Public Goods as a Compensation in Cartel Cases

Lukáš Tóth

(with Maarten Pieter Schinkel)

Amsterdam Center for Law & Economics

Motivation

Non-competition concerns like "public interest" or "sustainability" enter decision making process of competition authorities:

ACM position paper

- General conditions for consideration of sustainability interests in cartel cases

UK's Enterprise Act

- Bases for public interest-exemptions in merger proceedings

2013 "Dutch Energy Deal"

- Over 40 Stakeholders, Reduction of capacity by 10%
- Higher anticipated prices
- Consumers to be compensated by lower damage to health: five old plants closed

Central Question

How to weigh the non-competition interests should they collide with creating a more competitive market environment?

Public Interest = Public Good

- Public goods: non-excludable & non-rivalrous
- Clear air, knowledge, national defense
- In utility functions of consumers
- Costly to produce

→ Cost-benefit analysis instead of broad PI concept

Key Issues

- Consumers damaged by the price increase are not necessarily the consumers benefiting from the public interest
- Informational requirements, monitoring
- Equity concerns: who pays, who benefits

Approach

- Non-cooperative private and public provision of public goods (building on Bergstrom et al., 1986)
- Possibly cartelized industry producing a private good
- Cartel formation = private good price increase
- Heterogeneous Consumers
  - In preferences
  - In wealth endowments
- **Compare consumer welfare in two states of the economy:**
  - **Competitive industry providing no public good**
  - **Cartelized industry mandated to compensate consumers**
- Investigate how much of the public good is needed to compensate each consumer for the price increase
- Incentive compatibility: conditions under which such a compensation is also profitable for the cartelized industry

Results

Anticompetitive agreements serving a public interest (≈ accompanied by public good production) may be Pareto-improving: Consumers are fully compensated & firm profits increase

Intuition: Mitigating the free-riding incentive innate in public good (under)provision

→ Cartel agreement accompanied by PG provision can serve as a welfare-enhancing means of taxation

- BUT: Government policy (taxes & subsidies) can achieve weakly higher welfare gains more efficiently
- BUT: The informational requirements for the competition authority are immense: it needs to know who the most damaged consumers are and the proper size of the compensation
- If heterogeneity of consumer preferences is high, Pareto-improvements are less likely to exist due to "one size fits all" nature of public good provisions
- Firms have an incentive to misrepresent the consumer preferences and public good levels provided
- Due to consumer behavior (substitutions between different goods), the compensation needed to make everyone at least as well-off is (weakly) higher than consumer surplus-based estimates suggest

Conclusion: a case against promoting public interest considerations by market authorities

Contact information

UNIVERSITEIT VAN AMSTERDAM
Amsterdam Center for Law & Economics

Lukáš Tóth
ACLE,
Tinbergen Institute
E-mail: toth.lukas@gmail.com
www.acle.nl
www.tinbergen.nl