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THE PROMOTION OF COMPETITIVE NEUTRALITY BY COMPETITION AUTHORITIES – Attacking State Restraints and Assuring Competitive Neutrality

- Paper by Eleanor M. Fox -

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Attacking State Restraints and Assuring Competitive Neutrality

– Paper by Eleanor M. Fox* –

Introduction

1. State restraints comprise some of the most harmful restraints on competition; therefore the OECD recommendation on competitive neutrality is critically important to a competitive marketplace. I want to argue, however (and I realize, against years of tradition), that the project of competitive neutrality is mis-framed. The project would be better framed as "controlling undue state privileges and other restraints." The important task is not to level the playing field but to protect the market. Fairness to private firms is a by-product benefit.

2. Second, I argue, the extent to which the competition LAWs of a number of jurisdictions reprehend undue state restraints is underappreciated. Therefore stress need not be principally on advocacy but equally on law enforcement and the opportunity for law reform. Jurisdictions should be better apprised of law reform opportunities.

3. Third, the task to reprehend undue state restraints is frustrated because of the separate silos assigned to public and private restraints, the overbreadth of a lobbying defense, and the too-easy acceptance of a sovereignty defense, especially in cases of cross-border restraints. The institutional structure of the European Union offers a basis for overcoming these hurdles and integrating the trade-and-competition disciplines. Regional market integration depends on it.

1. The immense harm from state restraints and the relevance of competition law and policy

4. In 1995 Fox & Ordover wrote, thinking globally: *"It is debatable … whether much would be accomplished … on harmonization only on a cartel principle without removing tensions at other notable points, for example, … anticompetitive government action."*[1]

5. In 2005, Professor Tim Muris wrote:[2]

> *"Protecting competition by focusing solely on private restraints is like trying to stop the water flow at a fork in a stream by blocking only one channel."…*
>
> *"[R]egulatory success in attacking private restraints increases the efforts that firms will devote to seeking public restraints. Indeed rational firms are likely to prefer public restraints. Public restraints can be far more effective at restraining competition."*[3]

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* Eleanor Fox, Professor, New York University School of Law, December 3, 2021.

[1] Eleanor M. Fox and Janusz A. Ordover, The Harmonization of Competition and Trade Law – The Case for Modest Links of Law and Limits to Parochial State Action, 19 World Competition 5, 11 (1995).

[2] Timothy Muris, Principles for a Successful Competition Agency, 72 U. Chi. L. Rev. 165, 170 (2005).

[3] Id. at 170.

6. These are immutable observations. Yet the law is hardly robust in eliminating undue state and local state privileges and restraints (hereinafter "state restraints"). The difficulty lies not in identifying the restraints as harmful to competition. The difficulty is two fold. One, it lies in distinguishing restraints *unnecessary* to fulfill a reasonable view of the public interest, for government must be given room to operate, and bona fide state restraints very often have by-product effects that we would not want to expose to competition law challenge. The second difficulty is institutional: designing a competition system that allows a challenge to undue state restraints without (for a number of jurisdictions) threatening separation of powers and the balance of power between legislative and executive/administrative functions.

7. Advocacy by the competition authority does not face these problems. The competition authority can assess the state conduct or measure and advocate. Effectiveness depends on persuasion. Persuasion is a good but weak tool. Persuasion is not likely to work in the worst cases of vested interests and cronyism where those with power want to keep their privileges. Competition law enforcement against excessive and competitively harmful state restraints is obviously a much stronger tool, if it can be judiciously crafted and can be adopted. A number of jurisdictions have overcome the two challenges – identification of which state restraints are unreasonable, and a system that protects against undue interference by the competition authority with other branches of government.4 This essay argues that competition law enforcement should be recognized as a critically important component if we want to make markets more competitive and, also, to realize the promise of regional integration.[5]

2. The OECD Project; the 2021 Recommendation

8. The OECD project on competitive neutrality is an important piece of this effort. But why is it framed as "competitive neutrality"? Why is it framed in terms of assuring a level playing field for private actors who would otherwise face a competitive disadvantage with public actors? Do we care centrally about disadvantages to private firms, or do we care centrally about making the market work? To be sure, disadvantage to private firms vis-a-vis state-privileged firms can be a clue to harm to competition, but it is also true that we could achieve competitive neutrality by privileging all firms equally (everyone gets the same subsidy) without curing the competitive harm, and that competitive neutrality is only a piece of undue state restraints.

9. The 2021 recommendation[6] actually nods in the direction I suggest. The following three recitals highlight the market problems (almost) delinked from neutrality claims:

> *"HAVING REGARD to the 2017 Ministerial Council Statement recognising 'the need to address market failures and prevent government policies and business practices that distort competition, including state aids and subsidies' …;*

[4] Eleanor Fox & Deborah Healey, When the State Harms Competition, 79 Antitrust L.J. 769 (2014).

[5] Eleanor Fox, Integrating Africa by Competition and Market Policy, forthcoming, Review of Industrial Organization, available on SSRN, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3873432 .

[6] See Recommendation of the Council on Competitive Neutrality, OECD, adopted 30/05/2021, https://www.oecd.org/competition/competitive-neutrality.htm.

"RECOGNISING that competition promotes efficiency, helping to ensure that goods or services offered to consumers more closely match consumer preferences, producing benefits such as lower prices, greater choice, improved quality, increased innovation, and higher productivity;

"RECOGNISING that government actions may distort competition in the market …."

10. But of course the Recommendation returns to its neutrality core:

"CONSIDERING that governments are increasingly developing tools to address distortions related to competitive neutrality …."

11. The document recommends that adherents should ensure competitive neutrality by:

"1. Ensuring that the legal framework applicable to markets in which Enterprises currently or potentially compete is neutral and competition is not unduly prevented, restricted or distorted. To this effect Adherents should: …

"iii. Carry out competition assessments that identify and revise existing or proposed regulations that unduly restrict competition …".

12. As a thought experiment, we might notionally remove the words "neutral" and "neutrality." What is the effect? The effect is a recommendation that agencies try to ensure against government actions and measures that "unduly prevent, restrict or distort competition." Is this not a better framing? – a recommendation against undue government restraints?

3. Competition LAWs of a number of jurisdictions reprehend undue state restraints; should this be a best practice?

13. The competition laws of a number of jurisdictions reprehend undue state and local restraints. These were compiled and analyzed, as of several years ago, in Fox & Healey, When the State Harms Competition, as part of an UNCTAD project. [7] An appendix highlights sample statutory provisions.[8] An updated copy of the appendix is available.[9] The sample provisions span the range from equal coverage of SOEs, to application of competition law to enterprises granted exclusive rights and special privileges, to public procurement including provisions that allow the competition agency to challenge complicit public officials, to free movement of goods and services clauses that reprehend unreasonably restrictive cross-border state/provincial measures, to abuse of competitive neutrality, to abuse of government administrative power to harm competition, and, where the competition law does not cover or remedy the conduct, authorization of the competition authority to challenge anticompetitive state acts, e.g. in court.

14. Much of the competition agency activity challenging government restraints involves local/municipal restraints. Among the jurisdictions most active in this area are Russia and Lithuania. Peru is one of the jurisdictions most active in annulling regulations that are "bureaucratic barriers." Peru annuls thousands a year. The European Union is the most prominent jurisdiction that has a holistic appreciation of combined state and private

[7] Fox & Healey, supra note 4.

[8] https://unctad.org/system/files/official-document/ditcclp2015d6_en.pdf.

[9] An updated version is available on request from eleanor.fox@nyu.edu or her assistant heldenfels@mercury.law.nyu.edu.

restraints. This grew naturally within the European common market, but the various threads have been adopted in many national laws. The EU framework, which foresees a challenge to hybrid cross-border public-private restraints, has great potential for regional FTAs and common markets, as treated below.

15. The subject of national competition laws addressing undue state restraints is a good candidate for seeking to formulate best practices or at least to facilitate cross-fertilization with a view to law reform. In its international implications, it is at least as important as seeking convergence on substantive cartel principles.[10]

4. The silo problem and the need to fuse public and private restraints where they are intertwined; the regional benefits of a holistic vision

16. The sharp separation of public and private restraints is a problem. While there are some private restraints that exist without state facilitation, public restraints are often adopted to support private vested interests; at the extreme, corruptly so, as in the (common) case of procurement officials in league with bid riggers. Often there is an interplay between private interests that have captured the regulator – as in Mexico's hybrid restraint that pushed the price of cross-border telephone calls up to the highest levels in the world,[11] the Saskatchewan potash producers who played off the dumping laws and the antitrust laws,[12] the US aluminum industry that hid behind a government plan to control the flood of imports from Russia,[13] and the Italian matches industry, which met its match in EU law, which caught both the public and private restraints.[14] The intertwining is perhaps most noticeable in developing countries with high levels of corruption, where goods do not naturally flow over the borders that logic would predict; leading firms somehow get the privilege to stay dominant in their markets, protected below the radar screen from competitive imports.[15]

17. Restraints may be public, they may be private, they may be a combination; if the competition agency is empowered to challenge both, it will have sources of data and evidential bases to connect the dots to which it would not otherwise have access. Procurement bid-rigging is a good example.

18. The problem distinctly surfaces in connection with regionalism. Regional integration holds the promise of many benefits through scale, scope and vision, especially in a region of developing countries where competition agencies are often too small or under-resourced to fend for themselves. Theoretically, regionalism can overcome these limitations. Yet border restraints of member nations (often hybrid with leading firms) are

[10] See Fox & Ordover, supra note 1, at 11.

[11] See Eleanor Fox, WTO's First Antitrust Case – Mexican Telecom: A Sleeping Victory for Trade and Competition, 9 JIEL 271 (2006).

[12] See Bloomkest Fertilizer v. Potash Saskatchewan, 203 F. 3d 1028 (8th Cir. 2000).

[13] See Frederic Jenny, Competition, Trade and Development Before and After Cancun, in Fordham Corp. L. Institute, Chapter 26, 631, 633-35 (B. Hawk ed. 2004)

[14] Consorzio Industrie Fiammiferi (Italian Matches), Case C-198/01, EU:C:2003:430.

[15] See, e.g., Simon Roberts, Common Law Prescriptions and Competitive Outcomes: Insights from Southern and East Africa, Chapter 8 in RECONCILING EFFICIENCY AND EQUITY: A Global Challenge for Competition Policy (D. Gerard and I. Lianos, eds. Cambridge 2019).

a most serious problem, and unless the border restraints fall, the region – such as the whole African continent, will never be effectively integrated, despite a common market.[16]

19. The European Union institutional framework provides an attractive starting point for a solution. The EU law prohibits unreasonable state restraints as well as unreasonable private restraints. It spells out, through its case law, what is an unreasonable state restraint – protecting the states' rights to protect their people but condemning state acts and measures that unreasonably and disproportionately harm trade and competition in the Union. Building on the model, nations and regions can develop a trade-and-competition violation or at least a mode of tight collaboration that allows trade (internal market) and competition authorities to join forces in understanding and prohibiting hybrid restraints.[17] Likewise, on national and cross-border levels, competition officials and prosecutors might tightly collaborate (there are models, as in the Brazilian "car wash" scandal) to prove and prohibit a fused competition/corruption offense.

5. Conclusion

20. Undue state restraints are a huge problem that can undermine effectiveness of competition law, both nationally and cross-border. Competitive neutrality is a corner of the problem. Most competition laws are not fit for the task. Nor do any other laws (such as commerce clauses) do the job. Therefore unreasonable state restraints boldly "wander around," undisciplined. Empowering competition authorities to challenge unreasonable state restraints, whether or not tethered to competitive neutrality, promises to significantly improve competition in nations, in regions, and in the world.

[16] See Integrating Africa, supra note 5. See also Eleanor Fox, Competition Law, Developing Countries, and Regional Agreements: Tearing Down Silos and Building Up Scaffolds, Afronomics Law, August 2, 2021, https://www.afronomicslaw.org/category/analysis/symposium-introduction-markets-competition-and-regional-integration-global-south.

[17] Integrating Africa, supra.