 defines liner conference as:
 - “ ... A group of two or more vessel-operating carriers which provide international liner services for the carriage of cargo on a particular route or routes within specialized geographical limits and which has an agreement or arrangement, whatever its nature, within the framework of which they operate under uniform or common freight rates and any other agreed conditions with respect to provision of liner services”
- Exemptions for agreements between carriers (liner conferences) granted by EC were subject to *conditions* attaching to exemption and *obligations* attaching to exemption

Shipping Conferences



- Though Shipping Conferences are waning, they still remain an important factor in many trades
- Micco and Perez (2001: p 3) claimed that, in 1997, import freight costs represented 5.25 per cent of world imports (fob)

Shipping Conferences



- Rate levels important because transport costs have a chilling effect
- Limao and Venable (2000) estimated that raising transport costs by 10 per cent can reduce volume by more than 20 per cent
- Radelet and Sachs (1998) showed that “doubling shipping cost (e.g. from 8 per cent to 16 per cent *cost, insurance and freight, or CIF, band*) is associated with slower annual growth of slightly more than half of one per cent point

Shipping Conferences



- Manufactured export sector is more gravely affected because access markets is an important determinant of growth for countries that have an assembly-manufacturing sector.
- Clyde and Reitzes (1995) found in the context of the US that increased market concentration in the shipping sector led to higher freight rates as well as greater price discrimination on the basis of commodity value
- Micco (2001) found that shipping conferences exerted some mild monopoly power

Shipping Conferences



- A World Bank study in 2000 by Fink, Mattoo and Neagu estimated that the average total cost reduction in transport prices with the break up of carrier agreements would be 25 per cent (for US)
- Liner ships may organize themselves into cartels, consortia, alliances or joint ventures
- They may result in information exchange which may facilitate concerted action that are anti-competitive in nature

What is a consortium ?



Consortium is defined, Art. 2 (1), Regulation 823/2000 (EC) as follows:

“.. An agreement between two or more vessel-operating carriers which provide international liner shipping services exclusively for the carriage of cargo, chiefly by container, relating to one or more trades, and the object of which is to bring about co-operation in the joint operation of a maritime transport service, and which improves the services that would be offered individually by each of its members in the absence of the consortium in order to rationalize their operations by means of technical, operational and/or commercial arrangements , with the exception of price fixing”

Consortia



- Joint ventures, global alliances and mergers have resulted in concentration in the liner shipping sector going up over the years.
- While in 1998 twenty (20) leading carriers in the liner sector controlled 35 per cent of the world container capacity, this figure exceeded 72 per cent by 2000 (OECD, 2001)
- While concentration, by itself is not anti-competitive, higher concentration levels tend to create dominant players who may abuse their dominant position.

Conference Practices*



- Steps to control competition between member shipping companies:
 - Price discrimination
 - Price and output rules
- Loyalty contracts (to prevent shippers from using non member shipping lines)
 - Dual rate system
 - Fidelity rebate system (4-6 months)
 - Deferred rebate system
- Predatory pricing (to eliminate non-member shipping companies)

* Source: Report of the Study Group on Regulations And Competition Policy, Japan

Adverse Effects of Conferences - 1



- Conferences have inefficiencies generally attributed to cartels
 - Static inefficiencies
 - Productive inefficiencies
 - Lack of innovation
 - Inefficient rent seeking

Case for Exemption For Conferences - 1



Price Stability ?

- Not been found to be factually & historically correct
- Many shipping contracts now include mechanisms to pass on the risk of major variable changes, such as currency and fuel price fluctuations, to shippers
- Indeed, OECD (2001) found that there have been annual swings, in the region of 200 per cent on some European trades
- OECD (2001) found that there may, in fact, be proof to the contrary
- At any rate the major concern of shippers is not price instability as such but high price
- Price stability should be left to the market forces to achieve

Case for Exemption For Conferences - 2



Regular services ?

- The argument that cartelization would enable regular services (by allowing economies of scale), may only be theoretically true
- Even if it is true it may be possible for customers to use a freight forwarder, rather than to allow a cartel. Freight forwarders could align the requirements of customers with the nearest independent sailing

EFFECTS
OF
SHIPPING
CONFERENCES

Effects of Conferences: India - 1



- More than 90 per cent of the India's merchandise trade by volume and more than 70 per cent by value are transported by ships
- **Conferences** being in the nature of cartels may be subject to presumption of 'appreciable adverse effect on competition'.
- Burden of proof is on the conference concerned to prove it to be otherwise

Effects of Conferences in India - 2



- **Alliances, consortia and joint ventures** are also in the nature of horizontal agreements.
- Their acts would be judged by the Competition Commission of India based on facts

Effects of Conferences in India - 3



- **Price increases:** Conferences announce increase in prices from time to time. IBPC reportedly announces increases from time to time under Rate Restoration Initiative
- A conference rate increase of US\$ 600/20' and US\$ 1200/40' reportedly being implemented in three stages by IBPC as follows:
 - 1st May 2007 an increase of US\$ 200/20' and US\$ 400/40'
 - 1st July 2007 an increase of US\$ 200/20' and US\$ 400/40'
 - 1st Sept.2007 an increase of US\$ 200/20' and US\$ 400/40'

Effects of Conferences in India - 4

- Such concerted action may be tantamount to price fixing
- IPBC Conference reportedly sets the THC rates in the Indian ocean region
- Such rates tend to become standard rates for other liners as well
- Such price increases reduce the competitive edge of Indian products
- There is strong demand that freight charges and shore side charges need to be separated

Effects of Conferences in India - 5



- Freight rates are raised unilaterally. Results in uncertainty
- Conferences reportedly tend to impose other extraneous surcharges during peak time such as roll over charges, peak season surcharge, fuel surcharge, which, it is argued, are generally above the 'reasonable' increase in freights that may be expected when demand increases more than supply
- In case such conferences are dominant players in the relevant shipping market they may be accused of abuse of dominant position

Effects of Conferences in India - 6



- While the presence of Indian ship owners in the system of conference is insignificant, the negative effects of concerted action by conferences are felt by Indian shippers and exporters and importers
- Bunker adjustment factor (BAF), Currency Adjustment Factor (CAF), and Terminal Handling Charges (THC) are basically the major regular surcharges recovered from the shippers
- Documentation fees, equipment –related charges like repositioning of empties, transfer fees insurance, cleaning etc are other charges recovered as ancillaries

Move Towards Competition In Shipping



- **EC** : Phasing out of block exemption for conferences by October 2008
- **US** : Review of Immunity, by Anti Trust Modernization Commission.
- **JAPAN** : Immunity exists. But granted on a case by case basis.
Abolition of Special Shipping Designation (2006)
- **Australia** : Part X under review. Productivity Commission recommended repeal of Part X
- **PR China** : No exemption to shipping

Move Towards Competition In Shipping

- Thailand : Shipping no longer exempt
- South Korea : Exemption exists. Action by EC and US will guide Government before acting on KFTC advice
- India : Competition Act, 2002 does not exempt Shipping Conferences

THANK YOU