ANOTHER LOOK AT THE COMPETITIVE ASSESSMENT OF INFORMATION EXCHANGES AMONGST COMPETITORS IN EU COMPETITION LAW

*Bernardo Sarmento & Jorge Padilla**

Abstract: *Competition antitrust authorities dedicate considerable effort and resources to the assessment of the competitive effects of information exchanges amongst competitors; an amply justified approach given the potential of such conducts to faccilitate collusion. In this article, we contrast the insights from economic theory on information exchanges among competitors with the legal test set out in the case law. We argue that while the legal test draws on insights from economic theory, the practical difficulties to meet the standard of proof might result in excessive type I errors. The cost of such type I errors has been dramatically increased by the new Damages Directive, which highlihghts the importance that competition authorities consider whether the standard of proof they require to rebut a presumption of illegality is correct and proportionate.*

1. INTRODUCTION

Many of the most prominent enforcement decisions of the Portuguese Competition Authority ("PCA") during its first fifteen years of existence concern price fixing cartels.[1] This is likely to remain true in the future. Indeed, the PCA has recently confirmed as one of its enforcement priorities the

* Bernardo Sarmento is an Economist at Compass Lexecon. Jorge Padilla is Senior Managing Director at Compass Lexecon, Research Fellow at CEMFI (Madrid) and teaches competition economics at the Barcelona Graduate School of Economics (BGSE) and the Toulouse School of Economics (TSE). The views expressed in this paper are the responsibility of the authors and cannot be attributed to Compass Lexecon or its clients. The authors welcome comments at the following email address: bsarmento@compasslexecon.com.

1 See for example PRC 2016/08, PRC 2014/02, or PRC 2011/10,

"detection and investigation of anticompetitive practises, namely cartels".[2] Several of the PCA cartel decisions, however relate to information exchanges amongst competitors rather than to straightforward (or plain vanilla) price fixing agreements.[3] These exchanges were condemned by the PCA as restrictions of competition by object and were fined severely. The PCA motivated is decisions by reference to the potential of such practises to facilitate the implementation of collusive practises resulting in higher prices to the detriment of consumers.

The PCA is not the only competition authority that has shown concern with the potential anticompetitive effects of information exchanges amongst competitors. In recent years, several national competition authorities have undertaken similar investigations and adopted similar decisions.[4] More importantly, the European Commission ("EC") itself has pursued several cases of information exchanges amongst competitors.[5] Some of those have been appealed to the European Courts, which has helped clarify the legal approach to the competitive assessment of the exchange of information amongst competitors under EU law.[6]

The efforts and resources dedicated by competition authorities to the assessment of the competitive effects of information exchanges amongst competitors are amply justified. The welfare costs of collusion are large and well documented.[7] Price fixing agreements result in a transfer of rents from consumers to suppliers and, most importantly, a reduction in output which generates a deadweight welfare loss. Not surprisingly, over the years, the fight against (explicit) collusion has been a top priority in the agenda of many competition authorities. Clemency programs have been introduced around the world to induce cartelists to defect and facilitate the detection of price fixing. Competition authorities have dedicated considerable resources to make those programs more efficient over time. Many agencies are currently

2 See *Autoridade da Concorrência* (2017) *Prioridades da Política de Concorrência para o ano de 2018*, 22 December 2017. (Translated from the original in Portuguese.)

3 See for example PRC 2005/26 or PRC 2007/02.

4 See for example the CNMC decision on S/DC/0579/16 *Derivados Financieros* in Spain, or the Bundeskartellamt decision B11-11/08 in Germany, or the CMA decision on Case CE/9859-14 in the UK.

5 See for example COMP/38.511 – *DRAMs*, COMP/39188 – *Bananas*, or Case AT.39850 *Container Shipping*.

6 It is the case, for example, of the recent Container Shipping case or the Bananas case which was appealed to the General Court and subsequently to the Court of Justice. See Case T-588/08 *Dole Food and Dole Germany v Commission*; Case C-286/13 *Dole Food and Dole Fresh Fruit Europe v Commission*. See Section 2.2 below.

7 See among others Tirole, 1988:chapter 6.

investing significant resources to developing and perfecting mechanisms aimed at identifying cartels and other instances of collusive behaviour *ex officio*, especially in public procurement markets.

It is then natural, and, one should not find surprising, that companies willing to escape the rigours of competition find explicit coordination much less attractive than they did in the past. Unfortunately, this does not mean that those companies are likely to accept a *status quo* characterised by unfettered competition. Instead, they may try to approximate the outcomes of explicit coordination by colluding tacitly.[8] And yet, while they may have the incentive to collude tacitly, they may lack the ability to do so due to asymmetries of information regarding market fundamentals and/or their inability to observe, forecast and interpret market outcomes accurately. Information exchanges can facilitate (tacit) collusion by mitigating those information asymmetries and reducing market uncertainty. They help firms operating in tight oligopolies to coordinate their prices around a mutually agreed or "focal" price and to monitor their actual prices and hence punish deviations from the focal price.

The case for investigating information exchanges amongst competitors is therefore clear. Caution is, however, advised when assessing actual information exchange cases, as not all information exchanges are born equal. Not all information exchanges are anticompetitive and not all potentially anticompetitive information exchanges materially reduce consumer welfare, as we explain in what follows.

2. ASSESSING INFORMATION EXCHANGES AMONGST COMPETITORS

2.1. Lessons from economic analysis

The competitive assessment of information exchanges is a highly complex matter. It is well documented in economic theory that information exchanges can be procompetitive or anticompetitive, and often have no effects at all (in which case we say that the information exchanged is "cheap talk").[9]

8 Alternatively, they may attempt to achieve supra-competitive prices by merging. In fact, horizontal mergers and information exchanges need not be seen as alternatives but as complementary ways to approximate joint profit outcomes.

9 See Farrell & Rabin, 1996, and references therein.

We can distinguish four strands in the information exchanges literature. The first strand highlights the ability of certain information exchanges to have procompetitive effects, either because they lead to a more efficient functioning of the market or because they strengthen competition.[10] The second strand shows that under certain market conditions some exchanges of information can facilitate collusion and may thus cause consumer harm.[11] The third strand of the literature tries to assess the sign of the competition impact of an exchange of information depending on the nature of the uncertainty being reduced, the structure of the affected market and the strategic variables through which firms operating in that market compete (e.g. prices versus quantity or quality).[12] Finally, the fourth strand of the literature clarifies that information exchanges which involve no commitment by the firms to any particular future conduct are unlikely to have a real effect on competition.[13]

An impartial reading of the economic literature can only produce one, perhaps frustrating, conclusion: there is no definite answer as to whether and when information exchanges amongst competitors are anticompetitive. More importantly from an enforcement perspective, there are no unambiguous rules that could help competition authorities and courts identify the economic contexts under which those exchanges would be unambiguously anticompetitive. Economic theory has thus far being unable to produce clear-cut "identification rules".[14]

Rules often employed in competition law enforcement, such as for example the one that states that "private exchanges of future information are necessarily anticompetitive" cannot be endorsed by economic theory.[15] As explained above, the sharing of private information about future conduct (e.g. future prices) will likely increase market transparency by making available to competitors information which otherwise would not be in the public domain. This increase in market transparency may in turn facilitate tacit collusion, either by allowing competing firms to reach a focal point or to monitor compliance with the collusive price. However, this is not necessarily the case.

10 See Padilla & Pagano, 2000; and Jensen, 2007.

11 See among others Ivaldi, Jullien, Rey, Seabright & Tirole, 2003: 4-5; and Motta, 2004.

12 See Kühn & Vives, 1994.

13 See note 10 supra.

14 See Evans & Padilla, 2005.

15 For a more detailed discussion on the appropriateness of such rules to analyse information exchanges please see Padilla, 2010.

Consider for example a market where future supply is given (i.e. predetermined) at the time information on future prices/sales is exchanged. In that scenario, which admittedly is somewhat extreme, the information exchange cannot produce anticompetitive effects.[16] Consider alternatively a case where all exchanges of information are bilateral and take place in a fragmented industry where many firms compete. Such bilateral information exchanges may not be capable of producing the degree of coordination necessary to achieve collusive outcomes.[17]

While unable to provide identification rules, economics does generate useful insights on the relevant factors to analyse when assessing the competitive effects of exchanges of information: the characteristics of the market where the exchanges take place (i.e. is the market prone to tacit collusion?) and the characteristics of the information exchanged (i.e. is the information exchanged of the type required to move the market from competition to collusion).[18]

The first step is thus to analyse the market where the exchange of information takes place and whether this market has the characteristics of a market where tacit collusion would be viable if competitors benefitted from a sufficient level of market transparency. If the market in question does not exhibit such characteristics, then the information exchange will be unable to cause harm.

The second step in the assessment is to investigate the nature of the information exchanged. For example, information about past cost and demand information or about future market conditions is unlikely to help competitors to coordinate their strategies on a focal price or to monitor their conduct in order to detect and punish deviations. On the contrary, exchanges of information about future prices and commercial initiatives may be sufficient to align prices and information about prices actually charged can facilitate the enforcement of the tacitly collusive price.

An information exchange which increases transparency in a market where collusion is possible may be able to distort competition and thus cause antitrust harm. Whether it is likely to do so in reality is hard to assess by only looking into the characteristics of the affected market and the nature of the

16 This is the case discussed in Jensen, 2007.

17 As noted by William Baumol in the case of technology exchange programs where the negotiation and supervision of the arrangements is done bilaterally and consequently does not allow the required level of coordination to implement price fixing or the holding down of R&D outlays. See Baumol, 2001.

18 This is the same view of the European Commission. See European Commission, 2011: para 75.

information exchanged. In particular, in a market prone to collusion but for the absence of market transparency, only an information exchange that increases market transparency *significantly* will likely facilitate collusion.

So while the assessment of the characteristics of the affected market and the nature of the information exchange can help competition agencies establish that the information exchange in question is *capable* of restricting competition, such analyses will not be able to conclude whether that anticompetitive distortion of the competitive process is *likely*. As explained above, such conclusion can only be reached after assessing the magnitude of the impact of the information exchange on market transparency in order to determine its sufficiency. In our experience, this is a difficult task and, for that reason, we believe that, even in cases where the information exchange appears to be capable of causing antitrust harm, it is crucial to go beyond capability and establish effects.

In other words, we consider that an information exchange can only be found to be anticompetitive as a matter of economics, if the following three conditions are verified cumulatively: (a) the market where the information exchange takes place is conducive to collusion; (b) the nature of the information exchange increases market transparency and facilitates coordination on, and enforcement of, a collusive outcome; and (c) there is evidence of effects insofar as this evidence corroborates that the impact of the information exchange on market transparency was sufficient.

The economic test above is very different from the test commonly advocated for the assessment of explicitly price fixing agreements, since those explicit agreements are found to distort competition without an analysis of their actual effects. This difference is justified in our opinion. Price fixing agreements, in contrast with exchanges of commercially sensitive information, are unlikely to give rise to efficiencies and/or enhance rivalry. Moreover, such explicit agreements are structured so as to resolve the coordination and enforcement problems that competitors may not be able to address tacitly even in a completely transparent market. The likely effects of price fixing agreements can therefore be safely presumed where that is not truly possible for most exchanges of information.

2.2. Implications for the legal test

Information exchanges amongst competitors are analysed in the EU under the legal framework set out by Article 101 TFEU. Article 101(1) TFEU establishes that agreements which restrict competition by *object* or *effect*

are considered infringements of EC law. These conditions are not cumulative. Object restrictions relate to conducts which "can be regarded by their very nature, as being harmful to the proper functioning of normal competition".[19]

The case law shows that information exchanges amongst competitors are often regarded as object restrictions.[20] Whether a specific information exchange is found to be restrictive of competition by object requires an assessment of "its objectives and the economic and legal context".[21] For instance, it is settled case law that exchanges of commercially sensitive information which reduce the level of uncertainty in the market and which the parties' act upon when deciding about their own commercial strategies are considered to be restrictions of competition by object. Object restrictions are presumed to be anticompetitive and can be condemned without the need to produce any evidence that anticompetitive effects took place (or would likely take place).

This legal test does take into account the insight from economic theory that not all information exchanges are born equal. This is shown by the fact that the case law requires a preliminary assessment of the nature of the information exchanged and the economic context where that exchange occurs. However, in our opinion this legal test may cause a competition agency to conclude the existence of an object restriction when the information exchange in question is unlikely to produce anticompetitive effects because its impact on market transparency is insufficient to overcome the coordination and enforcement hurdles that make tacit collusion difficult. Thus the legal test may lead to presumptions of anticompetitive harm when no harm is likely. Or, in other words, it risks erroneously characterizing as anticompetitive certain information exchanges that are neutral and even some that are procompetitive.

As an example let us apply this framework to the Kerala fisherman information exchange case studied in Jensen (2007).[22] Robert Jensen analysed the impact of the adoption of mobile phones by fishermen and wholesalers in the Indian state of Kerala and the consequent reliance on these technologies to exchange information on the allocation of ports. Jensen showed

19 See Case C-286/13 Dole Food and Dole Fresh Fruit Europe v Commission – para. 114.

20 See cases listed in note 7 supra.

21 See Case C-286/13 Dole Food and Dole Fresh Fruit Europe v Commission – para. 117.

22 See Jensen, 2007.

that this exchange of information resulted in a reduction of price dispersion and waste, thus having a positive impact on both consumer and producer welfare.

Applying the legal test to this case we would find that (i) the information exchange involved commercially sensitive information which reduced market uncertainty, since competitors communicated to each other the port in which they would sell their fish captures (volumes), and (ii) the parties' acted on this information, since the information exchanged had an impact on the allocation of ports and hence on the supply available on those ports. As a matter of law, this would then be an object restriction even though it produced no anticompetitive effects.

The rebuttable presumption of illegality that results from the application of the applicable legal test may be justified given that assessing effects, as the economic test proposed above requires, is a complex exercise which may result in under-enforcement. The rebuttable presumption of illegality in the case law reduces the likelihood and cost of potential type II errors (i.e. the errors committed when anticompetitive practices are not found to be illegal).[23] Of course, a legal rule that minimises the expected cost of a type II error is bound to increase the likelihood and cost (and therefore the expected cost) of a type I error (i.e. the error committed when a pro-competitive practice is found to be illegal). The expected cost of the type I error can be reduced, or even eliminated, if the legal criteria for rebutting the presumption are correct as a matter of economics and are applied fairly and without bias.

As a matter of law the presumption of illegality that is applied to an object restriction can be rebutted by the parties to the information exchange by showing either that (a) the conduct could not have an anticompetitive effect (i.e. rebutting the Article 101(1) conclusion), or alternatively that (b) the conduct led to compensating efficiencies so that the net effect was pro-competitive (i.e. establishing an Article 101(3) defence). This makes sense as a matter of economics. The difficulty in practice is that the standard of proof typically required to show (a) or (b) is very high; in our opinion, unjustifiably high. Since the burden of proof regarding (a) and (b) rests on the parties, this implies that the legal test is biased and, as a result, is likely to produce too many false positives (type I errors) and cause a problem of over-enforcement.

23 For a discussion of the error-cost framework to the design of antitrust rules see Evans & Padilla, 2005.

Note, in particular, that the cost of the type I errors has been dramatically increased after the adoption of the *Damages Directive*,[24] since now a finding of infringement not only results in a fine but also leads to onerous compensation claims.

3. CONCLUDING REMARKS

In a moment where antitrust enforcers around the world place large efforts on fighting cartels, it is normal for non-compliant firms to search for alternative and less explicit ways to reach their anticompetitive objectives. Since the exchange of commercially sensitive information may in some markets result in collusive outcomes, it is of utter importance that enforcers keep paying close attention to how competitors interact with each other and how and what they communicate amongst themselves.

One cannot ignore, however, that, while some information exchanges may facilitate tacit collusion and harm consumers, many others, even when similar in nature, may bring about procompetitive effects or may produce no effect at all. As there are no clear identification rules to distinguish between those different types of information exchanges, caution is advised.

The legal standard that emerges from the case law imposes a rebuttable presumption of illegality on certain information exchanges which may not necessarily be anticompetitive. Under this legal test, some information exchanges that are procompetitive or that can have no effect on competition may nonetheless be found to restrict competition by object. As such, enforcers are excused of analysing the *likely* effects of those exchanges and feel entitled to dismiss evidence showing no *actual* anticompetitive effects.

Our view is that while this legal test may be justified, as it possibly mitigates the expected cost of under-enforcement, it opens the door to costly type I errors and may therefore result in over-enforcement. To assuage such possibility, it is extremely important that competition authorities do not treat *de facto* the rebuttable presumption in the case law as a *per se* illegality rule.

Following the transposition of the *Damages Directive* by the Member states, every infringement decision by a competition authority is likely to give rise to follow-on damages proceedings where the participants in the

24 Directive 2014/104/EU of the European Parliament and of the Council of 26 November 2014 on certain rules governing actions for damages under national law for infringements of the competition law provisions of the Member States and of the European Union.

information exchange will, under the current legal text that assimilates those exchanges to explicit price fixing agreements, face a presumption of harm. Courts will have to decide whether to award compensation to the claimants and, if so, calculate the quantum subject to that presumption of harm.

The quantification of the damages caused by an antitrust infringement is not a trivial matter. It involves complex economic analyses. Moreover, in many Member states, such disputes are resolved by non-specialized courts which place a disproportionate weight on the presumption of harm. Firms involved in an information exchange which by its nature and the characteristics of the affected market is considered to be an object infringement will thus face an uphill battle when defending themselves even if the exchange in question caused no anticompetitive harm.

Because of this, and given that changing the legal test is not something that competition authorities can do, we believe that competition agencies in the EU, including DG Comp and the PCA, should consider whether the standard of proof they require the parties to meet in order to rebut the presumption of illegality that is attributed to certain information exchanges in certain markets is correct and proportionate.

BIBLIOGRAPHY

Baumol, W. J.
2001 "When is inter-firm coordination beneficial? The case of innovation", 19(5) *International Journal of Industrial Organization* 727-737.

EUROPEAN COMMISSION
2011 *Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements*, 14 January 2011.

Evans, D. & Padilla, J.
2005 "Designing Antitrust Rules for Assessing Unilateral Practices: A Neo-Chicago Approach", 72(1) *University of Chicago Law Review* 73-98.

Farrell, J. & Rabin, M.
1996 "Cheap talk", 10(3) *Journal of Economic Perspectives* 103-118.

Ivaldi, M., Jullien, B., Rey, P., Seabright, P. & Tirole, J.
2003 "The economics of tacit collusion", Final report for DG competition, European Commission

Jensen, R.
2007 "The digital provide: Information (technology), market performance, and welfare in the South Indian fisheries sector", 122(3) *Quarterly Journal of Economics* 879-924.

Kühn, K. U. & Vives, X.
1994 *Information exchanges among firms and their impact on competition*, Institut d'Analisi Economica, Barcelona.

Motta, M.
2004 *Competition policy: theory and practice*, Cambridge University Press.

Padilla, J.
2010 "The elusive challenge of assessing information sharing among competitors under the competition laws", *Roundtable on Information Exchanges Between Competitors under Competition Law*, 879-924.

Padilla, A. J. & Pagano, M.
2000 "Sharing default information as a borrower discipline device", 44(10) *European Economic Review* 1951-1980

Tirole, J.
1988 *The Theory of Industrial Organization*, MIT Press.