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Tools for Ensuring Competition and Fair Trade

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Why is Knowledge of Antitrust Principles Important for Regulated Utilities?

- Before one deregulates an industry, one must understand what tools remain as enforcement options
- If an industry is deregulated, antitrust laws may be the only protection against unfair business practices, such as predatory pricing



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Types of Anticompetitive Practices

Price-Fixing

- Any agreement or informal arrangement between competitors to fix prices or bids

Horizontal price fixing occurs when direct competitors on the same level of distribution agree on prices

Vertical price fixing is an agreement between two or more people at different levels of the chain of distribution to set or control the resale price



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Bid Rigging

- Rotating Bidding: competitors designate on a rotating basis which one will present the low bid
- Bid Suppression or Bid Limiting: one or several competitors refrain from bidding, or drop out of the bidding, to enable a competitor's bid to be accepted
- Complimentary Bidding: competitors submit token bids too high to be accepted
- Allocating Business: general division or allocation of customers or territories
- Allocating Markets: some firms agree not to compete at all in certain territories or for certain kinds of business in return for reciprocal treatment



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Detecting bid rigging

- Look for patterns over time
- Receiving fewer bids than you would expect
- Inexplicably large gaps between the winning bids and all other bids
- Receiving low bids on a regular basis from the same manufacturer in a given area
- A certain manufacturer is bidding substantially higher on some jobs than on similar jobs with no accountable cost difference



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Group Boycotts and Concerted Refusals to Deal

- Any combination or agreement among competitors not to sell, buy, or otherwise deal with a particular business entity
- Primary boycotts: combinations or agreements not to deal with the business targeted as the victim
- Secondary boycotts: refusals to deal with the customers, sellers or suppliers of the targeted victim



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Tie - Ins

- The use of market power by a commercial entity to require the purchase of additional articles or services the buyer may not want



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Mergers

Three types of mergers:

- Horizontal
- Vertical
- Conglomerate



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Horizontal Merger

- Eliminates side-by-side competition between two firms
- Invariably raises market power
- The effect can be large or small, depending on the two firms' market shares and on other conditions in the market



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Vertical Merger

- Tie together two firms in the chain of production
- Debate on if they raise market power
- Raise profitability



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Conglomerate Merger

- Joins two unrelated activities
- Does not change the structure of either market directly
- Argued that no increase in market power will result
- But, it may enlarge the scope of the combined firm's strategies beyond what the two firms could do before merging



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Motives for Mergers

- **Market power and profits**
- **Technical economies**
 - Economies of scale may be provided by horizontal mergers if the merging firms were both below the minimum efficient scale
 - Vertical economies are gained by joining firms at two levels of production
 - Economies of diversification may arise from conglomerate mergers. The whole firm may be stabilized by combining diverse activities rather than having “all eggs in one basket.” The activities’ fluctuations will tend to even each other out, making total operation less risky



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Motives for Mergers

- **Pecuniary economies**

- Pecuniary economies provide money benefits without improving the use of real resources
- Merged firm may be able to enforce lower prices for the inputs it buys
- Tax laws and accounting rules may raise the profitability of mergers
- Merger may give promotional advantages if market power is transferable (advertising, sales, networks)



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Takeovers

- One firm seizes another against its managers' will
- The firm makes a sudden tender offer to buy the target firm's stock at a price well above the going price
- If it gains at least 51% of the stock, the target firm is taken over and absorbed into the acquiring firm
- Often occurs when a firm is thought to be managing its assets so poorly that its stock price is low and a new owner could gain a better return and raise the stock price; firm is seen as a bargain
- Many mergers are partially takeovers even if they do not appear to be



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Monopolies and Attempts to Monopolize

Unfair business practices used to achieve the intended monopoly, such as pricing an article at or below cost in order to drive a competitor out of business



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Antitrust and Fair Trade Laws

Purpose of Antitrust Laws

- Antitrust laws are the rules of a competitive marketplace
- Competition is about price, selection, and service
- Antitrust laws protect the process of rigorous competition to protect consumers from anti-competitive mergers and business practices



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Antitrust and Fair Trade Laws

Economic Effects of Antitrust Laws

- Reduce concentration in industries by controlling mergers
- Encourage price competition by controlling price-fixing
- Provide strong incentives for businesses to operate efficiently, keeping prices low and quality high
- Prevent creation of new market power



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Comparison of Laws

United States Federal Antitrust and Fair Trade Laws

Sherman Act of 1890

- Section 1. Every contract, combination in the form of a trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is hereby declared illegal.
- Prohibits certain types of cooperation among suppliers
- Classic target is price-fixing



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United States Federal Antitrust and Fair Trade Laws

Sherman Act of 1890

- Section 2. Every person who shall make any such contract or engage in any such combination or conspiracy, shall be deemed guilty of a misdemeanor.
- Makes market dominance illegal



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United States Federal Antitrust and Fair Trade Laws

Clayton Act of 1914

- Outlawed four specific practices and added a general rule against unfair methods of competition
- Section 2 forbids sellers “to discriminate in price between different purchasers of commodities” but permits discrimination where there are “differences in the grade, quality, or quantity of the commodity sold” where the lower prices made “only due allowance for differences in the cost of selling or transportation” and where they are offered in “good faith to meet competition.”



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United States Federal Antitrust and Fair Trade Laws

Clayton Act of 1914

- Section 3 forbids sellers to “lease or make a sale or contract for sale of...commodities...on the condition that the lessee or purchaser thereof shall not use or deal in the...commodity...of a competitor....”
- Section 7 forbids any corporation engaged in commerce to acquire the shares of a competing corporation or to purchase the stocks of two or more corporations that were competitors
- Section 8 prohibits interlocking directorates between corporations engaged in commerce where “the elimination of competition...between them would constitute a violation of any of the provisions of the antitrust laws”



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United States Federal Antitrust and Fair Trade Laws

- Generally, the Clayton Act outlawed discrimination in prices, exclusive and tying contracts, intercorporate stockholdings, and interlocking directorates
- Prohibitions are not absolute, only forbidden when their effect “may be to substantially lessen competition or tend to create a monopoly....”



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United States Federal Antitrust and Fair Trade Laws

- Robinson-Patman Act of 1936 prevents price discrimination that harms competition
- Originally passed in the Depression to protect small businesses from larger, often more efficient, competitors. Because of origins and complexity, it is not aggressively enforced at state or federal level. However, private parties use it often.
- Federal Trade Commission Act bans unfair methods of competition
- Hart-Scott-Rodino Antitrust Improvement Act of 1976 requires companies planning large mergers or acquisitions to notify the government in advance of their plans



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United States Enforcement

Two federal enforcement agencies

- Federal Trade Commission
- U.S. Department of Justice Antitrust Division



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United States Enforcement

Federal Trade Commission (FTC)

- Protects America's consumers
- Focuses on lighter, consumer-oriented industries
- Reviews mergers and acquisitions and challenges those that would likely lead to higher prices, fewer choices or less innovation



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United States Enforcement

FTC

- Seeks out and challenges anticompetitive conduct in the marketplace, including monopolization and agreements between competitors
- Promotes competition in industries where consumer impact is high, such as health care, real estate, oil & gas, technology, and consumer goods
- Provides information, and holds conferences and workshops, for consumers, businesses, and policy makers on competition issues and market analysis



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United States Enforcement

FTC

- The FTC does not act on behalf of an individual consumer or business but any information provided can help to expose illegal behavior
- With few exceptions, FTC investigations are not made public
- FTC staff takes firms before the Commission for rulings



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United States Enforcement

Antitrust Division of the U. S. Department of Justice

- Focuses on heavy industries
- DOJ takes firms to court, seeking to get convictions and remedies
- Also bargains behind the scenes and settles many cases with consent decrees before a final judgment is reached



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United States Enforcement

An enforcement agency's action may result in several kinds of economic impacts on a firm:

- **Investigation**

The study process can be large, long, and costly to the firm

- **Law suit**

Direct costs of litigation

Diversion of executive attention

Bad publicity; can affect a company's image and goodwill

Stoppage of company action



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United States Enforcement

- Conviction
 - Fines and other civil or criminal penalties
- Remedies
 - Constraint on behavior (injunctive relief)
 - Changes in company structure
 - Divestment
- Private damage suits



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United States Enforcement

- Because both agencies are small, they mainly try to develop a series of precedent-setting cases, rather than to pursue and catch every firm that might be breaking the antitrust laws
- Toward existing firms the threshold criterion for prosecution has been at least a 60-80% market share, plus some evidence that the firm intended to gain dominance or acted unfairly



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United States Enforcement

- Toward mergers:
 - Horizontal mergers are usually challenged if the resulting firm would have more than 25-45% of the market
 - Since 1980, all cases against vertical mergers have been stopped
 - Conglomerate mergers are left untouched
- Toward price-fixing:
 - Price-fixing is treated most strictly
 - Courts will not permit a defense that it was “reasonable”



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United States Enforcement

One enforcement problem is defining the market

- The two sides usually offer sharply differing definitions of the true extent of the market
- The plaintiff (agency or private company claiming to be the victim of monopoly) urges a narrow definition, which gives the defendant firm a high market share
- The defendant claims that the market is much larger, so that its share of that market is small
- Product features and geographic areas play a role
- A court's decision on this point often governs the outcome of the case, for if it accepts a large market, then harmful market power most likely does not exist



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Wisconsin Antitrust Laws

- Wis. Stat. § 133.03(1) prohibits “every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce...”
- Basic element: "agreement" which implies two or more businesses must be involved in the restraint. Statute does require overt act in furtherance of agreement unlike traditional criminal law



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Wisconsin Antitrust Laws

- Two types of violations under Wis. Stat. § 133.03(1)

Per se: An automatic violation if “agreement is established”

No justification or excuse allowed

Rule of Reason: Defendant may bring in evidence
justifying conduct



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Wisconsin Antitrust Laws

Two types of agreements.

- Horizontal agreements which are among competitors. Most horizontal agreements are *per se* unlawful because courts have found they hardly ever have pro-competitive effects or purposes
- Vertical agreements are those agreements involving businesses at different levels of competition (e. g., a manufacturer and its distributors). Most vertical agreements are not *per se* unlawful but may be unlawful under the rule of reason. A key vertical restraint that is *per se* unlawful is resale price maintenance, where a manufacturer goes beyond suggesting retail prices to a downstream seller and actually enters into an agreement as to what consumers will be charged.



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Wisconsin Antitrust Laws

- Wis. Stat. § 133.03(2) is directed at “Every person who monopolizes, or attempts to monopolize, or combines or conspires with any other person or persons to monopolize any part of trade or commerce....”
- Unilateral conduct may violate Wis. Stat. § 133.03(2), but the standards are much more amorphous and seldom result in criminal prosecution



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Wisconsin Antitrust Laws

- Monopolization - Basic elements
- Market Power: Usually defined as the ability to raise price or exclude competitors without much concern for reaction of competitors
- A share of $2/3$ or more of the relevant market is often deemed a sufficient basis from which a court will infer market power
- Market definition issues key
- Barriers to entry increasingly playing role here



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Wisconsin Antitrust Laws

- "Attempt to Monopolize" - Basic elements
- Market Power: The amount required is less than in the case of a monopolization count. In some cases, market share as low as 30 percent is sufficient
- Specific intent to monopolize: An intent to acquire additional market power by targeting a specific rival. This is usually more difficult to prove than the general intent requirement in the monopolization case
- General intent to monopolize: An intent to increase market power which need not be targeted specifically on a competitor



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Wisconsin Antitrust Laws

- Wis. Stat. § 133.04 prohibits price discrimination.
- Wis. Stat. § 133.04(1) No person may discriminate, either directly or indirectly, in price between different purchasers of commodities of like grade and quality, for the purpose or intent of injuring or destroying competition in any level of competition or any person engaged therein



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Wisconsin penalties and enforcement

- Criminal penalty for violations of Wis. Stat. § 133.03 includes fines up to \$50,000 and imprisonment of up to 5 years for individuals; \$100,000 fine for corporations
- Civil forfeitures: \$50,000 for individual, \$100,000 for corporations
- Civil lawsuit for injunctive relief and triple damages can be brought by state
- Private lawsuits may be brought by anyone for triple damages or injunctive relief; 80% of antitrust lawsuits are brought by private parties



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Wisconsin penalties and enforcement

- Wisconsin Attorney General is given authority to institute, manage, control and direct all antitrust prosecutions. Small staff assigned to enforcement
- Wisconsin District Attorneys have authority to bring criminal or injunctive actions but must give the Attorney General copies of the pleadings filed within 3 days of filing



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Limited Public Utility Exemption from Wisconsin Antitrust Laws

Wis. Stat. s. 133.07(2) This chapter does not prohibit activities of any public utility ... which are required by ch. 196 or rules or orders under ch. 196, activities necessary to comply with that chapter or those rules or orders or activities that are actively supervised by the public service commission. This subsection does not apply to activities of a public utility that are exempt from public service commission regulation



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Zambian Antitrust Laws

Ch. 417 The Competition and Fair Trading Act

- The purpose of the Act is “to encourage competition in the economy by prohibiting anti-competitive trade practices; to regulate monopolies and concentrations of economic power; to protect consumer welfare; to strengthen the efficiency of production and distribution of goods and services; to secure the best possible conditions for the freedom of trade; to expand the base of entrepreneurship; and to provide for matters connected with or incidental to the foregoing”



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Zambian Antitrust Laws

- Any category of agreements, decisions and concerted practices which have as their object the prevention, restriction or distortion of competition to an appreciable extent in Zambia or in any substantial part of it are declared anti-competitive trade practices and are hereby prohibited. 7(1)



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Zambian Antitrust Laws

- Enterprises shall refrain from the following acts or behavior if, through abuse or acquisition of a dominant position of market power, they limit access to markets or otherwise unduly restrain competition, or have or are likely to have adverse effect on trade or the economy in general. 7(2)
 - Predatory behavior towards competition including the use of cost pricing to eliminate competitors. 7(2)(a)
 - Discriminatory pricing and discrimination, in terms and conditions, in the supply or purchase of goods or services. 7(2)(b)



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Zambian Antitrust Laws

- Making the supply of goods or services dependent upon the acceptance of restrictions of the distribution or manufacture of competing or other goods. 7(2)(c)
- Making the supply of particular goods or services dependent upon the purchase of other goods or services from the supplier to the consignee. 7(2)(d)
- Imposing restrictions where or to whom or in what form or quantities goods supplied or other goods may be sold or exported. 7(2)(e)



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Zambian Antitrust Laws

- Mergers, takeovers, joint ventures or other acquisitions of control whether of horizontal, vertical or conglomerate nature. 7(2)(f)
- Colluding, in the case of monopolies of two or more manufacturers, wholesalers, retailers, contractors or suppliers of services, in setting a uniform price in order to eliminate competition. 7(2)(g)



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Zambian Antitrust Laws

- The Commission shall keep the structure of production of goods and services in Zambia under review to determine where concentration of economic power exists whose detrimental impact on the economy outweighs the efficiency advantages, if any. 11(1)



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Zambian Enforcement

Zambia Competition Commission (ZCC)

- Function is to monitor, control and prohibit acts or behavior likely to adversely affect competition and fair trading in Zambia. 6(1)
- Determine where concentration of economic power exists whose detrimental impact on the economy outweighs the efficiency advantages, if any. 11(1)



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Zambian Enforcement

ZCC

- Power of enforcement and investigation
 - No power to issue binding legal orders; cases should be taken to the Court of Law for judicial determination
 - The Commission may accept money by way of donations.
11(2)(a)



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Zambian Enforcement

Enforcement methods

- Actions may be formal or informal
- Go through the courts for a final court decision
- Bring action formally but settle by compromise
- Threatening action may be enough to change behavior
- Set precedent with some cases that will change behavior in the industry
- Intervening with regulatory agencies
- Private antitrust cases



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Dealing with Utilities in a Dominant Position

- ZESCO is in a dominant position as described in the Competition and Fair Trading Act Section 7(2)
 - ZESCO has market power
 - ZESCO has a market share of greater than 40%
 - There are barriers to entry into the market
 - It is the function of the ZCC to investigate the abuse of a dominant position as well as to prevent or redress the abuse of a dominant position. 6(2)(a) and (c)



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Dealing with Utilities in a Dominant Position

- ZESCO has a monopoly undertaking as described in Section (2) of the Competition and Fair Trading Act
 - ZESCO controls over 50% of the market
- Section 11(1) recognizes that full competition may not always deliver the most desirable outcome



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Dealing with Utilities in a Dominant Position

Role of Regulation

If competition is not perfect, regulation is even more important.

Price issues

- Price needs to allow a rate of return that keeps firms in the market and investing
- Reasonable rates for consumers
- Assistance and payment arrangements for low-income customers



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Dealing with Utilities in a Dominant Position

- Review of Supply Contract arrangements
 - Market power of a dominant firm may allow it to buy at such a low price that suppliers cannot recover their costs



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Dealing with Utilities in a Dominant Position

Regulatory issues

- Ensure consumer access to information
- Restrain from arbitrary administrative actions
- Commitment to a stable policy process
- Independent and impartial regulators



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Dealing with Utilities in a Dominant Position

Regulatory Oversight

- Construction pre-approval
- Construction cost recovery pre-approval
- Affiliated interest agreement pre-approval
- Holding company pre-approval
- Merger pre-approval
- Abandonment pre-approval