NO-POACH AGREEMENTS: PURCHASING POWER TYPE, EXPLICIT v. TACIT COLLUSION, AND LESSONS FROM SELLERS' CARTELS

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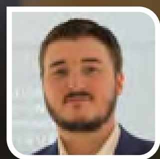

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NO-POACH AGREEMENTS: PURCHASING POWER TYPE, EXPLICIT v. TACIT COLLUSION, AND LESSONS FROM SELLERS' CARTELS

By Richard May

From near obscurity just over a decade ago, no-poach agreements are now in the crosshairs of several competition authorities worldwide, including the U.S. and EU. No-poach agreements are a type of buyers' cartel where employers explicitly collude to increase their purchasing power over their employees. They are the mirror image of market allocation of customers by sellers. This short article makes three observations in relation to no-poach agreements. First, depending on market structure, purchasing power can be monopsony or bargaining power. It appears that no-poach agreements could be either and that this is worth some consideration when prioritizing enforcement. Second, no-poach agreements are a form of explicit collusion which recent increased enforcement should deter, but strong enforcement may also have increased the risk of tacit collusion. At the same time however, if the prevalence and enforceability of non-compete clauses in employment contracts decreases, employer incentives to collude explicitly may increase. Finally, given competition authorities' significant experience of sellers' cartels, there are interesting lessons to learn from them for the enforcement of buyers' cartels (including no-poach agreements). The article highlights this potential with two examples.

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I. INTRODUCTION

Traditionally, purchasing power has been in the shadows of competition policy. This may be changing, at least for purchasers in labor markets.[2] No-poach agreements in particular have received attention and increased enforcement action over the last decade. This is particularly true in the United States where there have been several high-profile cases, including against companies such as Google, Apple, Disney, and eBay. The Department of Justice ("DOJ") even launched its first criminal proceedings in relation to no-poach agreements recently.

The U.S. has not been alone. Other countries have had experience with no-poach agreements, including Brazil, Turkey, Hungary, Croatia, the Netherlands, and Spain among others. Some jurisdictions have also released public documents on the topic, such as Japan, Hong Kong, and Portugal.[3] However, many jurisdictions still appear to have taken neither public enforcement action nor provided clear statements of their intent to do so.

No-poach agreements have been detected in a wide range of industries, ranging from digital markets, movie production, healthcare, IT services, flooring production, railways, and fast-food franchises. Different industries, and different job profiles, give rise to the potential for purchasing power to affect labor markets differently. In particular, whether the agreement between employers produces monopsony or bargaining power. The first section of this article briefly introduces these concepts and explains why both appear to be relevant in the context of no-poach agreements.

Explicit collusion, such as agreeing not to poach each other's employees, is a risky business. If reaching an understanding without explicit communication, namely tacit collusion, could achieve the same outcomes then this would surely be preferred. The second section considers how the incentives to collude explicitly have been affected by recent developments, including increased scrutiny of non-compete clauses in employment contracts.

The final part of the article considers no-poach agreements as an analogy to the market allocation of customers by sellers. It argues that such an analogy is useful for future enforcement against no-poach agreements, and provides two stylized examples from past cases.

II. PURCHASING POWER DERIVED FROM COLLUSION

A. Monopsony power v. Bargaining Power

Collusion between purchasers may provide purchasing power, pushing prices paid for inputs (such as labor) down. Purchasing power for employers, here derived through reduced competition for existing workers, will lead to worse outcomes for workers. However, the effect of this derived purchasing power on overall welfare can depend on whether it is monopsony power or bargaining power.[4]

Under monopsony power, sellers face the mirror image of monopoly. Wages are set by the monopsonist, which faces an upward sloping supply curve. Thus, by reducing demand to lower wages, the quantity of labor falls.[5] As a result, in most situations monopsony power should be considered contrary to the goals of competition policy.[6]

There are of course multiple nuances to the theoretical models of monopsony and its overall effect on welfare, but perhaps two worth mentioning here are the possibility of "take it or leave it" offers and the extent of downstream market power. The first appears unlikely to apply in the context

2 The OECD Competition Committee considered competition in labor markets in a Roundtable in 2019 and again at the OECD Competition Open Day in 2020. Prior to an upcoming roundtable this June on Purchasing Power and Buyers' Cartels, the Committee considered Monopsony and Buyer Power in 2008. See OECD, *Monopsony and Buyer Power*, Background Paper (2008), ("OECD 2008").

3 For example: Autoridade da Concorrência, *Labour Market Agreements and Competition Policy*, Issues Paper - Final Version, September 2021; and Competition Commission Advisory Bulletin, Hong Kong Competition Commission, *Competition Concerns Regarding Certain Practices in the Employment Marketplace in Relation to Hiring and Terms and Conditions of Employment* (April 9, 2018).

4 For more on this distinction, see OECD (2008). Kirkwood (2014) also discusses a similar distinction, referring to bargaining power as countervailing power: Kirkwood, John B, *Collusion to Control a Powerful Customer: Amazon, E-Books, and Antitrust Policy*, University of Miami Law Review, Vol. 69, No. 1 (2014).

5 Assuming there is no wage discrimination.

6 Broadly defined as beneficial to consumers and society as a whole. Exactly what the goals of competition policy should be is itself a topic rich in discussion. A summary of some of this debate can be found in of OECD, *Competition in Labour Markets*, Background Note (2019) Section 2.3.

of labor markets.[7] Regarding the second, if a monopsonist also possesses downstream market power, reduced output and increased marginal costs are likely to lower quantity and raise prices downstream, harming consumers.[8] When there is no market power downstream however, there is unlikely to be a material effect of the monopsony power downstream other than shifting volume away from the monopsonist to downstream competitors.[9] Similarly though, there will not be a benefit to consumers through lower prices, just increased profits for employers at the expense of workers.

Purchasing power is bargaining power when both parties negotiate bilaterally and have some market power. In such situations, parties bargain over the economic rents available. Purchasers with bargaining power therefore seek to extract most of the economic rent, reducing profits to sellers but generally not affecting overall volumes. In the context of no-poach agreements, reducing the possibility for a current employee to move to a rival may reduce their outside option and lower the outcome of pay negotiations.

Bargaining power for purchasers can be beneficial to competition and welfare overall, particularly if it offsets supplier market power to reduce the marginal costs for downstream sellers, potentially to be passed on to consumers.[10] However, bargaining power can also lead to results contrary to the goals of competition policy, even aside from the harm to workers. For example, bargaining power acquired through no-poach agreements could affect competition in downstream markets, including by facilitating downstream collusion.[11] Further, bargaining power could reduce dynamic and productive efficiencies, through its effect on upstream competition and on the incentives of sellers to innovate and manage risk. For no-poach agreements, a particular concern is the potential for workers to be precluded from new, and potentially more productive, employment opportunities.[12]

B. No-poach Agreements: Monopsony Power or Bargaining Power?

No-poach agreements provide a mechanism for employers to derive purchasing power, without the need to enter potentially complex agreements on wages or other employment terms.

It may be natural to initially consider no-poach agreements as providing bargaining power to employers, as they appear limited to restricting the outside option for current workers. However, by reducing the number of alternatives for workers, employers may become their only option, allowing them to set wages akin to a monopsonist facing an upward sloping supply curve. Therefore, while the welfare effects of both monopsony power and bargaining power will depend on the circumstances, it appears worthwhile considering which should apply to no-poach agreements. This article argues it could be either.

For simplicity, consider two broad categories of workers. Those with a broad set of skills that are applicable to a wide range of jobs, and those with specific, and harder to obtain or rarer, skills that suggest a particular job match.

In the former case, employer purchasing power from collusion appears likely to be closely associated with monopsony power. In such instances, employers may have many potential employees. These employees will differ, living in different locations, having different willingness to travel and different requirements for job satisfaction. The wages that they are willing to accept will therefore vary. This variation will represent itself as an upward sloping supply curve to the employer; raising the offered wage will induce more workers to offer their services but increase the wage for all.[13]

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7 If the purchaser can make a "take it or leave it" offer to sellers to supply at a higher quantity at a price just covering average variable costs, then monopsony power may not reduce output and could lead to lower prices for consumers in downstream markets. In the context of labor markets, where the upward sloping supply curve is likely to reflect the reservation wages of workers, it is difficult to imagine monopsony power being successfully used with take it or leave it offers, at least beyond the short-term.

8 Assuming that labor costs rise with output, as the monopsonist raises wages to hire an additional worker the increased wage will need to be paid to all workers. Hence, the marginal cost of an extra worker is both their wage and the increased wages for the other workers, again assuming no wage discrimination.

9 This still may cause some harm to overall social welfare if it shifts production away from the most efficient firms, potentially increasing overall costs and prices.

10 Many assumptions are required to arrive at this outcome however, including the inability for upstream and downstream firms to contract efficiently and for downstream competition to be such that the costs are passed through. In the event of efficient contracting, such as a two-part tariff, purchasing power may shift the allocation of rents between parties but leave marginal costs unchanged (as the downstream firm will already face the true marginal cost of the product).

11 For example, if labor is highly differentiated such that it materially affects downstream products, market allocation upstream could facilitate a similar market allocation downstream by restricting the possibility of repositioning or entry.

12 Another factor to consider is the costs of workers switching jobs, and if these costs are high enough, these may be greater than lost productivity gains, suggesting the potential for no-poach agreements to be welfare enhancing. See Shy, O. & Stenbacka, R., Anti Poaching Agreements in Labor Markets, Economic Inquiry, Western Economic Association International, vol. 57(1), pages 243-263, (January 2019).

13 A number of authors have argued that labor market frictions, such as costs of recruitment, can also cause employers to face upward sloping supply curves, for example: Krueger, A. B. & Posner, E. A., *A Proposal for Protecting Low-Income Workers from Monopsony and Collusion*, The Hamilton Project, Policy Proposal (February 2018).

Moreover, monopsony power is more likely when employers have a choice of workers, yet workers face insufficient choice of employment such that employers can lower wages by withholding demand (even if this may result in higher levels of vacancies).[14]

In the case where specific skills are required for a job, and hence finding a good match is more difficult, considering employer purchasing power through the lens of bargaining power appears more appropriate.[15] Certainly, many wages are influenced by a level of negotiation between the employer and employee, suggesting that bargaining power may be relevant here.[16]

Monopsony power and bargaining power seem plausible through no-poach agreements and, as explained above, both can lead to effects likely to fall foul of the aims of competition policy. Nevertheless, given the potential for no-poach agreements to affect a range of workers, competition authorities should at least be mindful of the type of purchasing power when considering enforcement. For instance, as some scholars have already argued, there may be reasons to be particularly concerned if no-poach agreements were prevalent in industries where monopsony power was involved, and this disproportionately affected low-wage workers.[17]

III. TACIT OR EXPLICIT COLLUSION BETWEEN EMPLOYERS

A. Colluding Tacitly or Explicitly

Collusion can be tacit or explicit. Both will reduce competition, but generally, explicit collusion is more likely to fall foul of antitrust laws.[18] No-poach agreements are examples of explicit collusion. Tacit collusion arises when firms can obtain mutually beneficial outcomes without the need for direct communication or agreement. In the current context, firms could individually realize that it is in their mutual interest not to poach rival's employees and punish severally those that try.[19]

As explicit collusion likely carries a higher risk of penalty, it has a higher expected cost for participants.[20] Therefore, for firms to choose explicit collusion over tacit collusion, the expected benefits must be higher. This would be the case if tacit collusion failed to deliver the same outcomes, for example if it was too difficult for firms to second-guess a mutually beneficial outcome or to monitor how others adhered to it. In the case of no-poach agreements, the feasibility of tacit collusion between employers will depend upon the specific circumstances of each market. However, not poaching rival employees appears a relatively simple focal point and reasonably easy to monitor, suggesting tacit collusion may be feasible.

B. Effect of Recent Developments

The recent attention on labor markets by some competition authorities must have affected how rational firms consider the relative pros and cons of tacit versus explicit collusion.[21] While just over a decade ago awareness of the potential for penalties from entering into a no-poach agreement may have been low, it is now implausible that awareness will not have risen significantly. All else equal, this will have risen the expected cost of participating in explicit collusion.

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14 The strength of the monopsony power will depend on how meaningfully the agreements decrease the ability for each firm's current workers to work elsewhere in search of higher wages. The existence of other employers not party to a no-poach agreement will only reduce monopsony power if employment there is attractive. This may not be the case even with higher wages if it included increased travel or worse working conditions to the worker concerned. Note also that if wage discrimination is not possible, then employers may be unwilling to fill vacancies, even if a pool of potential workers unaffected by no-poach agreements exists.

15 Genuine bilateral negotiation is more likely the greater the specific skills required and the harder those skills are to acquire. By definition, no-poach agreements most directly affect current workers, who may have acquired job specific skills or revealed information on their skill levels relative to potential replacements.

16 See, for example: Cahuc, P., Postel-Vinay, F. & Robin, J.M., *Wage Bargaining with On-the-Job Search: Theory and Evidence*, Econometrica, Vol. 74, No. 2 (March 2006), pp. 323-364.

17 For an example of an argument for increased enforcement in this direction, see Krueger & Posner (2018).

18 It is worth noting that currently not every competition authority may have the ability to take action against explicit collusion by employers (for example in New Zealand or Australia). This might provide an interesting "natural" experiment for future empirical economic research on the effects of enforcement action in this area.

19 A punishment strategy could be to poach significant numbers of staff or target the firm in another way, perhaps in a downstream market.

20 Assuming firms are aware of the law and consider that there is a risk of detection and punishment. The considerable efforts exerted by competition authorities to raise the awareness of cartel provisions and the need for compliance programs in their respective jurisdictions suggest this may not be a trivial assumption. See for example: OECD, *Competition Compliance Programmes*, OECD Competition Committee Discussion Paper (2021) http://oe.cd/ccp.

21 While there is debate about the size of the deterrence effect, it is undeniably an important rationale for intervention for many competition authorities.

However, as is rarely the case, all else is not equal. Notably, there has also been an increased interest in the existence of non-compete clauses in employment contracts, with several jurisdictions publicly stating their intentions to crackdown on the practice.[22] Non-compete agreements are vertical agreements that place restrictions on worker's short-term alternative employment prospects. They may deliver outcomes nearly identical to no-poach agreements without explicit collusion and there is evidence to suggest that non-compete clauses are reasonably prevalent.[23] Given the recent developments, they may be less attractive for employers in the future. If so, then explicit collusion could be more appealing to some firms as expected benefits rise relative to alternatives.

Going forward, competition authorities and policymakers should be mindful of the effects of different enforcement actions on the incentives of employers. If necessary, this could include considering how to tackle employer purchasing power acquired through tacit collusion, such as market studies or advocacy.

IV. LESSONS FROM CUSTOMER ALLOCATION CARTELS

No-poach agreements could be considered the mirror image of customer allocation agreements by sellers. Buyers' cartels and sellers' cartels are not identical; no two cartels will be. However, there is value from such an analogy due to the relative wealth of experience of sellers' cartels. For example, such experience may provide clues on buyers' cartels, including no-poach agreements, that may be of benefit for competition authorities in considering how to detect them. It could also offer insights into their prevalence. The final section of this article provides two examples from sellers' cartels and relates them to no-poach agreements. There are likely to be more lessons available.

A. "Do" Poach Agreements

The European Commission's pre-insulated pipe cartel case in Denmark offers an example of a potential mechanism that may have relevance to buyers' cartels.[24] The cartel, formed between sellers of pre-insulated pipes, faced a market entrant that was not part of the agreement. As part of their response, they agreed to collectively poach key staff from the entrant to weaken it.

While the focus of this piece has been on agreements not to poach employees, an important part of cartel formation is the ability to punish firms that deviate from, or externally threaten, the agreement. In this context, there is potential for cartelist employers to adopt a "do-poach" element in agreements. Entrants that experience a collective effort from rivals to poach their staff may have stumbled onto something, and competition authorities may wish to keep an eye out for such situations.[25]

B. Loser Fees and Burning Switchers

Another potentially interesting example, also from the 1990s, is from an Australian Freight cartel.[26] During the cartel period, part of the agreement between the firms was that they would not poach each other's customers. As noted previously, this is the mirror image of a no-poach agreement. The cartel also included provisions to deal with breaches of the agreement, for example if a customer insisted on switching. This included the payment of "loser fees" as compensation between cartelists to restore balance. Intriguingly, the cartelists also enacted a policy to "burn" switching customers by deliberately providing them with poor service. On at least one occasion, this caused delays to the freighting of a perishable good.

Such mechanisms have the potential to make cartels significantly more stable, so it is worth considering their applicability to no-poach agreements. On the face of it, it would appear easier for an employer to avoid suspicion by refusing to accept a new employee than for a seller to refuse a new customer. In some circumstances though, it may be better for employers to allow a switch if not to do so would raise suspicions. Therefore, if seeking to detect no-poach agreements, it may be worth monitoring the durability of job switches in addition to overall switching levels.

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22 For example, in July 2021, the Biden Administration issued an order encouraging the FTC to ban or limit non-compete agreements.

23 According to Starr (2021), 18 percent of U.S. workers have such clauses in their contract: Starr, E. et al, *Noncompetes in the U.S. Labor Force*, Journal of Law and Economics (2021).

24 1999/60/EC: COMP IV/35.691/E.4 - *Pre-Insulated Pipe Cartel* (1998).

25 While poaching staff from rivals is part of the competitive process, coordinated efforts to strategically poach staff from a new entrant could result in unusually high numbers of simultaneous departures evenly distributed among rivals.

26 Press release, Australian Competition and Consumer Commission, *Transport company, executives found guilty of attempted price fixing*, MR 039/98 (February 26, 1998).

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