Monographs on Investment and
Competition Policy, #8

#0109

कट्स CUTS

# Competition Policy & Law Made Easy

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# *Introduction*

Consumers gain a lot from healthy competition in the market. This is because of two reasons: first, competition enables the firms to operate efficiently and second, competition offers consumers a greater choice of products at lower prices. This, in turn, leads to higher benefits to the consumers and helps in economic growth and development.

However, to ensure that consumers enjoy maximum benefits, competition must be maintained in the market. This is ensured through a sound competition policy, of which competition law is an integral part. Herein comes the role of the Government: Government, in general, and the competition authority in particular. They should keep an eye on the market behaviour and use several tools to promote competition on one hand, and check anti-competitive practices, on the other. Thus the national interest and the consumers' interest rather than individual producer's interest are protected.

More so, consumers and their representatives themselves have to be alert in order to keep the government as well as the competition authority of their country active in implementing competition rules. This becomes more important in the liberalised era, where less regulated market players are well informed and organised, while consumers are still ignorant and unorganised.

This publication aims at generating minimum amount of awareness that could be helpful for a common person to identify anti-competitive practices in the market place and take action to rectify the same.

It is divided into three sections. Section I introduces 'competition' and describes its various facets like types, advantages, etc. Section II, which forms the main part of the document, describes various types of hurdles to competition and illustrates them with suitable examples in the form of real cases. Finally, Section III introduces the competition law and policy to the reader.

# I. Competition

### What is Competition?

According to the English language dictionary, *competition* is an event or a contest in which people fight for superiority or supremacy.

In the market, competition is taken as a process whereby firms fight against each other in order to secure customers for their products by adopting any means (fair or unfair).

### Advantages of Competition

Competition drives firms to become more efficient and to offer a greater choice of products at lower prices because of the fear that only the fittest will survive in the market. This ensures best possible utilisation of available resources. Since consumers' purchasing power increases as a result of lower prices, consumers are better off. For example, a poor person used to buy battery cells for Rs 5 each. Due to competition the prices have come down to Rs 2. The poor fellow saves Rs 3 which s/he uses to buy something else.

### Ways of Competition

- *Fair Competition:* This relates to the adoption of fair means by firms, such as producing quality goods, becoming cost-efficient, optimising the use of resources, adopting the best available technology, investing in research and development, etc.
- *Unfair Competition:* This relates to the adoption of unfair means such as: fixing prices with the rivals, setting a price which is lower than cost in order to throw out competitors from the market, advertising that belittles others' product, etc.

### Types of Competition

- *Price Competition:* This is a form of competition among suppliers where the suppliers try to win customers by offering them a product at a price which is lower than their competitors' price. Lowering down of price is expected to bring about an increase in the market share of the lower priced product. But this strategy may not click for those customers who are loyal to any particular brand and are not price conscious.

- *Non-price Competition:* This is a form of competition among suppliers where they try to win customers not by lowering price but by advertising, offering after-sales-service, using sales-promotion tools, etc.

**Different Forms of Competition in the Market**

Before understanding the different forms of competition in the market, it is essential to understand what market is.

*Market* is an exchange mechanism that brings together sellers and buyers of any commodity or service. It is simply a transaction, not a place that is usually supposed to be, where a buyer agrees to pay a price for the product that he buys from a seller. Forms of competition in the market can be distinguished according to the structural characteristics of the market such as: number of sellers and buyers, the type of goods produced, the nature of entry barriers i.e. new firms cannot enter the market, etc.

Generally, there are four forms of market and the associated competition:

*1) Large number of sellers and buyers, identical goods, free entry and free exit:* This form of competition is called, "*Perfect Competition*". The existence of a very large number of sellers, producing identical goods, results in same price for these goods.

Existence of a unique price implies that in this form of competition, firms are price takers and not price setters and can sell any quantity of the products they desire at the existing market price.

A single individual producer whose share in the market is very small cannot influence the market. The degree of competition (price or non-price) is so low that it can be said that competition is virtually absent here. Moreover, on account of entry and exit being free and easy in this market, firms make only normal profits in the long run (i.e. normal return on capital employed which is comparable to that obtainable in other equally risky markets plus a bonus for the risk bearing function that the producer undertakes).

**Example:** Perfect competition is an ideal situation and does not exist in practice but a near perfect competition can be seen in the market for vegetables. Almost everywhere in the world where there are large number of buyers and sellers, the buyers have perfect information about the market and no individual seller can usually influence the market on his own.

2) *Single seller, large numbers of buyers, no close substitutes of the product, high entry barriers:* This form of competition is called, "*Monopoly*". In this market form, the monopolist (i.e. the only seller) is the price and output setter. The monopolist can set price and allow demand to determine output or, can set output and allow demand to determine price. There may be reasonably adequate substitutes but not close substitutes. For example, road transport services (public and private), airlines etc. are reasonably adequate substitutes for railways but not close substitutes. Because of absence of close substitutes, competition is absent in the railway sector.

**Example**: In most of the developing countries of the world, pubic utilities such as railways, electricity are examples of monopoly where the State is the sole supplier and there are no close substitutes.

3) *Large number of sellers and buyers, existence of close substitutable products, no entry barrier:* This form of competition is called, "*Monopolistic Competition*". Existence of a large number of sellers and buyers may give an impression that this form of competition resembles perfect competition. But it is unlike perfect competition. Here the existence of a large number of a buyers and sellers does not imply that only a single price prevails in the market. Rather, several prices exist in this market form. Each firm enjoys certain price setting power over its product because of product differentiation. Firms do not engage in price competition in this market form since the effect on the demand for the product of the low-priced firm is negligible. Instead, they engage in non-price competition, such as product differentiation, to attract more customers, not as a reaction to the decision taken by other firms.

**Example:** In most of the countries of the world, markets of the fast moving consumer goods (FMCGs) such as soap, toothpaste and other toiletries are examples of monopolistic competition where a large number of close substitutes are available. However, in order to remain in competition, the suppliers actively engage in product differentiation to attract customers.

4) *Very few sellers, large number of buyers, large number of branded products, high entry barrier:* This form of competition is called, "*Oligopolistic Competition*". The number of sellers is so small that they are conscious of their interdependence (be it in price, product or promotion). They take into account the competitors' possible reactions while deciding their strategy. Firms, in this market form, tend to produce large number of branded goods in order to diversify the product line and thus compete on non-price terms (such as brand loyalty) and strengthen this with high advertising budgets.

**Example:** In India, CSP (Cellular Service Provider) industry can be taken as an example of oligopolistic competition where only two firms are allowed with respect to each circle, such as, Airtel and Essar in Delhi circle, Hutchinson and BPL in Mumbai circle etc. They compete on non-price competition (facilities like cricket match score, stock market quotation etc.) among themselves and take competitors' possible reactions into account while deciding their strategy.

**Different forms of competition can be best understood by a tabular presentation:**

| Models of competition | Number of buyers | Number of sellers | Nature of products | Barriers to entry and exit |
|---|---|---|---|---|
| Perfect competition | Very Large | Very Large | Identical Products | None |
| Monopoly | Very Large | one | Single Product | Very Large |
| Monopolistic competition | Very Large | Large | Minimum differences | None |
| Oligopolistic Competition | Very Large | Very few | Large differences | Large |

# II. Hurdles To Fair Competition

Business firms, while competing with one another, often adopt means that are either restrictive (Restrictive Trade Practices or RTPs) or unfair (Unfair Trade Practices or UTPs) in nature, in order to deform or eliminate fair competition for acquiring a larger market share. These restrictive or unfair means are hurdles to fair competition and consumers are the ultimate losers. Though hurdles to fair competition usually occur in combination, the different types of hurdles can be distinguished as follows:

- Collusive Agreement for
  a) Price fixation
  b) Market allocation
  c) Output restriction
  d) Bid-rigging

(The above mentioned collusive agreements are horizontal in nature i.e. they take place between two or more firms at the same level of production-supply chain and who are competitors to each other. These are hard-core cartels and are most serious anti-competitive practices. Consequently, these are dealt severely by most competition laws.)

- Refusal to buy or supply
- Tie-in arrangement
- Exclusive-dealing arrangement
- Resale price maintenance
- Territorial allocation between supplier and dealer

(The above mentioned agreements are vertical agreements i.e. between two firms that are at different levels of production-supply chain. These are less serious than the hard core cartels, but can generate competition concerns in the market.)

- Mergers & acquisitions resulting in dominance in market
- Abuse of dominance
- UTPs (Misleading Advertisement or False Representation)

1) Agreement to fix prices: Sometimes the competitors in the market collude (form a cartel) to fix prices. The competitors could be at any level in the production and distribution process and the collusive agreement may be with respect to primary goods, intermediary inputs or finished products. The colluding firms undertake these kinds of activities in order to eliminate price competition between them. Sometimes they also follow this route in order to eliminate entry of any potential competitors into the market. This trade practice is seen between two suppliers or two distributors or two retailers, i.e. between two firms at the same level in the supply-distribution chain. So it is a horizontal restraint and restrictive in nature (Restrictive Trade Practice, RTP).

**Example**

Mitsubishi Corp. of Tokyo was taking part in an international conspiracy to fix prices of graphite electrodes that are large carbon columns used by Electric Arc Furnaces (EAF) or “mini-mills” in the making of steel. A federal jury in Philadelphia convicted the company. Mitsubishi owned 50 percent of UCAR International Inc., the world’s largest producer of graphite electrodes from 1991 until early 1995. UCAR pleaded guilty in 1998 for participating in a world-wide conspiracy to fix the price of graphite electrodes, paying a US$110mn fine.

*Source: Financial Express, 13.02.01*

**Example**

The global Lysine cartel, which included all significant lysine producers of the world, doubled the world price of lysine for three years. Lysine is a feed additive for poultry and swine.

The cartel successfully fixed very precise prices (to US$0.01 per pound) and sales quotas throughout the world and did so even though different prices and quotas had to be set in different places. Over the life of the conspiracy, the cartel raised prices on over US$1.4bn in global sales, which implies overcharges of US$140mn.

*Source: Report of the Ministerial level meeting of the OECD, 2000*

2) Agreement to allocate market: This agreement takes place between two or more firms to allocate markets among them, i.e. who shall deal where and with whom in order to avoid competition among themselves. Firms can decide to allocate markets either geographically or according to customers or class of customers. When the colluding firms face competition from any outside firm, then these firms may allow each other to compete freely while continuing to allocate areas where they do not face outside competition. The agreement between two firms to allocate market is a very serious anti-competitive practice, and may have a greater impact on competition due to price-fixing.

**Example**

Four sugar producers in Spain were engaged in market allocation agreement (apart from price fixing, sales quota agreements) that restricted sugar supply to the level at which maximum monopoly profits could be earned. As a result, Spanish sugar prices, for many years, were 5 to 9 percent higher than those in the rest of Europe. Based on a complaint from associations of businesses that use purchase sugar, and based on information collected through a raid, the Spanish Service for the Defence of Competition uncovered the sophisticated cartel and slapped 8.7mn euros fine on the four producers.

*Source: Report of the Ministerial level meeting of the OECD, 2000*

**Example**

The US Department of Justice investigated an international cartel operating in the citric acid industry and uncovered a complex conspiracy to carve up the world by allocation of sales volumes among the members of the cartel and agreeing on what prices would be charged across the globe. Citric acid is a flavour additive and preservative found in soft drinks, processed foods, cosmetics, detergents and pharmaceuticals.

All major producers (like Bayer, ADM, Jungbunzlauer, Hoffmann-La Roche and Cerestar Bioproducts BV) admitted guilt and paid fines totalling more than $85mn for their participation in this four year cartel. The conspiracy is believed to have affected over $1bn in commerce in the US during its duration.

*Source: A Framework for the Design Implementation of Competition Law and Policy, World Bank and OECD*

3) Agreement to restrict output: Under this agreement, firms frequently agree to limit supplies to a proportion of their previous sales. In order to enforce this, a pooling arrangement is often made whereby firms selling in excess of their quota are required to compensate other members, who may be selling less than their agreed quotas, by making payments to the pool. The ultimate objective of limiting supplies is to raise price of the product in the market.

**Example**

Recently, the US anti-trust authorities have unveiled an international price fixing conspiracy involving several leading and sophisticated pharmaceutical manufacturers of the world. These include Swiss pharmaceutical companies Hoffmann-La Roche and Lonza AG; BASF, Degussa-Huls Agand Merck KGAA of Germany; Rhone-Poulenc of France; etc.

These companies led a global conspiracy to fix prices of vitamins, allocate markets, supply contracts and sales volume, apart from bid-rigging at various times.

Majority of the colluding firms admitted their involvement in the cartel. Roche agreed to pay US$500mn, the largest criminal fine in the US, while five executives of Lonza AG pleaded guilty and agreed to cooperate in the ongoing investigations apart from paying a fine of US$10.5mn. BASF accepted a US$225mn fine. On the other hand, Rhone-Poulenc escaped punishment and supplied much of evidence.

*Source: CUTS ReguLetter, No.1, December 2000*

**Example**

Hindustan Pilkington Glass Ltd. in India entered into a market sharing arrangement with Surat Cotton to prevent it from making or selling certain glass products in consideration of payment of an agreed compensation. Surat Cotton was to sell its stocks to Hindustan Pilkington Glass Works Ltd. and keep the plant and machinery idle and was not to associate with anyone for making or selling the glass products. This was held to limit the supply of glass products and hence restrictive.

*Source: Law of Monopolistic & Unfair Trade Practices, S. M. Dugar, Third Edition, 1997*

4) Agreement to decide which competitor will win a tender: The buyer, who invites competitive offers or quotations through a tendering procedure, will receive offers solely from the members, who have entered into an agreement of collaboration and who have secretly arranged among themselves as to which firm will make the lowest offer. The other members of the collaboration will either decline to participate in the tender or will make fake offers, called "cover bids". This kind of agreement among firms is called "bid-rigging" or "collusive tendering". The tendering process is designed to promote fairness and ensure that lowest possible prices are received. Bid-rigging subverts this competitive process.

Mechanisms for bid rigging are numerous and varied such as:

*Bid suppression*: One or more competitors agree to refrain from tendering or to withdraw a previously submitted tender so that another firm can win the tender.

*Complementary bidding*: The competing firms agree among themselves as to who should win a tender, and then agree that the others will submit artificially high bids to create the appearance of vigorous competition.

*Bid rotation*: The competitors take turns being the winning tender, with others submitting high bids.

**Example**

Four major printers used to supply manifold business forms used for computer printout paper, snap-set forms, and similar products. Historically, the government tendered original orders but placed repeat orders with the firm that had supplied the first order. After concluding that it could improve prices by tendering all orders, the government began to do so from a list of qualified printers, including four major firms. The resultant price decline became a concern to the major companies and their sales managers.

The sales managers of the four companies met and agreed on a bidding strategy. The price book of the market leader, available to all, was used to determine benchmark prices for each product for all the companies. It was agreed that when a tender was called, the previous supplier of the particular form would bid at or below the benchmark price, whereas all others would bid higher. After a while, the companies concluded that this method was too difficult and agreed that the former supplier would simply tell the competitors how much it was bidding and others would bid higher or not at all.

During the conspiracy, about 300 separate tenders were called by the government, and bidding patterns were consistent with the agreements. The arrangement started to break down after the entry of new competitor, which began winning bids. The new firm was approached to join the existing arrangement. The new competitors, instead, complained to the authorities and provided initial information that led to the start of the investigation.

*Source: A Framework for the Design Implementation of Competition Law and Policy, World Bank and OECD*

**Example**

The French TGV cartel attempted to obtain monopoly profits in connection with the building of the high speed train system. The cartel was threatened by the prospect of a competitive bid from a foreign firm. The cartel members then offered to pay the other firm up to FF 75,000,000 if it would submit a higher bid on one part of the project and not bid on any other part of the project. After the firm rejected the payment and submitted the lowest bid, the conspirators corrupted the auction process in a second attempt to exclude it, but they were discovered and fined FF 378,000,000.

*Source: Report of the Ministerial level meeting of the OECD, 2000*

5) Agreement on refusal to buy from /supply to certain sellers/buyers: Here firms that are at different levels of the same production-supply chain enter into agreement (vertical agreement) whereby, they agree among themselves not to sell to or buy from certain customers. In other words, they agree to refuse to deal with any third party, normally a competitor of one of them. Though this may be a fair marketing strategy for optimum profit, sometimes such practices may reduce competition in the market and consequently could be restrictive in nature.

From the point of view of competition law and policy, vertical agreements are most likely to be harmful when at least one of the transacting parties is dominant in either upstream or downstream market. However, even restrictive vertical agreements that involve dominant firms can result in efficiency gains. Thus whether or not such practices are anti-competitive, depends on the specific case.

**Example**

VHP an Australian steel manufacturer, which controlled 97 percent of market, was manufacturing 'Y' bar used as fence posts, among other things. VHP used to sell this product only to its subsidiaries for retail selling.

Another company called Queensland Wire (QW), manufacturer and seller of barbed wire, tried to purchase 'Y' bar from VHP but could only get it at higher price, while one of the QW's competitors, AWC, a subsidiary of VHP, used to sell barbed wire together with 'Y' bar that was supplied to them by VHP at reasonable price. Though there was not a complete refusal to supply, the supply was made at a higher cost. The point to be noted here is that there was no substitute product for 'Y' bar.

The judgement by Australian Competition & Consumer Commission was in favour of QW as here the refusal or rather costlier supply was found to have an anti-competitive effect.

*Source: Report of the Asia-Pacific Regional Workshop on Competition Law, Jaipur, India, 16-17 April, 2000*

| Example |
|---|
| The European Commission fined Volkswagen AG, Europe's biggest carmaker, for barring its Italian distributor from selling cars to people living in Germany and Austria. Volkswagen, its Audi unit and their distributor had, over a decade, "systematically" rejected orders from foreign customers seeking to take advantage of lower Italian car prices. Under the European Union rules, car makers are allowed to sell through dealers which offer only one manufacturer's products, but can not prevent dealers selling to individuals or companies acting on their behalf who want to take advantage of cheaper prices of 15 - nation bloc.<br><br>The Commission said it had found "written evidence", during 1995 raids on Volkswagen and Audi and their distributor Autogerma, based in the northern Italian town of Verona, of pressure exerted on dealers to refuse cross-border orders. Its investigation concluded that a dozen dealers had their contracts terminated for not respecting Volkswagen's instructions and a total of 50 had been warned of the risk they would take if they sold outside. |
| *Source: Financial Times, 23.09.01* |

6) Forcing customers to buy other products along with the desired product: Here the supplier sells a product (tying product), which is dependent on the purchase of some other product, usually a slow moving product (tied product). This tie-in arrangement is such that even if the customer does not want to buy the tied product, he has to buy it in order to get the desired product. A good example of this kind of agreement is "full line forcing," requiring downstream firms to purchase a particular product.

However, such behaviour should not be considered abusive if the firm does not have market power in the tying goods. In general, a tie-in cannot be motivated by abuse if the two products are used in fixed proportions (as in the case of industrial goods) or if the tying goods are vertically related i.e., one good is used as an input to the production of the other good.

**Example**

Ghoten Gas Agency, a Kolhapur based cooking gas supplier in India, was forcing the buyers to buy hot plates at the time of releasing fresh gas connection. The Competition Authority held such a practice, where purchaser of one good is required to purchase some other goods which the customer may not even be interested in, to be a restrictive trade practice. The Authority also directed that wherever a customer purchased a hot plate simultaneously with a fresh gas connection, the gas agency should make it clear on the invoice that the hot plates were purchased voluntarily. Further, a notice board should be prominently displayed in the agency's premises that the customers were free to purchase hot plates either from Ghoten Gas Agency or from any other source.

*Source: Law of Monopolistic & Unfair Trade Practices, S. M. Dugar, Third Edition, 1997*

**Example**

Loew's Inc. in USA, in selling feature films to television stations, laid a condition that it (Loew) would license for sale of one or more feature films upon the acceptance of a package or bloc containing one or more unwanted or inferior films. The sole claim of illegality rested on the manner in which the product was marketed. The court, after examining the whole issue, held the tying arrangement illegal.

*Source: Law of Monopolistic & Unfair Trade Practices, S. M. Dugar, Third Edition, 1997*

7) Exclusive-dealing agreements: Here upstream firms (e.g. producers) force an agreement upon downstream firms (e.g. retailer), whereby the latter is prohibited from dealing with competing producers or distributors. This dealing arrangement can act as a barrier for new entrants and hence affects competition adversely.

**Example**

Adidas-Salomon, the German sport goods manufacturer, signed a contract in the early 1990s with the French football league association to give it the exclusive right to supply equipment to all soccer teams in the French first division. A French court ruled against Adidas and imposed a fine of US$2.2mn for anti-competitive practices. The ruling, which followed complaints from rivals, could cast doubt on the legality of similar contracts between sports leagues and equipment manufacturers in Europe and the US.

*Source: Financial Times, 02.01.01*

**Example**

Bangalore Jute Factory engaged itself in exclusive dealing arrangement and it was evident from a clause written to its distributor, reading: "You shall not, without our consent in writing, deal in any product manufactured by any other party local or foreign – which is similar to the product covered by this agreement." The Monopolies & Restrictive Trade Practices Commission in India held this practice to be restrictive.

*Source: Law of Monopolistic & Unfair Trade Practices, S. M. Dugar, Third Edition, 1997*

8) Resale price maintenance: Here the producer dictates the resale price of goods that would be charged by the retailers. Sometimes price floors or ceilings are imposed. When resale price maintenance is imposed, the price of goods becomes uniform at all points of resale irrespective of the difference in location, character and quality of the services provided. This practice, however, need not always be anti-competitive.

| **Example** |
|---|
| Volkswagen AG, the biggest German and European car manufacturer, instructed its German Volkswagen dealer network in 1996 and 1997 to observe 'price discipline' as regards the new VW Passat, and not sell this model at prices considerably below the recommended list price. Volkswagen sent three circular letters to its dealers, urging to limit or not to grant rebates to customers in respect of the sale of the (then) new VW Passat model, which was launched on the German market in October 1996 (Limousine) and in June 1997 (Estate Version). In addition to these circular letters, the company addressed individual letters to certain dealers, warning them against granting large discounts, and threatening them with retaliatory measures (for example, the termination of the dealer contract). The European Commission held this practice to be restrictive and fined the carmaker 30.96mn euros. |
| *Source: Competition Policy newsletter, Directorate General of the European Commission, No. 2, June 2001* |

| **Example** |
|---|
| Apple Computer Inc. was suspected to be pressurising retailers not to sell its *iMac* desktop and iBook notebook computers below the retail list prices. Japan's anti-monopoly watchdog, the Fair Trade Commission (FTC) held such a practice to be restrictive and issued a warning to its Japanese unit over suspected resale price maintenance. However, no administrative penalty was imposed on Apple Computer Inc. |
| *Source: Economic Times, 04.10.2000* |

9) Exclusive distribution agreements: This agreement is between the supplier and the distributor, where the former dictates the latter on his/her market. That means, whether or not the distributor will sell to any particular region or to particular class of customers is to be decided by the supplier. Again these are marketing strategies, generally followed by firms, but sometimes these practices may pose competition concerns.

**Example**

JCB, one of the UK's biggest manufacturers of construction equipment was restricting sales by its distributors outside their allotted areas in the UK, France, Italy and Ireland.

The European Commission fined JCB US$36mn for this act. The restrictions had been used for over 10 years to 1998, to indirectly stop customers from buying machines at lower prices in other countries.

The Commissioner justifying the fine said, "it is shocking that important companies present in all member states still jeopardise the most fundamental principles of the internal market to the loss of distributors and, ultimately, consumers."

*Source: Financial Times, 22.12.2000*

**Example**

McDowell & Co. Ltd., in India, imposed territorial restriction on its franchise-holders manufacturers/bottlers, to the effect that they were to confine their selling operations to areas allocated to them and prohibited them from selling their products at any place outside the respective areas. The MRTP Commission held this practice to be a restrictive one.

The Commission observed that in view of the relatively small share of McDowell in the soft drink industry and relatively large areas allocated to each bottler, the territorial restriction was not substantial and did not restrict or discourage competition but the possibility of these restrictions inhibiting competition at a later stage cannot be ruled out if and when the market share of McDowell increases significantly.

*Source: Law of Monopolistic & Unfair Trade Practices, S. M. Dugar, Third Edition, 1997*

10) Merger and acquisitions: Merger is a fusion between two or more firms whereby the identity of one (or more) is lost and results in a single firm. Acquisition (or takeover) of one firm by another usually involves purchase of all or a sufficient amount of the shares of another firm to enable it to exercise control.

Such mergers and acquisitions (M&As) might be horizontal, vertical or conglomerate. Horizontal M&As involve firms that are competitors i.e. at the same level of production-supply chain. For example, two firms producing toothpaste merge together.

Vertical M&As involve firms that are at different level of production-supply chain. For example, a firm producing cold drinks merges with the other producing bottles to contain such cold drinks.

Conglomerate M&As involves firms in diversified and unrelated business. For example, a firm producing cars merges with a firm that deals in finance. While horizontal mergers may raise competition concerns, vertical and conglomerate mergers, generally, do not raise any competition concern.

When two competitors merge together, it is but obvious that the market share of the merged entity would be more than that they individually used to share. Broadly there could be three cases due to any horizontal merger:

(a) a monopoly situation may arise;
(b) the merged entity may become a dominant player in the market; or
(c) even the merged entity could not capture enough market power

While cases (a) and (b) might pose competition concerns, case (c) is unlikely to give rise to any competition concern, if there remain other competitors in the market. Hence, the issue from the point of view of competition law and policy is not merger in itself, but whether such merger results in a monopoly situation or a dominant market player. Consequently, the determination of relevant market becomes the central issue. The merging entity would try to define the relevant market in broader terms so that their market share becomes lesser. Once the relevant market is determined, often it becomes very clear whether or not such mergers are anti-competitive.

**Example**

A planned merger between Avianca, Columbia's oldest and largest airliner, and its rival Columbia's second largest domestic airliner, Aces, was ruled out by regulatory authorities on competition grounds that the merged company would have been four times bigger than its nearest domestic rival.

Avianca, which represents almost half of the sales of its holding company Valores Bavaria, had been trying to clean up its balance sheet and saw the merger as a potential answer to the financial problems which have plagued Avianca, Columbia's flagship international carrier and one of the world's oldest airlines, which made losses of 98.4bn pesos (US$42.7mn) in the first quarter of 2001 compared with a loss of 37.8bn pesos last year.

The companies had showed the need to unite to compete in international market, at a time when Columbia is opening its international air routes to foreign carriers, which could have left the door open for proposals to cooperate on international operations only.

*Source: Financial Times, 12.06.01 & 13.06.01*

**Example**

The Australian Competition and Consumer Commission considered a case of merger involving two biscuit manufacturers (say A and B). A had 75 percent share of the biscuit market, while B had 15 percent share. Both decided to merge. ACCC wanted to block the merger as it would result in a dominant market player. One argument that merging entities put forward was that the 'market' to be considered here should be the 'market for snacks' and not mere 'market for biscuits'. Consequently, the market share of A would be 10 percent and that of B would be mere 1 percent. So, the main issue to be decided by the Commission was that 'whether it is a market for biscuits or a market for snacks'. The Commission ultimately disallowed the proposed merger, deciding it as a market for biscuits.

*Source: Report of the Asia-Pacific Regional Workshop on Competition Law, Jaipur, India, 16-17 April, 2000*

11) Abuse of Dominance: 'Dominant' means 'having authority or control'. Hence, a dominant firm would mean having authority or control over the market. With that authority and control a dominant firm can restrict new entry in the market or foreclose the commercial opportunity of weaker traders or create barriers in economic freedom of its probable competitors. In other words, a dominant firm is in place to adversely affect existing as well as future competition in the market.

However, it is not dominance in itself that is a cause for concern but when the same is abused. At times, it becomes a very complex issue from the competition policy perspective. First, the existence of dominance has to be determined, which takes into account many factors such as defining relevant market, determining market share and market power etc. And when dominance is established, its abuse is identified and investigated.

Typical abuses by dominant firms are:
- charging excessive prices
- price discrimination (charging different prices, according to the profile of the customer)
- tie-in sales (discussed above)
- refusal to deal (discussed above)
- predatory pricing (it is a practice of a dominant firm selling its product at very low prices, generally below cost, so as to drive competitors out of a market or prevent new entry and then successfully control the market. Predation is condemned not because it results in lower prices now, but because it is likely to lead to reduced output and higher prices in the future)
- raising rivals' cost (for instance, encourage higher wages industry-wide by using collective bargaining arrangements by dominant (large) firms to increase the costs of smaller, marginal firms. Raising rival's cost by engaging them in litigation or strategic advertising to such a degree that it raises sunk-cost investment for smaller rivals and potential entrants)
- abuse of intellectual property rights (competition concern may arise in three categories: the acquisition of IPR; transfer of technology through licensing arrangements, and cooperative arrangements among innovating firms. These practices raise such concerns when they constitute attempts to extend market power by excluding entry into a market, suppressing innovation etc.)
- other vertical restraints (restrictions that an upstream firm, e.g. a manufacturer or a wholesaler, places on its downstream firm, e.g. a retailer) such as:
- exclusive dealing (retailers agree not to sell rival products – also discussed above)

- exclusive territories (downstream retailer agrees to limit where it sells the product – also discussed above)
- resale price maintenance (retailer agrees not to sell below price established by the manufacturer – also discussed above)

**Example**

*Wal-Mart Store, Inc. v. American Drugs (1995)* explains predatory behaviour among other conducts by a firm. Wal-Mart is a leading super market chain in the US selling pharmaceuticals out of its chain of shops in Faulkner County in Arkansas. In order to beat the prices charged by rival pharmacies, the headquarters of Wal-Mart sent out explicit order to its Pharmacy Managers to resort to price reductions on some of the items. In case of certain items, the retail price charged by Wal-Mart was found to be even less than its wholesale purchase price. Furthermore, the key words in Wal-Mart's subsequent advertisement were "meet or beat the competition without regard to cost".

In this backdrop, three local pharmacies in Faulkner County filed a complaint against Wal-Mart for violating the Unfair Trade Practices Act of Arkansas State. Giving specific instances of items, which Wal-Mart was selling at a price lower than the wholesale purchase price, the complainants said that the said advertisement and offers for sale were made with the intent to deceive purchasers, to substantially lessen competition, unreasonably restrain trade and injure competitors.

However, the court came to the conclusion that Wal-Mart's measures were not anti-competitive and hence complaint should be rejected. For the purpose of proving predatory behaviour on the part of Wal-Mart, the first question asked was whether Wal-Mart has market power. Secondly, it was asked whether the price is below the cost. Thirdly, whether the impugned measure is to drive out the competitors. Lastly, whether there is an entry barrier i.e. unless entry barrier is very high competitors would re-enter the market. Considering all these facts, the court came to the conclusion that there is no predatory behaviour on part of Wal-Mart.

*Source: Report of the Asia-Pacific Regional Workshop on Competition Law, Jaipur, India, 16-17 April, 2000*

| Example |
| --- |
| Ceylon Oxygen Company, a monopoly Sri Lankan company, used to manufacture and distribute oxygen and other industrial gases. In 1987, it was nationalised and subsequently converted into a public limited company. In 1991, it was privatised and was taken over by a Norwegian company. Due to a natural entry barrier (high investment sector), the company enjoyed a monopoly in the market. The prices of the domestic gas cylinder were hiked substantially. In 1993, a new company IG entered the market and had to face many hurdles before it penetrated the market. At present, they have 20 percent of the market share. Even with the new player in the market, the price of domestic gas cylinder is still high. It is pertinent to note here that there was no substitute to LPG. |
| *Source: Report of the Asia-Pacific Regional Workshop on Competition Law, Jaipur, India, 16-17 April, 2000* |

12) Misleading advertisement and false representation: Any statement which is not true either because it hides facts that are important or suggests falsehood would be a false statement. Similarly, where a statement is put in such words or context that it may give rise to two meanings, one of which is false, would be misleading. These kinds of practices come under 'unfair trade practices' (UTPs), which in a strict sense is not a competition issue. However, as it harms consumers, some competition laws deal with it as well.

| Example |
| --- |
| Britain's biggest high street electrical chain, Currys, was claiming in their advertising that it offered 'unbeatable low prices'. The Advertising Standards Authority of the UK banned the advertisement and has ordered the company to remove the slogan from all newspapers and print advertising, saying that the advertising slogan was misleading as Currys did not always offer the lowest prices and was of the view that price comparisons showed Currys was often more expensive than its rival Comet. Moreover, when Comet was charging a lower price, Currys maintained its higher price. |
| *Source: Business Line, 07.02.01* |

| Example |
| --- |
| Roche Group was running a TV commercial advertisement that promotes its weight-loss drug Xenical but “lacks fair balance” information such as listing of the side effects. The US Food & Drug Administration (FDA) told the firm to stop the advertisement. Under the FDA guidelines, “help-seeking” advertisements, which focus on a disease but don’t specify a drug, need not list side effects. But, a full-length advertisement for a specific drug must spell out risks as well as benefits. In the present case, the advertisement effectively promoted Xenical without using the drug’s name. It alerted viewers to personalise support programme for weight loss called XeniCare while Xenical was the only weight loss product with a support programme, Xenicare. |
| *Source: Wall Street Journal, 21.05.01* |

# III. Competition Policy and Competition Law

### What Is Competition Policy?

Competition policy is essentially understood to refer to those governmental measures that directly affect the behaviour of firms and the structure of the industry. A consistent and realistic competition policy should include both:

i) *Economic policies* adopted by Government, that enhance competition in local and national markets (such as, policy of economic de-regulation and privatisation etc.); and

ii) *Competition law* designed to stop anti-competitive business practices by firms and unnecessary government intervention in the market.

Therefore, **Competition Policy = Economic policies that affect Competition + Competition Law**

Following flow-charts (figures 1 & 2) could explain competition policy and law in a nutshell.

**Figure 1: Components of Competition Policy**

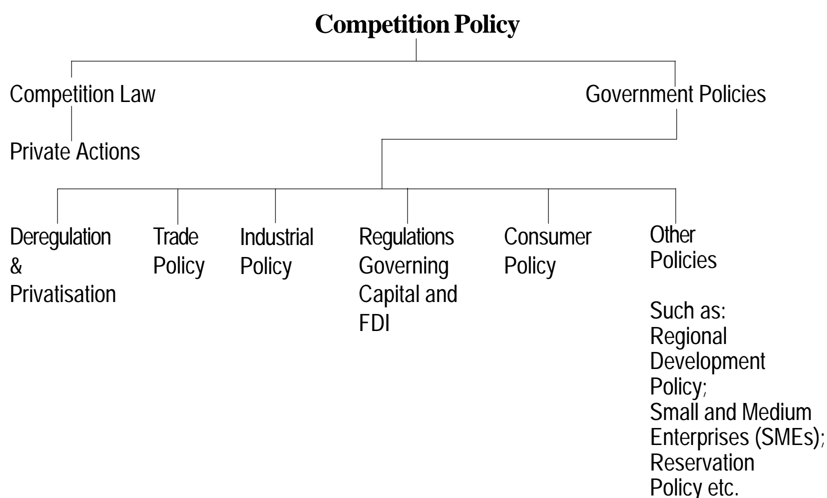
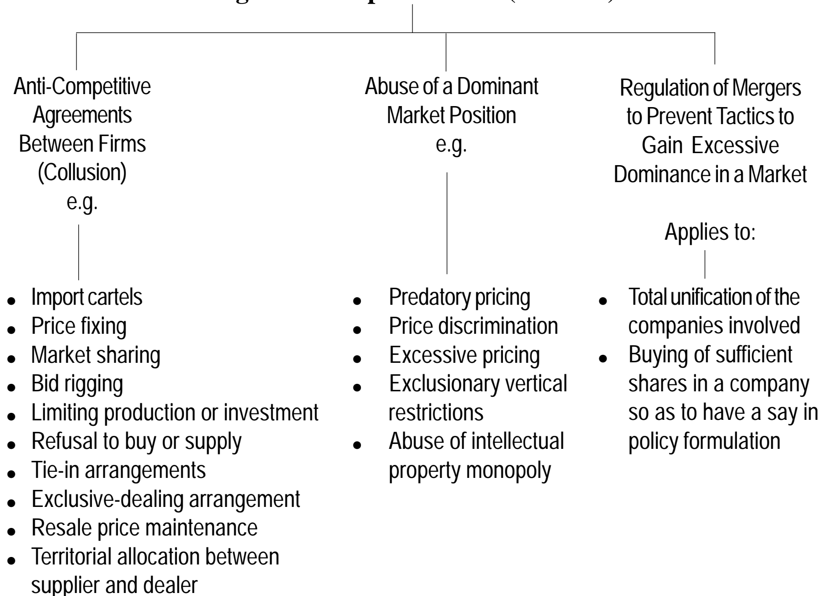


**Figure 2: Competition Law (National)**




A competition law, in general, consists of provisions with respect to:

★ Behaviour and structure of firms in the market, such as:
- Anti-competitive agreements
- Abuse of dominance
- Mergers & acquisitions
- Unfair trade practices (not all competition laws address it)

★ Institutional and enforcement design, such as:
- Structure and composition of competition authority
- Selection and terms and conditions for the members of competition authority
- Powers and functions of competition authority
- Other implementation provisions

★ Competition advocacy, which consists of:
- Public analysis, comment sand recommendations by a competition authority with respect to anti-competitive effects of existing and future policies, laws, regulations, and other actions of the government
- Generating and enhancing awareness of the stakeholders, such as business, consumers etc, on competition issues.

### Why Competition Policy Is Necessary?

It is generally observed in many markets that as time passes, markets become subject to concentration, and the number of firms operating in them reduces while the size of those still active, increases considerably. In this context, it is often said, "competition kills competition". Since competition in economic sense is always unstable and has a natural tendency to give rise to monopoly, it is necessary to ensure that competitive pressure is constantly maintained. Given this, the need for an active competition policy arises from the following factors:

- To take care of the anti-competitive practices designed to restrict the free and fair competition in the market;
- To take care of the unfair means adopted by firms against consumers to extract maximum of consumers' income; and
- To maintain and promote the competitive spirit and culture in the market.

### How Can Competition Policy Benefit Consumers?

Competition policy can benefit consumers in the following ways;

1) It ensures best possible utilisation of available resources.
2) It ensures better quality products at lower prices to consumers; and
3) It checks hurdles to fair competition.

The first two ways are attributable to the positive instrument (Economic Policies) and the third way is attributable to the preventive instrument (Competition Law) of competition policy. Let us explain this point.

Economic policies, such as deregulation and privatisation, can create opportunities for new businesses and stimulate efficiency in the economy (It is to be kept in mind that this idea may not hold good in case of public utilities such as, infrastructure, power and railway where large number of producers may actually lead to inefficiency). Moreover, since firms become efficient and in order to compete in the market, they offer greater choice of products and services at lower prices and thus consumers gain the most.

### Competition Authority

In general, to implement the competition law a separate agency is created that is termed, for academic purpose, as competition authority. For instance, the Indian competition authority is Monopolies and Restrictive Trade Practices Commission which implements the Indian competition law, "Monopolies and Restrictive Trade Practices Act, 1969."

Broadly, a competition authority has following four essential functions, which are, in general, performed by separate wings of the authority.

1) *Investigation:* The competition authority makes inquiries about anti-competitive practices in the market either on receipt of complaints or on its own.

2) *Prosecution:* After the inquiry, if the competition authority finds that any firm is posing hurdles to fair competition then it makes charges against the defaulting firm.

3) *Adjudication:* Taking necessary decisions including the imposition of restrictions on or granting injunctions against the defaulting firm is one of the functions of a competition authority. In many countries, the competition authority does not have judicial powers, which are discharged by general or special courts or tribunals.

4) *Advocacy:* Competition advocacy may be in upward or in downward direction. In upward advocacy, a competition authority advises or recommends to the government, while making any policy or enacting any law, that such policy or law has anti-competitive effects. It may also suggest to the government to scrap an existing law/policy or formulate a law/policy so that competition in the market is enhanced. In the downward advocacy, it informs and educates the business, consumers etc. on competition issues, conducts studies and publishes reports on anti-competitive practices, comes out with press releases, etc.

**Conclusion:**

A sound competition policy is an integral part of an effective consumer protection policy, as it protects consumers from the market place abuses. So it is a must that Government should develop an active competition policy that protects the consumers from market abuses and simultaneously ensures free and fair competition. Furthermore, economic, political and historical factors vary from country to country and the design or structure of the competition policy must take this into account.

The key to success of competition policy lies in other policies being coherent with the overall economic environment, on one hand, and the competition law coherent with and complementary to the competition policy, on the other.

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