

Serial Offenders: A Discussion on Why Some Industries Seem Prone To Endemic Collusion

The OECD Global Forum on Competition

Fighting cartels and other anticompetitive agreements is priority for the Federal Antimonopoly Service (hereinafter the FAS Russia). The anticompetitive agreements strongly limit the economy and infringe upon customers' interests.

Today, the FAS Russia has vast experience in indication of cartels on different markets: construction market, chemical industry market, biological resources extraction market, fish and seafood market, food market, uniform delivery market, pharmaceutical market, convalescent facilities market etc.

Alongside this, it is possible to distinguish several sectors/industries that are most at risk of systematic violations (cartels). The following sectors can be distinguished within the practice of the FAS Russia: construction and construction materials, chemicals, food, deliveries of uniform, deliveries of convalescent facilities.

Within this contribution, we will present information based on the experience of the FAS Russia of reviewing antimonopoly cases on investigating cartels, as well as bid rigging in the construction sector.

Besides that, we will present information on serial offences and offenders on the convalescent facilities market and on the uniform delivery market. The last two subjects were specially selected by us because, in our view, in addition to the commodity markets, stated by OECD, they are of particular interest from the position of the serial offences analysis.

Sectors, exposed to repeated offences

According to the FAS Russia's observations, the cartelization is a serious issue in the construction industry. The statistics of the FAS Russia show that 30% of all antimonopoly agreement cases are cases on antimonopoly legislation violation in the construction and renovation sector, including road construction. Besides, we discovered that 40% of all investigated cases on bid-rigging are the cases, connected with the construction sector.

The example is a case on the bid-rigging on bridge crossing construction in Veliky Novgorod amounted 21 million RUB. The investigation found that two companies had concluded and executed an oral agreement (cartel), aimed to maintain prices during auctions (Paragraph 2 Part 1 Article 11 of the Law "On Protection of Competition"). Due to the actions of the parties to the agreement, only one participant took part in the auction and became a winner for a highest possible price. The case was investigated jointly with the Investigation Committee of the Russian Federation.

Another cartel on the construction market was revealed via analysis of the results of the auction on Krasnoyarsk regional cancer office reconstruction to the sum of 6,2 billions RUB. The violation was reflected in maintaining prices during auction (Paragraph 2 Part 1 Article 11 of the Law "On Protection of Competition").

Two companies, than corresponded to the requirements, were admitted to participate in the auction. During all stages of the auction, the companies' behavior was suspicious and they proposed prices only up to the agreed level of reduction of the initial price. Besides, the participants submitted identical applications for participation that included complex multi-page technical documentation. These proposals must have included original technically design solutions and offers of the competitors. However, the identity of the applications was detected by the FAS Russia and then proved by the independent experts. Apart from this, the antimonopoly authority received evidences by examination of the monetary movement and attraction of the subcontracting parties.

In spite of the fact that the cartels in the construction and construction materials sector are frequently identified, the FAS Russia did not detect the serial offenders in this field.

In terms of the serial offences, such offences were detected on the uniform delivery market and on the market of deliveries of convalescent facilities over the last few years.

In particular, the first investigation on the uniform deliveries took place in 2010-2011. The decision on this case was made in June, 2012. At that moment, the bid-rigging cartel consisted of many companies (32 legal entities) which operated on this market. Today, the FAS Russia carries out another investigation on this market. It should be noted, that the behavior of the new cartel's participants is similar to the behavior of the participants in 2010-2011.

In its examination of the antimonopoly agreement between suppliers of the uniform, the cartel signs were detected via auction analysis.

In the first case (2010-2011) – the FAS Russia established, that the auction processed the following way: the reduction of the starting price was no higher than 0,5%; there were only one or two price proposals etc.

In the second case (in 2015) the parties of the antimonopoly agreement used the same IP-addresses to enter and participate in the electronic auctions. Consequently, this became one of the signs to start an antimonopoly investigation. At a later stage it was found, that the parties' behavior repeated the scheme, which was used between 2010-2011: the reduction of the maximum starting price of the contract on 0,5%; refusal from price proposal by all participants accept one-two participants etc.

The price-maintaining cartel on the uniform delivery operated for several years, and consisted of many companies, which operated on this market (32 companies) and spread on five regions. The substance of the offence summed up in the auction price maintenance (violation of the Paragraph 2 Part 1 Article 11 of the Law "On Protection of Competition"). The strategy of the cartel participants was to win the auctions alternately. Most of the participants refused to propose prices and then received subcontracting or other compensation. The offence was investigated via analysis of the documents (information) and assessment of the auction participants' behavior. Also, the expert reviews were conducted through the probability theory and theory of games. The independent experts pointed out that such behavior is not possible (probable) in absence of the antimonopoly agreement. Apart from this, during the investigation one of the

participants admitted its guilt and used the leniency program (in accordance with 14.32 of the Administrative Offences Code)¹.

Another example of the offences on the same market are the cartels organized by the suppliers of the convalescent facilities. The first investigation was conducted between 2011-2012. In 2013, the FAS Russia made a decision and imposed fines on the companies. At that moment, the cartel was operating in one of the regions of the Russian Federation. At present, we found that such scheme had spread to several entities of the Russian Federation. The careful attention of the FAS Russia to this market is supported by the social importance of the auction subject.

During the first investigation (in 2011) there was a situation on the market when only one company became the winner of almost all the auctions. This was a signal for the antimonopoly investigation.

In the second case (in 2015) the circle of the cartel participants expanded. The tactics of the cartel was different. The participants used the same IP-addresses to enter and participate in the electronic auctions and this was a signal for revealing of the cartel. Several companies frequently used the same IP-addresses to participate in auctions.

The prices maintaining cartel on the purchase of the convalescent facilities (violation of the Paragraph 2 Part 1 Article 11 of the Law “On Protection of Competition”) is interesting, because it includes the behavioral model, which is called by the participants of the state auctions - “taran” (ram): three companies (this model requires the participation of at least three companies) out of overall number of the auction participants (cartel) unite against fair participants of the auction. The agreement is implemented in the following way: during the auction, two participants of the agreement pretend to be competing and then abruptly reduce the maximum initial price of the contract. At this, the fair participants loose interest to the auction. Then, in the last moment, one of the cartel participants makes a bet, which is little lower than the bet of the fair participant. After that, the applications of the first two cartel participants, which took the first and the second place, are found invalid because of the absence of the necessary documents for concluding a contract (it is made intentionally). As a result, the contract is concluded with the third participant of the cartel who applied with the price that was a little bit lower than the initial price of the auction.

The FAS Russia revealed several suchlike cartels (with similar behavioral model) and, with a view to improving the practice on the revealing of the cartels, had sent in its administrative units detailed instructions on the revealing of the cartels.

In the investigation process, the FAS Russia bases on the best world practices of identification and suppression of the cartels. The FAS Russia shares its experience via meetings/consultations or other ways of communication. For these purposes, the interministerial and interstate agreements are concluded. In the cases, mentioned above,

¹ A person (a group of persons, defined in accordance with the antimonopoly legislation of the Russian Federation), who voluntary reported to the federal antimonopoly authority or to its administrative unit on the conclusion of prohibitive agreement or on prohibitive coordinated actions, releases from administrative responsibility, in case this person respects the following terms:

On the moment of the person's report, the antimonopoly authority did not have the corresponding information or documents about the administrative offence;

The person refused from further participation in the agreement or from conduction of the coordinated actions;

The presented information and documents are sufficient for identifying of an event of the administrative offence.

the international cooperation was organized only to study the methodology and practices of the cartel investigation. The practical cooperation did not exist within these cases.

The situation changed after the introduction of the electronic auctions. The number of the “agreed” procurements had reduced. Recently, however, the FAS Russia has started detecting such agreements. The companies, which do not want to have fair competition, find different ways to agree even within the electronic auctions. Nevertheless, the total number of the offences had reduced.

Possible factors which lead to endemic collusions

In practice, decisions of the FAS Russia on cartel cases base on direct or indirect evidences. It also takes into account economic features: market volume, number of market participants and their relative shares (many small companies or few large ones), rate of technological changes in production processes and pace of innovation development, differentiation of goods (services) by competitors (high, low or absent), required amount of capital, cost of production, barriers to market entry etc.

For example, in the case on uniform deliveries, mentioned above, one of the arguments of the defender during antimonopoly investigation was impossibility of further price decline due to objective economic reasons (cost of energy, raw materials and transportation). However, in course of investigation and economic analysis it was found that the profitability of individual items was up to 20-40% depending on a company and technological processing.

First of all, permanent structure of market participants should be mentioned among the main reasons of existence of endemic collusions. Some market features could narrow number of legal entities that could provide certain goods or services. Awareness on other market participants, its capacities (for instance, technological processing and sales), customers or other information create certain conditions for cartel existence.

Secondly, similarity of goods procured annually for state or municipal needs or homogeneity of market demand.

It can be concluded that the more narrow and specific demand is, the more market could be subject to violations.

Enforcement

As for additional measures despite of fines, in particular, information disclosure, in accordance with information policy of Russian competition authority, results of case investigations should be public except information constituting trade secrets. All the decisions are available on the official site of the FAS Russia. This measure is a part of activity of the FAS Russia on competition advocacy and prevention cartels. Thus, information disclosure is one of anti-cartel measures.

The FAS Russia considers that administrative measures on anticompetitive agreements are adequate and effective in current situation.

In particular, in accordance with Article 14.32 of Code of Administrative violations of the Russian Federation (hereinafter – Administrative Code) undertaking of anticompetitive agreement could follow to:

- for officials: 20 000 – 50 000 RUB (~300 – 800 USD) of fines; disqualification up to 3 years; :

-for legal entities. fine from 1 to 15 % of the violator's turnover on the market or in the procurement process from 10 to 50 % from the initial bidding but not more than 4 % of the violator's turnover;

In Russian Federation, antimonopoly sanctions are supplemented by criminal liability. In particular, cartel participation is a criminal violation. Article 178 of the Criminal Code of the Russian Federation establishes the following liability for anticompetitive agreements: fine and (or) disqualification and (or) up to 7 years imprisonment.

For example, in the case on uniform delivery the FAS Russia imposed 15 mln RUB (~ 220 000 USD) fines on legal entities. Information on officials was transmitted to the law enforcers to address the issues of initiation of a criminal case.

In case on supply of the convalescent facilities, the FAS Russia imposed 7 mln. RUB (~100 000 USD) fines on legal entities. Information on officials was transmitted to the law enforcers to address the issues of initiation of a criminal case.

In case on bridge construction, the FAS Russia made a decision on existence of violation of antimonopoly legislation. All the information was transmitted to the Investigative Committee of the Russian Federation. As a result of its own investigation, the Investigative Committee of the Russian Federation sent its indictment to the court. The Court issued a guilty verdict against officials and sentenced them to imprisonment, disqualification and fines.

Sanctions for violation of antimonopoly legislation, in accordance with principles of proportionality and fairness, are proportional to the gravity of an offence. In order to prevent and suppress serial offences a number of aggravating and mitigating circumstances are taken into account in the decision-making process (in accordance with Article 14.32 of the Administrative Code).

In particular, among aggravating circumstances it could be identified: continuation of anticompetitive conduct; repeated administrative violation, etc. Stiffening of sanctions for antimonopoly violations is supposed to be deterrent factor, that could prevent endemic collusions.

On an ongoing basis the FAS Russia exercises activity on preparation and implementation of key decisions, which change production and trade relations towards competition development in different sectors.

The Courts have supported position of the FAS Russia in cartel cases in the field of constructions, chemicals, food, biological resources, fish and seafood, etc.

Amendments to Russian legislation based on enforcement practice of the FAS Russia were adopted. In particular, using of warnings and admonitions was expanded.

As a result of analysis of the FAS Russia' activity, amendments to Administrative Code were adopted concerning qualification of gravity of the offence: repeated collusion, continuing offence, etc.

Investigative practice of the FAS Russia related to anticompetitive agreements influenced development of leniency program. Analysis of violations and enforcement

situates a basis for legislative initiatives of the FAS Russia in order to development and maintenance of effective competition environment. Such work is exercised on ongoing basis.

In investigation process, the FAS Russia takes into account the best international practices of detection and suppression of cartels. We believe that international cooperation is one of the key elements of effective anti-cartel activity. The FAS Russia exchange experience with its foreign colleagues through holding meetings and consultations or with the help of other communication tools.

Moreover, the FAS Russia actively participates in OECD meetings devoted to fight against cartels. It also is active member of the Working Group of International Competition Network. Due to its huge enforcement practice Russian Federation became an author of the relevant Section of the Treaty on Eurasian Economic Union, which came into force on the 1st of January, 2015. We hope that provisions of this Treaty will be a base for future anti-cartel enforcement practice which will be implemented by Eurasian Economic Commission.