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All of the Economic Aid the U.S., Eu, and Japan Give to the Developing World Is Stolen Back by Our Illegal Price-Fixing Cartels

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All of the Economic Aid the U.S., EU, and Japan Give To the Developing
World is Stolen Back by Our Illegal Price-Fixing Cartels

[alternative title]

How International Cartels Negate All The Benefits
Of Foreign Aid To The Developing World

Robert H. Lande

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I. Title was intended to shock you. To put my thesis slightly more completely:

The Equivalent of “All the Economic Aid the US, Europe, and Japan Give to the Developing World is Stolen Back by Our Illegal Price-Fixing Cartels” Other than that its not the identical dollars given in foreign aid that are stolen back, only their equivalent number of dollars, its true.

II The last few years I have been studying cartels.

A. Cartels are a relatively bipartisan area of antitrust - unlike mergers, monopolization, Bush Administration diverted enforcement resources to this area, Bush signed legislation that increased max fine from \$10 m to \$100 m. Whether they - or the Democrats - have been tough enough is a different issue.

B. Example: Vitamin cartel - 1990-1999 44% overcharges on average.

1. Caught, fined in US, EU, a few other places, some private actions, a few officers went to jail. But Prof. Connor's study shows they made a profit!
\$8 billion fines and payouts = huge amount! But less than 40% of their overcharges!

But developing world? Cartels are illegal in most nations. Peru successfully sued a poultry cartel. But how often could Peru successfully sue companies like F. Hoffman La Roche for fixing the prices of vitamins? Rarely. Not a fair fight.

2. Empigram - USSC held that foreign consumers cannot sue in US courts. (I worked on a losing amicus brief saying they should be allowed to, as the only practical way to deter international cartels.)

3. For US consumers - bottle of vitamins went up from \$5.00 to \$7.00 due to the illegal cartel. Most of us can afford it. The cartel simply stole from each of us.

But the poor in the developing world? No vitamins for many poor people - devastating!.

C. Example #2 - the Lysine cartel, led by ADM. Lysine is used to make animal feed. The price of every egg, every chicken, in the world increased significantly due to this cartel. Peru might be able to successfully sue its local poultry industry when they fix prices. But how can Peru successfully sue international companies like ADM? I could give hundreds more examples.

III. Got the idea of comparing cartel profits to foreign aid when I read an article by 2 well respected economists, & Valerie Suslow, "Contemporary International Cartels and Developing Countries".

A. Article totaled the commerce from the developed world to the developing world from all the convicted cartels they could find, \$51.1 billion in 1997; 4% of all their imports from the developing world.

B. They observed that if the illegal cartels has overcharged by an average of 10%, this would total roughly 15% of the \$39.4 billion the World Bank said was donated as foreign economic aid by the US, EU and Japan to the developing world in 1997. (Roughly \$7 billion of this was from the US.)

IV. Here is why their number struck such a response in me.

A. Why assume a 10% cartel overcharge? In 1987 the USSC trying to devise criminal fines for price fixing cartels. How high raise prices on average?

B. Asked Douglas Ginsburg, who was Reagan's AAG for Antitrust, who estimated 10%. The USSC used the 10% price rise in its formula. Immediately attacked as being too high by some scholars with small, possibly non-representative studies of 10 or so case studies. By the defense bar with anecdotes that 10% was too high.

C. Issue lied dormant for roughly 15 years.

V. Dr. John Connor and I decided to study it. Tulane Law Review 2006

A. Every US judge and jury verdict in a cartel case since 1890 (most settle - only found 24) 31% mean overcharge.

B. Every economic cartel study - Dr. Connor found more than 300 - a 49% mean overcharge.

VI. Plus, what % of cartels do we detect? Less than 100%, for sure.

A. Important since we should divide overcharge by the probability of detection and proof. If cartels steal \$1, and there is a 50% of catching and proving it, then divide \$1 by 50%, and fine them \$2.

B. I should add that there also are criminal penalties and private treble damages suits for price fixing. So the overall optimal deterrence issue is quite complicated.

C. Ginsburg said 10% of cartels were detected. Folk wisdom in the antitrust field that we only detect 1/3 - the reason antitrust has treble damages. And the % surely is higher now than in 1987. A number of academic estimates, all show 10% to 30%. No solid percentage, so I'm going to use the 1/3 assumption. A very conservative assumption.

VII. You surely can see where I am going

A. \$51.1 billion times 31% (the lower of 31% and 49%) = \$15.8 billion in cartel overcharges to the developing world.

B. If we multiply by 3 (under the assumption that we only catch 1/3 of all cartels) this = \$47.4 billion. This is slightly more than all the net foreign economic aid given by the developing world during 1997, of \$39.4 b!!

C. If we use the 49% figure, or we use Ginsburg's 10 fold multiplier, of course we get a much higher figure. Using these estimates, the illegal cartels, which even conservatives in the US, the EU, Japan, etc all condemn, steal significantly more from the developing world than these countries give them in foreign aid.

VIII Why is this so important? For a lot of reasons.

A. It probably means that cartels are vastly underdeterred even in the US and the EU. Fines should be increased significantly. Especially since so many are foreign - why let F. Hoffman La Roche, etc. steal from US consumers?

B. Hard to overstate the harm to developing world. They really can't afford the higher prices - and the reduced purchases this causes, for vitamins, chickens, etc.

C. Melodramatic to put it this way, but every time US, EU, Japan gives \$1 to the developing world, ADM, F. Hoffman La Roche, etc. steals back its equivalent. They negate or offsets all the good that our foreign aid does. Let's not be smug about the amount of foreign aid we give.

IX. Step back -- This large scale corporate theft could even slow or stop the spread of worldwide capitalism.

1. We are all capitalists of course. And we are trying to encourage the entire world to become more capitalist - for its own good.
2. Not only economic good - but also because we think that democracy flows from capitalism. Milton Friedman, "Capitalism and Freedom". We will all benefit from a world that is more capitalist and more democratic.
3. But we in the developing world aren't living by one of the most fundamental rules of capitalism: don't fix prices. Live by competition, not collusion.
4. How can we possibly ask the developing world to become good capitalists when we aren't playing by the rules of capitalism? Rules that we have all agreed to - compete, don't fix prices. Illegal, but inadequate penalties.
5. It's one thing to ask the developing world to open their borders to free trade. But quite another thing to open themselves to exploitation by illegal cartels. To let in companies who won't even abide by their own countries' rules. What does a term like "economic colonization" mean if not that developing world's companies should play by the laws they have agreed are fair?
6. Why hasn't all the foreign aid we have given over the decades done as much good as we would have liked? Why has there been so little progress in the developing world? Aren't we always giving them \$100 million to build new fertilizer factories, etc? Except that we are in effect giving them \$100 million for a fertilizer factory - and then some of our companies steal it back, illegally suck it out of the very economies we are supposedly trying to help!" We should be ashamed of ourselves.

X. The solution?

- A. Increase our foreign economic aid from \$7 billion? Sure, but hard to do politically.
- B. Dramatically increase cartel penalties, in the US, EU, everywhere in the developed world. (Sadly the developing world often does not have the necessary institutions.)
- C. Legislation to overturn Empigram?
- D. Not only to protect U.S. consumers. But also to protect consumers in developing world. The best form of foreign aid we can give to the developing world is to give them free and fair markets in which to compete.

NOTE - This thesis is very much a work in progress. I am still trying to nail down such things as: 1. Exactly how to define and measure “foreign economic aid”. 2. Whether cartels increase prices the same amount or percentage to the developing world as they do to the developed world? 3. I’m not sure what kind of piece to write. Perhaps not a conventional legal article.

All suggestions are most welcome. Bob Lande rlande@ubalt.edu

How International Cartels Negate All The Benefits
Of Foreign Aid To The Developing World

[alternate title]

The US, Europe, and Japan Actually Give No
Net Economic Aid to the Developing World

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Every time the US government, the EU, or Japan gives economic foreign aid to the developing world, corporations in the developed world illegally steals back its equivalent. For this reason the developed world actually gives no net foreign economic development assistance. This is intended to be an amazing statement, so let me show why it is true.

Almost everyone agrees that cartels are anticompetitive and should be banned. One of the bedrocks of worldwide capitalism is that when competing firms get together to fix prices, rig bids, or allocate markets or customers, they should be punished severely.

Although once popular outside of the U.S., cartels are now illegal not only in the United States, but also in Europe and most of the rest of the world. In the United States alone an international cartel can face criminal penalties that exceed \$100 million, private actions for mandatory treble damages, and 10 year prison sentences for culpable executives. In fact, one of the clearest of all the rules of international capitalism - a rule that started in the United States and gradually spread - is "don't fix prices." Although Democrats and Republicans often disagree about approaches to other areas of antitrust, President Bush signed legislation that significantly increased cartel penalties, and his Justice Department routinely prosecuted cartels. There is a bipartisan consensus in the United states - indeed, in all of the developed world - to eliminate the cartel problem.

Unfortunately, the penalties actually imposed by the developed world on illegal cartels consisting of firms from the developed world are only a fraction of those needed to deter their anticompetitive activity. This has terrible consequences for U.S. consumers, and is devastating for the relatively poorer citizens and economies of the developing world.

As an example, consider what happened to the most heavily punished illegal cartels in history - the international vitamins cartels.² During most of the 1990s the manufacturers of

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virtually every vitamin consumed outside China conspired in Switzerland to raise prices, by an average of 44%. Once caught they were fined in the United States, Europe and elsewhere, and forced to settle private damages actions in the United States. The best estimate, by Professor John Connor, is that all told they paid \$8 billion for their crimes. This seems like a huge amount - until you consider that (using constant dollars) their payouts were only approximately 34% of their illegally acquired profits! In other words, for the most prosecuted, most heavily fined, most sued cartel in world history, crime paid a handsome profit.

Cartel overcharges are the equivalent of theft, and of course theft harms those least able to afford it. Most U.S. consumers can afford to pay 44% more for their vitamins, although the burden on our poor and elderly consumers is considerable, and surely many could not afford to purchase artificially overpriced vitamins. Moreover, even wealthy people should not have their money stolen by cartelists or other thieves.

By contrast to the relatively fortunate situation of most Americans, however, many people in the developing world simply must go without. The very poorest people in many nations don't have the luxury of paying more, even for purchases of necessities like vitamins.

Or medicine. A large number of pharmaceutical prices have increased significantly by illegal cartels and monopolies. Augmentin, Busperone, Cardizem Platinol, Taxol, Relafen, Remeron, Terazosin... the list of pharmaceuticals whose prices were illegally raised by antitrust violators goes on and on. The record price increase for a pharmaceutical seems to be in the Mylan case; 2000%. At least, this is the highest increase that we know of.

These cases are by no means the only large ones that have found out about. Other illegal international price fixing cartels and monopolies that have been caught and forced to pay more \$50 million for overcharging consumers have involved such products as automotive refinishing paint, fructose, commercial explosives, graphite electrodes, lysine, rubber chemicals, and sorbates. In fact, a recent study by the American Antitrust Institute documented that, since 1990, at least 40 illegal cartels and monopolies each were forced to pay at least \$50 million in damages to overcharged U.S. consumers.³ Clearly, a lot of price fixing and other illegal activity by a lot of very large companies in a lot of very large markets is occurring.

One reason for this sorry outcome is that the United States the Sentencing Guidelines for cartel offenses are built upon a presumption that cartels raise prices 10% on average. The Sentencing Guidelines fix the criminal fine in terms of this number, and adjust it for a number of factors. However, a recent survey of hundreds of cartel studies and verdicts in

² This discussions of the vitamins cartels is from John M. Connor, "The Great Global Vitamins Cartels," http://papers.ssrn.com/sol3/papers.cfm?abstract_id=885968

³ Lande & Davis, "Benefits from Private Antitrust Enforcement: An Analysis of Forty Cases," 42 U. San Francisco L. Rev. 879 (2008)
http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1090661

U.S. cartel cases, by Connor & Lande, shows that cartel overcharges have been at least 31% on average, and probably have been roughly 49%.⁴

Another reason comes from a host of court decisions that have accomplished such technical “adjustments” as making class action certification more difficult, denying foreign consumers standing to challenge cartels in U.S. courts, and denying victims’ prejudgment interest. Moreover, the Supreme Court’s recent *Twombly* decision dramatically increased the burden of proof on those alleging firms engaged in a horizontal conspiracy. The Court made it extremely difficult for plaintiffs to discover whether firms had engaged in illegal collusion - unless plaintiffs somehow first found a “smoking gun” they would no longer be permitted even to start discovery into whether the cartel existed! This often is an impossible Catch 22 for the victims of price fixing.

Virtually incomprehensible to outsiders, together these court decisions effectively eroded antitrust’s so-called “treble damages” remedy so much that few cartels - even those that have been caught - end up paying even single damages.⁵ The example of the Vitamins cartels given above is hardly unusual. Yet, the legal system only can hope to deter illegal corporate behavior if the penalties exceed the expected gains. In fact, since cartels are so difficult to detect, optimal deterrence requires that the expected penalties significantly exceed the expected gains. Specifically, we should divide overcharge by the probability of detection and proof. If cartels steal \$1, and there is a 50% of catching and proving it, then divide \$1 by 50%, which means that the optimal fine would be \$2.

A final reason is that, as anemic as sanctions are in the United States, only the EU and a few other jurisdictions worldwide are able to impose even modest cartel penalties. Most developing nations lack the sophisticated and honest enforcement and legal system necessary to bring even a modicum of justice to an international cartel. Even if international cartels get caught and pay fines and damages in a few jurisdictions, they still typically profit overall due to their unpenalized sales to the developing world.

How harmful are these cartel overcharges on the citizens and economies of the developing world? In total they do a staggering, almost incomprehensible, amount of damage.

Professors Margaret Levenstein and Valerie Suslow published a study documenting how in 1997, U.S., EU, and Japanese companies sold more than \$51 billion a year in illegally

⁴ John M. Connor & Robert H. Lande, “How High Do Cartels Raise Prices? Implications for Reform of the Antitrust Sentencing Guidelines,” 80 *Tulane L. Rev.* 513 (2005), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=787907

⁵ Robert H. Lande, “Are Antitrust ‘Treble’ Damages Really Single Damages?” 54 *Ohio State L. J.*, 115 (1993), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1134822

cartelized products to the developing world.⁶ For this same year the World Bank reported that total official worldwide economic foreign aid, from the developed world to the developing world, totaled \$39.4 billion.⁷ Applying even the 31% average overcharge figure calculated by Connor & Lande (let alone their 49% estimate) to this \$51 billion in cartel sales, means that the developing world paid \$15.8 billion in illegal overcharges. This means that illegal international cartels stole the equivalent of 40% of all the foreign economic aid donated that year to the developing world by the developed world!

Moreover, Levenstein and Suslow could only total the sales of known cartels. What percent of illegal cartels are detected? No one knows, of course. The only official estimate was made in 1987 by the Reagan-appointed head of the Antitrust Division, and now U.S. Court of Appeals Judge, Douglas Ginsburg, that we caught at most 10%. Since then there have been a number of academic estimates, all in the 10% to 30% range. If we much more optimistically believe that today we catch one cartel in three, this would mean that, each year, cartels by firms in the developed world steal the equivalent of 120% of the amount of the foreign economic aid that the developed world gives to the developing world.

We don't even want to think about the implications if Judge Ginsburg's estimate that we only catch 10% of all cartels is correct today, or if cartels overcharge by 49% on average instead of by 31%. Moreover, the above calculations only have included the overcharges by international cartels. International monopolies also have overcharged the developing world by substantial sums. Since there is only non-systematic evidence as to how high illegal monopolies raise prices on average, and only anecdotal data on how much is sold to the developing world by illegal monopolies, no adjustment has been made to the above figure that was based on cartel overcharges alone. All we know for sure is the direction that the addition of data on monopoly overcharges would push the results.

The United States continually urges the nations of the developing world to become more capitalist - for their own benefit. It is the common wisdom that the nations of the developing world will develop their economies effectively only if their corporations learn to compete on the same bases as ours - under the conventional rules of market capitalism. But this advice is difficult for them to take when the developing world does not seriously require our own firms to abide by the lynchpin of capitalism that calls for competition instead of cartels.

It is one thing to ask developing countries to open their markets to trade that is free and fair. It is quite another thing to ask them to open their markets to cartels and monopolies. It is one thing to ask developing countries to engage in international competition. But it is a very different thing to ask developing countries to open themselves to exploitation by cartels and monopolies that will not obey their home nations' laws. Can these companies really be expected to obey the laws of the developing nations?

⁶ Margaret Levenstein & Valerie Suslow, "Contemporary International Cartels and Developing Countries", 71 *Antitrust L. J.* 801, 816 (2004).

⁷ *Id.*

This situation is especially sad because the magnitude of this illegal activity and the resulting impoverishment of the developing world is so appalling. In effect, every time the developed world gives the developing world the resources to build a new fertilizer plant or hydroelectric dam, its cartels and monopolies steal back the equivalent amount of money. How can the poorest nations of the world develop their own economies when they must pay billions in illegal overcharges to wealthy western corporations? How can many of the poorest citizens of the world be expected to subsidize wealthy western stockholders? All the good done by all of our foreign economic aid is undone, negated. Not only does this mean that the developing world give no net foreign aid - we might well be stealing more from the developing world than we donate to it.

Does foreign aid - whether given directly by the nations of the developing world or through such international organizations as the World Bank - result in vastly fewer benefits than we hoped? This is because, thanks to our cartels and monopolies, we do not actually give (net) foreign aid. Pity the economic development professionals whose job really is just to counteract the pernicious effect of antitrust violations!

The penalties against illegal cartels and monopolies in the United States, the EU, and Japan are so low that our businesses are not deterred from forming them. Unless we crack down much harder on illegal cartels and monopolies in a way that demonstrates to corporate managers that crime is not profitable, we should view our net "aid" to the developing world with shame, not pride.

Americans would be very unlikely to agree to increase dramatically the amount of foreign economic assistance we donate to the developing world. But we could do more for them if only we would prevent our only nominally illegal cartels and monopolies from impoverishing them. As a reward for doing the right thing, consumers in the United States also would benefit tremendously.