

Contents lists available at [ScienceDirect](#)

# Economic Analysis and Policy

journal homepage: [www.elsevier.com/locate/eap](http://www.elsevier.com/locate/eap)

Full length article

## Defending against potential collusion by your suppliers— 26th Colin Clark Memorial Lecture<sup>☆</sup>



Leslie M. Marx

*Fuqua School of Business, Duke University, United States*

### ARTICLE INFO

*Article history:*

Available online 16 January 2017

### 1. Introduction

This article reflects the comments that I made at the 26th Colin Clark Memorial Lecture in Brisbane. I am grateful for the opportunity to honor the distinguished economist Colin Clark in this way.

An important component of almost any manufacturing process is the procurement of inputs for use in that manufacturing process. When inputs are available from more than one rival supplier, manufacturers may be able to use that rivalry to police the prices they must pay for the inputs. For example, a manufacturer might solicit competing bids from rival suppliers, perhaps using a formal auction process, or perhaps through less structured negotiations that allow the manufacturer to play suppliers off against one another. An individual is using competition to police prices when he or she gets price quotes from alternative providers of services, such as home repair services or lawn services.

This process can work well when the alternative suppliers pursue their unilateral self-interest by being willing to undercut the prices of their rivals in order to win business as long as they prefer to win the business rather than not at those prices. Not only does this process help buyers to secure good prices, but it also leads to an efficient allocation of resources because the suppliers who win the business are the most efficient ones.

While the competitive process is good for buyers and for overall economic efficiency, suppliers may be able to increase their profits if they work together to suppress rivalry. For example, if suppliers divide up customers among themselves and agree not to bid aggressively for the customers allocated to their rivals, then all suppliers may be able to achieve higher profits. The suppression of rivalry using communication and/or transfers is referred to as collusion, and the firms engaged in collusion are referred to as a cartel. Collusion is typically prohibited by antitrust laws. However, the profitability of collusion means that it occurs despite its illegality.

For example, beverage manufacturer Coca-Cola purchases many inputs, including high-fructose corn syrup, citric acid, vitamin C, cardboard boxes, and freight shipping. All of these inputs have been the focus of antitrust action related to collusion among the suppliers. As another example, computer manufacturers Dell and Hewlett Packard purchase components and peripherals for the computers they manufacture, including CRT displays, LCD displays, DRAM, optical disk drives, and rechargeable batteries. Again, all of these inputs have been the focus of antitrust actions alleging collusion.

It appears that collusion has been pervasive among suppliers of auto parts, with a long list of auto parts being subject to prosecution, as shown in [Fig. 1](#).

<sup>☆</sup> Delivered on June 26, 2016.

E-mail address: [marx@duke.edu](mailto:marx@duke.edu).

Air conditioning systems	Electronic control units	Power steering assemblies
Air flow meters	Electronic throttle bodies	Power window motors
Air fuel ratio sensors	Fan motors	Radiators
Airbags	Fuel injection systems	Seatbelts
Alternators	Fuel senders	Spark plugs
Anti-vibration rubber products	Heater control panels	Speed sensor wire assemblies
Automatic transmission fluid warmers	HID ballasts	Standard oxygen sensors
Automotive hoses	High intensity discharge ballasts	Starter motors
Bearings	Ignition coils	Steering angle sensors and switches
Brake hoses	Instrument panel clusters	Steering wheels
Catalytic converter substrates	Inverters	Valve timing control devices
Compressors	Lighting fixtures	Windshield washer components
Condensers	Manual steering columns	Windshield washer systems
Constantvelocity-joint boot products	Motor generators	Wire harnesses

**Fig. 1.** Auto parts cartels with fines imposed.

Source: DOJ Auto Parts Cartel Investigation Chart, *Practical Law Antitrust*, Thomson Reuters, 2015.

Specific to Australia, the Australian Competition & Consumer Commission provides information on a number of cartels that it has prosecuted.<sup>1</sup> As a result of collusion involving two Australian suppliers of cardboard boxes, Visy and Amcor: “Thousands of firms (and ultimately millions of consumers) were significantly overcharged by the cartel. The Federal Court ordered Visy and Amcor to pay \$95 million in damages to a customer class action involving more than 4500 businesses”.<sup>2</sup> Collusion among suppliers of air cargo services on routes to and from Australia involved Qantas, British Airways, Japan Airlines, and Korean Airlines. In Queensland, suppliers of pre-mixed concrete, Pioneer, Boral, and CSR, colluded: “Market shares were maintained by the companies recognizing certain customers (referred to as ‘pets’) as belonging to certain suppliers and agreeing not to compete for their business. The participants even engaged an accountant to monitor market shares so they could enforce compliance with the agreement”.<sup>3</sup> Collusion in ocean shipping involving Nippon Yusen Kaisha and others resulted in Australia’s first criminal cartel charge against a corporation.<sup>4</sup>

Thus, despite being illegal, collusion happens, even in Australia. The threat of collusion among input suppliers puts buyers in a position of needing to adjust their procurement practices and level of vigilance over their suppliers—costs that they would not have to incur if they could rely on competition to police prices. With this background, it is useful to ask what manufacturers can do to defend against collusion among their input suppliers.

One component of a defensive strategy against collusion is to identify collusive agreements early by recognizing the “tells” that can be associated with collusion. A second component is to target defensive resources wisely on inputs most likely to be of concern. And a third component is to review procurement practices to ensure that they are not contributing to the problem.

In addition, the legal environment may suggest certain strategies related to such things as document retention, contract design, or certifications by suppliers that they have complied with antitrust laws. I will not focus on these strategies in this article, but rather focus on economic issues. However, these legal strategies may be important, depending on the environment, and so deserve attention. For example, a failure to document past purchases may prevent a manufacturer from being able to recover damages should an antitrust violation be identified. Certifications by suppliers that they have complied with antitrust laws may enhance the ability to prosecute illegal conduct if, for example, claims of fraudulent concealment allow an extension of the statute of limitation. I leave these types of issues for legal counsel.

In Section 2, I describe the structures that a cartel would need to put in place to be effective and what traces those structures can leave in the economic evidence, information that can potentially put manufacturers in a position to detect collusion early. In Section 3, I discuss how a manufacturer might identify which of its inputs are most susceptible to collusion so that defensive resources can be focused on those. In Section 4, I describe attributes of a procurement process that can be disruptive to attempts by suppliers to collude effectively. Finally, in Section 5, I conclude.

<sup>1</sup> <https://www.accc.gov.au/business/anti-competitive-behaviour/cartels/cartels-case-studies-legal-cases#price-fixing>.

<sup>2</sup> *Id.*

<sup>3</sup> *Id.*

<sup>4</sup> <https://www.accc.gov.au/media-release/australia%E2%80%99s-first-criminal-cartel-charge-laid-against-nyk>.

Download English Version:

<https://daneshyari.com/en/article/5052693>

Download Persian Version:

<https://daneshyari.com/article/5052693>

[Daneshyari.com](https://daneshyari.com)