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COMPETITION POLICY

1994 WORKSHOP WITH THE DYNAMIC NON-MEMBER ECONOMIES

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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FOREWORD

This document presents the main papers and summary of the proceedings of a workshop on Competition Policy held in Paris on 1st and 2nd December 1994 as part of the ongoing Policy Dialogue between OECD countries and the Dynamic Non-Member Economies (DNMEs).

The workshop brought together over 90 participants and observers from OECD countries and DNMEs (Argentina, Brazil, Chile, Hong Kong, Korea, Malaysia, Chinese Taipei and Thailand), the World Bank, UNCTAD and the Institute for International Economics in Washington. The Business and Industry Advisory Committee to the OECD was also represented. All participants attended in their personal capacities.

As this was the first OECD/DNME workshop on competition policy, the focus for discussions was broad: the economic rationale for competition policy; how it relates to other economic policies, especially trade policy and regulation of specific sectors; what should be the objectives and scope of competition laws, including sectoral coverage; and finally how the laws should be enforced, involving the creation of appropriate institutions both at national and international levels.

The workshop was held under the overall Chairmanship of Mr. Frédéric Jenny, Vice-Chairman of the French Competition Council and current Chairman of the OECD Committee on Competition Law and Policy. In addition to the introductory session, the workshop was divided into four sessions. The four Chairmen were: Mr. Kyu-Uck Lee, Vice-Chairman of the Korean Development Institute; Mrs Janet Steiger, the then Chairman of the United States Federal Trade Commission; Mr. Noël Renaudin, Head of the French Competition Service in the DGCCRF, Ministry of Economics and Mr. Claus Ehlermann, Director-General of the Competition Directorate of the European Commission.

The views expressed in the papers are those of the authors only. The papers and proceedings are published on the responsibility of the Secretary-General of the OECD.

Makoto Taniguchi
Deputy Secretary-General

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WELCOMING ADDRESS

Makoto Taniguchi
Deputy Secretary-General of the OECD

Mr. Chairman, Ladies and Gentleman

It is a great pleasure for me to welcome you to this workshop on Competition Policy.

This workshop is the first to take place in OECD's Policy Dialogue with the Dynamic Non-Member Economies since the OECD's High Level Meeting with the DNMEs in Tokyo, on 19 October 1994.

The Tokyo High Level Meeting strongly expressed the view that the OECD/DNME Policy Dialogue should become an instrument by which the major actors in the world economy seek a convergence of view on appropriate economic policies. Based on this, the OECD Council has decided to strengthen the dialogue at the horizontal and sectoral levels. It has also been decided to hold High Level Meetings on a more regular basis in the future to discuss interrelationships of sectoral issues, and to orient the Policy Dialogue for the evolving challenges and opportunities of the 1990s.

So the Dialogue has come a long way since it was first launched with the Dynamic Asian Economies in 1989. As many of you are aware, in 1993 the dialogue was then extended to some Latin American countries that have made considerable progress towards stabilizing, liberalizing and restructuring their economies. In the dialogue, participants have explored many topics at the heart of the OECD/DNME economic relationship, particularly in the trade, investment and macroeconomic areas -- all drawing on the OECD multi-disciplinary approach.

It is appropriate that this is the first time that the DNME Policy Dialogue address the issue of competition policy. Consistent with the conclusions of the High Level Meeting, the OECD Council has also identified competition policy as a priority topic of the future. And we hope that workshops in the competition policy area might also make a contribution to future High Level Meetings.

For the background of our DNME partners, the OECD's Committee on Competition Law and Policy was established in 1961, primarily as a means of promoting international co-operation among competition policy authorities and officials in OECD Member Countries. The range of the Committee's activities has broadened considerably since that time, reflecting the growing recognition of the significance of competition policy. The OECD is aware that competition policy is a subject of interest well beyond the boundaries of our Member countries and that it is becoming an increasingly important subject at the regional and global levels.

What is the reason for this interest? It is clear that in a time of rapid economic change and development, governments are increasingly conscious of the need to ensure that domestic markets are operating to maximum advantage and that the economic reforms which are being undertaken are not stifled by the creation and maintenance of artificial barriers to market entry. Competition policy has a key role to play in this process. There is already a discernible convergence of ideas concerning competition policy.

Although there are marked differences in legal form and procedures for enforcement, there are nevertheless signs of convergence in terms of broad objectives and methodology.

It is recognized that for competition policy to be effective there is a need for more than the enactment of yet more laws. There is also a need for effective enforcement, a well thought-out agenda in terms of the relationship of competition policy with other government policies and finally, but not least, for the co-operation of the business community in the development of polices and institutions to implement them, which will help to achieve a more competitive economy.

At the global level, competition policy has become a prominent feature on the agenda of many international gatherings, particularly among economies with common trading interests. Within the OECD, the relationship between trade policy and competition policy is currently being explored jointly by the Committee on Competition Law and Policy and by the Trade Committee. The primary objectives are to ensure that the impact of trade liberalization on markets is complemented by a non-discriminatory and active domestic competition regime, to ensure that trade policy does not reduce competition, and to minimize areas of possible conflict. The relationship between trade and competition polices has already been addressed in previous trade policy workshops of the OECD/DNME Policy Dialogue.

As you are aware, the role of competition policy in the trade liberalization process has become of such general interest of late that it may become a topic of discussion in the context of the GATT/WTO talks, although this idea is still at a preliminary stage of discussion. Whether or not it becomes an issue for GATT discussion the subject will undoubtably be of continuing importance in the OECD.

These are some of the policy decisions which are the subject for discussion at this workshop. I hope that they will be the subject of an interesting and lively debate.

The great advantage of a workshop like this one, is that it provides the opportunity for experts to exchange ideas and share experiences on the role of competition policy in a market economy and also, I hope this workshop will provide a chance to make contacts which will form the basis for on-going communication between participating competition policy makers and enforcement agencies. In addition to participants from the government sector, we are also pleased to have with us today, a number of representatives from academic institutions and from the business community who are able to make their own significant contribution to debate. In this connection I would like to remind you that everyone participating in this workshop can contribute in your own individual capacity, not necessarily representing your own institutions or government.

To all of you here I would like to wish you a lively and fruitful discussion.

INTRODUCTORY REMARKS

Mr. Frédéric Jenny
Chairman of the OECD Committee on Competition Law and Policy

Mr. Taniguchi, Ladies and Gentlemen

As Chairman of the OECD Committee on Competition Law and Policy, I would just like to add my own welcome, both to colleagues from the Committee, many of whom are here today, and to participants and observers from Asia and Latin America who are here to share with us their own ideas and experiences on competition policy.

A meeting such as this makes one particularly conscious of the internationalization of competition policy. Although competition laws have existed in a number of industrialized countries for decades, in the last few years there has been a been a noticeable surge of interest in both OECD and non-OECD countries in competition policy as a means of improving economic performance. There are several reasons for this development which has characterized the 1980s. The failure of central planning and direct government regulation of the economy in achieving growth and efficiency have led to a turning towards macro-economic reforms. Competition policy, although not the only relevant policy, is an integral part of such a reform process, as many countries have recognized.

Beyond this, extensive government ownership and regulation have been used in the past in conjunction with restrictive trade policies. Successive international trade liberalization initiatives such as those we have just witnessed with the conclusion of the Uruguay Round have now seen the removal of many tariff and non-tariff with a consequential opening up of the international markets. This increased reliance on market forces has led to new concerns and it is becoming more generally recognized that certain types of business practices may frustrate or offset the benefits expected from trade liberalization unless they are properly dealt with. Competition policy in addition to dealing with restrictions which restrain the competitiveness of domestic rivals is also increasingly having to consider the impact of such restrictions on international trade. As Mr Taniguchi mentioned, recent speculation over the role of competition policy in an international trade forum, such as the WTO, has also sparked a wider interest in the subject of competition policy. What is clear at the moment is that for any further steps to be taken to facilitate the effectiveness of enforcement at the international level, we as competition specialists should have an agenda which would include:

-- first, a clarification of what the role of competition policy is within our respective economies;

-- second, an attempt to strive towards some convergence of views on the basic goals of competition law and policy;

-- third, to try to obtain agreement on the fundamental features of competition law; and

-- fourth, work together to refine our methodological tools of analysis in enforcing competition law.

Clearly, we can only have a preliminary discussion of such matters in this seminar over a couple of days but it is my hope that the contacts which are made here will help us make strides towards future international co-operation. I am particularly looking forward to hearing the views of our colleagues from the Dynamic Non-Member Economies about how they see the future of competition policy in their own economies.

INTRODUCTORY SESSION

THE CONTRIBUTION OF COMPETITION POLICY TO ECONOMIC DEVELOPMENT

Charles Oman
OECD Development Centre

Mancur Olson drew our attention, in his 1982 book entitled *The Rise and Decline of Nations*, to the serious harm that the actions of oligopolistic rent-seekers, organised special-interest groups, what Olson also called "distributional cartels", can do to a nation's welfare. In stable societies, where special-interest groups can organise and tend to accumulate over time, the costs to society can be huge -- far greater, notably, than the simple static inefficiencies one would expect to result from monopoly pricing.

The main effect of oligopolies, as distinct from monopolies, is to introduce more and more rigidity into society, through their actions both in the market and in politics. They tend to retard a society's ability to adapt new technologies, for example, and, more generally, to inhibit resource reallocation in response to changing conditions. While oligopolies resist change, moreover, when they do adjust they tend to adjust quantities rather than prices, which accentuates the business cycle. While oligopolistic market structures thus create price "stickiness" and retard an economy's natural adjustment to change in underlying "fundamentals" (consumer preferences, technology, etc.) such economies are also plagued by price instability in the form of oligopolistic "price wars". Oligopolies impose further costs on society because of their tendency to engage in heavy investment in excess capacity, which allows firms rapidly to expand output and benefit from economies of scale if a price war occurs, and in "competitive advertising", which, by definition, does not increase total demand for a product or service but is incurred by firms in the struggle for market share. Oligopolies also greatly increase the complexity of regulations, both private and public, thereby adding to the accumulation of rigidities in society that are reflected in economic as well as political bureaucratic inertia. All of this can greatly retard growth and impose significant cumulative losses on society, in terms of foregone potential income and welfare, above and beyond the static costs of inefficient resource allocation that can be expected to result from monopolistic behaviour.

The growth of oligopolistic structures in the leading OECD countries during the 1950s and 1960s was accompanied by a gradual building up of rigidities that led, finally, from the late 1960s and especially during the 1970s, to a marked slowdown of productivity growth. That slowdown led in turn, in the latter half of the 1970s, to the emergence of stagflation in the United States and Europe.

The OECD policy response to stagflation was two-fold: interest rates were driven up, phenomenally, to bring inflation down; and markets were deregulated, to stimulate competition, in order to improve their functioning. Both responses were launched by the Carter Administration, in the late 1970s. High interest rates, induced by the Fed under Paul Volker, also contributed both to bringing on the recession of the early 1980s, and to the explosion of the "Third World Debt Crisis" in 1982. The latter in turn led many developing countries, notably but not only in Latin America, to turn from a largely inward-oriented approach to development policy, or "import-substituting industrialisation", to a much more outward-oriented and market-friendly approach.

The other policy response, market deregulation, was seen in the United States, and soon after by the Thatcher government in the United Kingdom, as the best way to overcome economic stagnation by combating the rigidifying effects of entrenched oligopolies. "Anglo-saxon" deregulation in turn put considerable pressure on continental Europe to follow suit, which led to the launching in 1985 of the Single Market programme.

Why is this discussion of "distributional cartels" and oligopoly relevant to economic development? There are two reasons. One, less important, is that Europe's Single Market programme points up the potential utility of regional integration agreements as a tool of competition policy for non-OECD as well as for OECD government. Such agreements can serve as a tool both to enhance competition in domestic and regional markets *per se*, and as a vehicle for achieving greater harmony in the convergence of competition laws and policies among countries. The second, less obvious but critical reason, is the relevance of Olson's analysis for understanding the root of many "structural" problems faced by numerous developing countries.

Olson himself believed that his analysis did not apply to developing countries, because he saw them as "inherently unstable" societies. But I am convinced he was wrong on this point. Highly concentrated oligopolistic power structures in both the private and public spheres are, if anything, more prevalent -- and their effects more nefarious -- in developing countries than in OECD countries. The "inherent instability" Olson perceived in developing countries is, I believe, very much a reflection of the instability caused by acutely oligopolistic structures which prevail, economically and politically, in many developing countries.

Four types of phenomena found in many developing countries -- veritable caricatures of what one can also find in developed countries -- illustrate the relevance of Olson's analysis to developing countries. All are phenomena which Olson's analysis points up as to be expected in societies plagued by highly concentrated oligopolistic structures and behaviour:

-- a high level of complexity of bureaucratic regulations, a great deal of government intervention, and significant bureaucratic inertia;

-- high levels of investment in excess capacity, competitive advertising and market segmentation in the "modern sector", which co-exist "paradoxically" with the problem of capital scarcity that virtually defines a developing country;

-- capital-intensive technologies in the "modern sector" -- which also appear paradoxical because they are highly insensitive to relative factor prices in labour-abundant economies -- and slow adoption of new technologies;

-- highly divisive local politics.

Competition policy, and the need to promote vigorous domestic competition as part of the foundation on which to build international competitiveness, is not merely as important for developing countries today, including many of the DNMEs, as it is for OECD countries. For many, it is in fact more important.

Nor is competition policy in developing countries "merely" a matter of reducing or overcoming the costs of monopolistic inefficiencies, important as it is to reduce those inefficiencies. It is above all a matter of promoting long-term growth and development. This is not a matter for developing countries alone, of course; and indeed, "globalisation" has focused new attention on it in OECD countries as well. But surely no country can be more concerned to achieve it than a developing country.

In conclusion, I wish to address a bit further the question of whether competition policy should strive to promote static economic efficiency or dynamic efficiency. My view is that, particularly for developing countries, Olson's analysis points strongly to the importance of promoting dynamic efficiency, even if that implies that a larger proportion of welfare gains should go to producers, relative to consumers, than if the objective is to promote static consumer welfare maximisation.

This is of course a contentious point. In broad terms, anglo-saxon economics tends to see competition policy as anti-trust policy, because of its view of the role of competition policy, set in a framework of comparative statics, as seeking to maximise consumer welfare. But many developing countries are also greatly concerned about how to develop firms within their borders that will be large enough, that will have the critical mass so to speak, to be able to compete in global markets. I would therefore argue for what might be called a more "Schumpeterian" view of the role of competition policy, as distinct from static consumer welfare maximisation and pure anti-trust, in the design and enforcement of competition policies -- policies that are, indeed, of vital importance today for economic development, and too often ignored or neglected in developing countries.

THE INSTRUMENTS OF COMPETITION POLICY AND THEIR RELEVANCE FOR ECONOMIC DEVELOPMENT

R. Shyam Khemani, World Bank[1]

Introduction

"Competition policy" in this context is defined in the broad sense as consisting of two parts -- one which is commonly referred to as "antitrust" or "competition" law and the other, which comprises micro-industrial policies such as tariff and non-tariff policies, foreign direct investment, unnecessary government intervention in the market place and economic regulation designed to prevent anti-competitive business practices by firms. Both parts of the policy impact on economic agents in the market place. "Competition" itself can be broadly defined as "the rivalry between sellers for the patronage of buyers both in price and non-price terms".

These definitions form the background to the key question with which we are concerned -- should countries be adopting competition policy as part of their economic framework policies to enhance economic development? The short answer to that question is that they should! The purpose of this paper is to briefly summarize some of the debate which surrounds the issue and explains why an appropriately designed competition law should have a central position in government framework policies.

The Objectives

Various objectives have been ascribed or suggested for competition law and policy over time and across different countries. While some countries have tended to place the emphasis on economic efficiency, others have combined the goal of economic efficiency with the impact of competition on the broad public interest, as a result of which factors such as employment, diffusion of economic power, regional development and pluralism also play a role in decision making. The difficulty is that it may not always be easy to balance such different and often conflicting interests. In our view, it is therefore preferable to pursue non-economic objectives through separate government policies.

Even where it is agreed that competition policy should be directed primarily towards economic efficiency, there is often debate over whether the aim is static or dynamic efficiency. In our view, governments do not have to directly foster one or the other. An environment where there is rivalry and where competition policy is widely taken into consideration will foster dynamic as well as static efficiencies. There needs to be a total economic welfare approach, not so much one entailing intervention but rather one which conditions the environment in which firms operate.

An issue which is particularly, although by no means exclusively, of concern to newly industrializing countries is whether competition policy should try to maximize consumer welfare or total (*i.e.* consumer plus producer) economic welfare. The answer to this question can affect the implementation

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1. This is a summary of "The Instruments of Competition Policy and their Relevance for Economic Development" by R. Shyam Khemani and Mark A. Dutz published in Claudio Frischtak (ed.) **Regulatory Policies and Reform in Industrializing Countries** (1995).

of competition law. For instance, some economists argue that the pressures of global competition make it necessary for governments to foster a few large domestic industries to act as "national champions" at least in the short run. This often results in the sacrifice of consumer welfare maximization in favour of producers. Empirical evidence on the question of the correlation between firm size and economic performance suggests that although high levels of industrial concentration are not necessarily inimical to competition, government policies of "picking winners" through high industrial concentration are often unsuccessful.

Is Trade Liberalization Sufficient?

If what is necessary is establishing the conditions of competition, does this mean that trade liberalization alone can act as an effective competition policy? There are some economists who suggest that with the removal of tariff and non-tariff barriers, imports will sufficiently temper market power so as to make a specific competition law redundant. There are however a number of factors which contradict this "trade liberalization alone" approach. One is that a large and increasing proportion of economic activity in industrialized, developing and emerging market economies relates to the non-tradeable sector on which import competition tends to have little impact. In addition, high transport costs and other barriers to entry can insulate domestic firms from foreign competition. Certain types of anticompetitive arrangements and business strategies also develop which can dampen the effects of import competition. Moreover, it is recognized that international trade policies, particularly anti-dumping policy are not necessarily structured to promote economic efficiency. For these and other reasons, it is not realistic to assume that liberalized trade will effectively substitute for and play the same role as competition policy.

The East Asia Experience

In recent years, a number of dynamic and high performing economies in East Asia have had higher growth rates than western industrialized countries and yet many of these countries have had no specific competition law. What is interesting is that the countries which have been successful have had what is in effect -- a competition policy. A World Bank study indicates that there are distinctive differences in the economic strategies followed in the 23 Asian countries which were the subject of the study. A strategy which is successful for one country is not necessarily transferable to another. The one common denominator is the high degree to which firms were exposed to domestic and/or international sources of competition. What is important is the degree of inter-firm rivalry which exists.

The perceptible trend away from protectionist policies has been generated not only by economic growth but also by concerns about fiscal constraints on government spending. Countries which have traditionally protected domestic firms found that protection was becoming unaffordable and this has become the catalyst for deregulation and liberalization.

While national governments can control their domestic market they cannot, if they are exporting nations, control the environment in which their firms operate. Competition law can help to ensure that sort of rivalry is sustainable on the international level. Since in the case of export industries the government is unable to control market conditions, protecting national industry may simply encourage inefficient practices which would be reflected in that firm’s performance on the international level. The World Bank study indicates that firms which face domestic competition are those who have been most successful internationally.

What this means is that even countries without a competition law -- so long as they have a policy to expose their firms to competition in the domestic market -- will find that this will foster growth. What would assist in ensuring that such growth is sustainable is a vigorous competition policy, including a competition law.

In the case of government assistance which takes the form of subsidies or state aids the lesson which has been learnt in the successful Asian countries is to provide incentives for rivalry rather than handouts to favoured enterprises. The government through these instruments can provide incentives.

Major Provisions of Competition Law

Competition laws generally consist of substantive conduct and structural provisions relating to business activity, together with additional procedural provisions on administration and enforcement. An advocacy role for the competition agency to promote competition in government policy-making can be a very important addition.

Laws which deal with the effects of horizontal collusion (i.e. restraints agreed by enterprises operating in the same market) are a key feature of most competition laws. Although it is accepted that such practices (which include price-fixing, market-sharing and bid-rigging) are serious violations they are often very difficult to prove and it may be important that the law includes provisions which give incentives to participants or injured parties to provide evidence to authorities of these activities and impose tough penalties as a deterrent. Many countries do in fact exempt certain types of cartel from prosecution where there is likely to be little impact on competition or, as with the case with R&D agreements, they have a positive impact. There is an active debate on whether export cartels should be permitted as an effective means of penetrating foreign markets or prohibited as likely to lead to unhealthy collusion on the domestic market.

Vertical restraints between suppliers and purchasers in separate upstream and downstream markets may also in some circumstances prove to be anticompetitive. There remains considerable controversy over whether particular agreements, while prima facie being restrictive of competition may in fact be beneficial to economic efficiency by overcoming certain market failures. For this reason most countries do not treat such restraints as *per se* offences but rather call for the examination of the particular restraint in the context of the overall market structure to see whether the overall impact is likely to be positive or negative. Whether distribution networks in newly developing countries disclose any specific problems is not clear and further research is required into this. Given the evolution of market structures in such cases it may be prudent to disallow long-term contracts between manufacturers and distributors which contain highly exclusionary provisions.

Of particular concern to competition authorities is the phenomenon whereby large firms dominant in a domestic market may adopt anticompetitive business practices in order to maintain and entrench their market position. In spite of the fact that most competition laws contain provisions aimed at preventing the abuse of a dominant position there is no clear determinant of what constitutes dominance. Moreover, the size of a firm is not itself a determining factor since large firm size may (particularly in market economies) be simply an indicator of economic efficiency. The analysis therefore tends to focus on the behaviour of the firm and its ability to strategically deter other entrants to the market. In previously centrally planned economies dominant firms tend to have resulted as a function of government policy, which raises the question whether an active deconcentration policy is necessary in order to create the structural basis for future competition.

Mergers and acquisitions are another form of business agreement where scrutiny may be required. It is not always easy to balance the trade-offs between the possible reduction in competition which occurs as a result of certain mergers (particularly in horizontal merger cases) and the economic efficiency gains which may result. However, the timely assessment of such arrangements may be very useful in preventing the creation or entrenchment of concentrated market structures which impede future competition. In several developing countries, concentration of wealth among a small number of families or groups may require attention to be given to conglomerate mergers. Those are generally of less significance to competition

authorities in industrialized countries where the trend at present is more towards divestment of unrelated activities and refocusing on core businesses.

Competition policy instruments are blunt not refined surgical instruments and have to be handled with care. For countries without experience in this field, a rules-based approach to competition would be appropriate and there should be the fullest interplay for market forces and the mobility of resources, deregulation and lowering of barriers to entry as instruments for promoting competition rather than law itself.

Administration and Enforcement

The experience to date of countries which have had long-standing competition regimes points to a few basic guidelines with respect to the administration and enforcement of competition law. These are namely that:

- the competition agency should be independent, insulated from political and budgetary interference and capture by interest groups;

- the agency should nevertheless be accountable (*eg.* through an annual report to Parliament);

- competition law should separate the activities of investigation, prosecution and adjudication;

- the process should build in checks and balances with rights of appeal, reviews of decisions, confidential treatment accorded to true business secrets, transparent administrative procedures and regulations;

- proceedings and case resolutions should be expeditious to avoid unnecessary transaction costs;

- to have a deterrent effect, the enforcement of the law should permit the imposition of significant penalties and various other remedies.

Conclusions

What does all this imply for the role of government and for the role of competition policy? Competition policy should not only be designed to prevent artificial constraints or private restraints on the market by business but also to foster the mobility of business from lower to higher value uses. This is not a matter of ideology but one of efficiency. Why should consumers (including business firms purchasing inputs) pay higher prices than is necessary? Why should market mechanisms that can organize production and allocate resources more efficiently not be given an unfettered role to play?

Competition law, by preventing the erection of artificial barriers to entry and facilitating market access to competitors, complements and buttresses the benefits of other government policies which promote competition. The absence of, or a badly designed and implemented, competition law can itself be a barrier to entry. For a competition law to be "appropriate" it requires more than just effective enforcement, it requires the conditioning of the business environment in which firms operate so that the process of competition itself operates to limit the discretionary exercise of market power.

What is being advocated is therefore not simply a reactive approach to specific anticompetitive situations but also a pro-active approach. This would involve competition authorities in an advocacy role to ensure that the competitive process is properly taken into consideration in broader economic policy making. This implies the up-grading of the competition enforcement authority to an active economic policy

oriented agency, well placed to argue for reduced barriers to entry and enhanced mobility of resources. This role is vital since many of the restraints on competition lie not only in the hands of private enterprise but also within the competence of government institutions and as a result of government regulation. The goal is to ensure that the type of policies which are adopted give the maximum play to market forces.

Increases in foreign investment and international trade enhance the possibility of friction between competition policies in different jurisdictions which has recently led to calls for the development of an international code to resolve problems between different countries. We share the view that development of an international code in this area may be difficult and suggest as an alternative the development of competition policy codes within regional trading blocs in the context of regional trade and economic integration arrangements.

SUMMARY OF DISCUSSIONS

PANEL I

INTERACTIONS BETWEEN COMPETITION AND OTHER ECONOMIC POLICIES

Introduction

As one speaker pointed out during discussion, competition policy does not operate as an island in the sea of economic policies, rather it is an integral part of them. It is this theme of interaction between competition policy and other economic policies which formed the basis for the first discussion session. Given the limited time available, it was only possible to deal with a few of the many interesting topics open to debate. The main areas covered were the role of competition policy in a small economy, trade liberalization, industrial policy, deregulation and privatization.

Competition policy in a small economy

The first issue raised was whether competition policy is really necessary for a small open economy. Some economists take the view that if a country pursues open trade and investment policies then these alone will guarantee a competitive outcome without the need for an explicit competition policy. However, as one participant pointed out, for an economy to be considered "open" may well presuppose the existence of some type of competition policy since, even if all tariff and non-tariff barriers and all barriers to investment were removed there may nevertheless be private barriers to entry. This is often exemplified in some service, sectors not exposed to international trade.

A commonly expressed view was that, in addition to maintaining and enforcing competition policy, one of the principal roles for the competition authority is to "keep other government authorities honest". In particular competition policy can act as a counterbalance to the possible capture by special interest groups of other government authorities. This led to debate over the justification for a policy of preferential treatment which many governments adopt to strengthen national industries in the face of foreign competition. One of the dilemmas for many newly industrialized countries is whether, in order to meet international competition, it is necessary for a government to encourage or at least overlook a degree of concentration in domestic industries.

For instance, Malaysia is a small economy, characterized by oligopolistic markets, with export based companies primarily owned by foreign investors with very few strong domestically owned companies. One participant raised the question whether in these circumstances competition policy and law is desirable and, if so, what the best timing would be for its introduction. Is it preferable to wait for the development of strong domestic companies who will be the engine of growth for the future or is it better to adopt a competition policy from the outset? If the latter, are there different types of competition policy which might be introduced at different stages of development?

In response to this, another participant expressed the view that the mere fact that the major exporting companies are under foreign ownership was itself not the problem it might at first appear to be. To support this argument, he cited Canada as an example of a country which at one time had the highest

per capita foreign investment in the world and yet did not suffer the pernicious effects of foreign ownership which some predicted. Similarly in Sweden, many of the largest and most successful companies are foreign owned but are based in Sweden to take advantage of favourable business conditions.

With respect to the timing of competition policy, there were differing views. The general consensus appeared to be that what was important was not so much that a specific type of competition law should be introduced but that government policy and business conditions should be directed towards ensuring the maintenance of conditions of rivalry between firms. In this context, it might be useful to introduce an appropriate competition law that dealt at least with the most injurious forms of anti-competitive practices. For instance, it was suggested that for many newly developing economies it would be appropriate to have a law which contained a few clear prohibitions of horizontal cartel conduct (price fixing, market sharing) and of other abuses of market power damaging to the economy. For other conduct, (with the possible exception of anti-competitive mergers) there can be a general provision which gives a green light to businesses unless they have market power (in a properly defined market) which causes undue restraint of competition. This targets the most harmful conduct without the need for heavy administrative intervention. There was some disagreement about whether export cartels should be prohibited, with some participants supporting the view that at least in the case of developing countries export cartels between small companies would be pro-rather than anti-competitive.

In general, it was agreed that competition policy was essential to guarantee the future development of a market economy and that it had an important advocacy role. There was however, no blueprint for competition law. It was suggested that the UNCTAD model law could be a useful starting point for countries planning to introduce a competition law and that expert technical assistance might be sought from bodies such as the OECD, World Bank and governments with considerable experience of competition law.

Competition and Trade

The discussion then moved on to the relationship between competition and trade policy. One of the lead speakers on this panel spoke of the growing importance of competition policy in the light of liberalized trade and investment. He warned that liberalization policies could be a force not only for positive change but also, in the absence of proper safeguards, could result in over-concentration in markets where businesses are tempted to use anti-competitive strategies to try and consolidate their own turf. Debates over anti-dumping and other forms of unfair trade practice have tended to focus attention on national interests in a narrow sense. In the speaker's view, a change of focus which would ensure non-discriminatory competition should be at the core of the new world trade order.

International co-operation between competition authorities is necessary not only to facilitate the investigation of cross-border restrictive trade practices but also to take remedial action against such practices. In the speaker's view, it will not be easy to conclude an international code on competition in the short term but it should be possible to reach some consensus on basic principles -- possibly on a regional basis. The speaker used as an example the Asian and Pacific area where rapid economic changes may require agreement on competition issues. Bilateral and trilateral co-operation agreements already exist. Australia and New Zealand for instance, some years ago harmonized competition policy under the CER Agreement. At the APEC meeting held at Jakarta in November 1994, there was a recommendation to include discussions on the linkage between trade and competition policy on the agenda of future meetings. One of the issues likely to be discussed is how far restrictive business practices impact on trade and investment. It is recognized that a regional debate on competition in APEC is somewhat complicated by the fact that not all member countries have national competition laws and even those that do, have such laws are far from having identical approaches. With time, it is hoped that bilateral or multilateral negotiation will assist in removing some of these inconsistencies.

Another reason for international co-operation is that private restrictions on competition could undermine free trade. For instance, territorial restraints along country boundaries may be used to impose price discrimination or a company with market power coerce customers into accepting tied purchases from them. In countries with a competition law, victims of such abuses can file a complaint with the local competition authority -- but what happens where a foreign company is at fault? Is it possible to prosecute that company? This comes down to the extraterritorial application of competition law and sensitive sovereignty questions, hence the need for international co-operation. A further reason concerns the treatment of cross-boundary mergers, where the companies concerned often have to apply to several authorities for approval, causing often unnecessary delay and confusion. International co-operation is necessary to reduce the transaction costs. A recent report sponsored by the OECD Competition Committee has already come up with several recommendations to facilitate multi-jurisdictional merger review.[1]

Anti-dumping can also pose problems. Penalties may be imposed on companies selling below the price of the goods in their home markets. However, in some cases the seller may be participating in legitimate price competition. This may particularly be the case where new technology has been introduced and production costs have been reduced significantly. The danger is that antidumping actions are used as a shield against genuine foreign competition.

The other concern from an international perspective is where competition authorities give the green light to practices which do not restrict competition at the domestic level but which might restrict competition at the international level. For instance, export cartels are either exempt or approved under OECD countries' competition laws. This, in the view of the speaker, is a violation of the principle of "national treatment". Such cartels are not always anticompetitive, but countries need to review their rationale for granting exemptions. Also to be considered is whether differences in national competition laws or an absence of competition law has an impact on international competition. To assess this, it will be necessary to gather information both on the substantive law and on the manner of its enforcement on a comparative basis. If there are problems as a result of such differences perhaps they could be dealt with by an international agreement on certain minimum standards.

Interestingly, Canadian law does attempt to deal explicitly with the interface between competition and trade policy. Where it can be shown that a tariff or non-tariff barrier has facilitated an anticompetitive arrangement in the domestic market, the Director of Investigations and Research may apply to the Cabinet for removal of that tariff. In addition, the Director also has a statutory right to give evidence in antidumping cases.

Finally, it was noted that within OECD member countries, there has been a trend towards a strengthening of competition policy and this has included countries which have strong free trade policies (such as those within the European Union), suggesting that trade policy was not enough.

Competition policy and Industrial policy

There was lengthy debate on the airline industry as an example of the relationship between competition policy and industrial policy, and in particular whether subsidies to encourage new product developments could be justified. Contrasting examples were given of subsidies which promoted a commercially successful product (*i.e.* the "Airbus") and where it did not (*i.e.* Concorde). It was agreed that great care has to be taken by government officials when granting subsidies. It is often difficult for government officials to assess what will become a successful product and indeed it is doubtful whether this is even a useful function for government. It was agreed that subsidy policies should be transparent and based on performance indicators. A good example of this was Korea where export credits were used as an

1. *Merger Cases in the Real World: A Study of Merger Control Procedures*, OECD, Paris, 1994.

incentive to firms to contest on export performance. In Sweden, government general subsidies are being phased out having been found not to be sustainable as international trade has increased. Another issue is the impact of indirect subsidies, which may take a number of forms -- for instance public procurement schemes which favour national companies. In brief, it was stressed that industrial policy itself should be based as far as possible on market mechanisms.

One of the questions raised was whether limitations on foreign ownership of industries (such as the financial industry) are justified to foster national self reliance. It was argued that foreign actors in the market may give better services which might otherwise exist. For instance, in Canada such restrictions existed on foreign bank entry until 1974, resulting in high cost commercial credit, which in turn contributed to undermining the competitiveness of domestic industry. OECD experience is that liberalization in this sector has contributed generally to the efficiency of the banking system. This appears to be backed up by studies in more recently industrialized countries.

Competition, Deregulation and Privatization

Mexico is an example of an economy in which competition policy was introduced as part of a programme of microeconomic reform. Trade liberalization began in 1986, with the accession to GATT and subsequently accelerated, resulting in the correction of relative prices and the reduction of price distortions. Price controls in the market were consequently reduced. Trade liberalization therefore had an important role in improving efficiency. However, this alone proved insufficient. One reason was that the service sector of the economy comprised 66 per cent of GDP, and was relatively isolated from the impact of imports. At the same time, it was exposed to control by certain strong interest groups. In the past six years, the government has pursued an aggressive deregulation programme to stimulate economic activity. and has commenced a program of privatization. Competition policy in this context can be very important to reinforcing structural change. The new law aims to enhance the self-regulating capacity of the market, although it is recognized that markets do not always function effectively and therefore may require some intervention. Efficiency is the primary aim of the law. Equity and fairness are not explicit goals but a more equitable distribution of income and better access to markets by smaller firms appears to be a by-product of the law.

It was not suggested that competition law of itself is sufficient to restructuring the economy especially where there has been no tradition of such policies. By the time a law is introduced markets may already reached a high levels of concentration there may have been a history of regulation which has enhanced the possibility of monopolization. Given the influence of other economic factors, Mexican law contains provisions which allow the competition authority to issue opinions on proposed legislation. The authority also works with government policy makers on the deregulation of significant and traditionally highly regulated industries, such as telecommunications and the financial sector. Any exclusions from competition law must be justified and are narrowly interpreted. In summary, the speaker's view was that, for economies who are newly adopting competition policy it is necessary to take a broad view of promoting the benefits of competition.

A rather different example was given from Chile, where there has been relatively little express interrelationship between deregulation, privatization and competition policy. There has been considerable privatization in Latin America over recent years particularly in the non-tradeable sectors. In most of these cases, little thought was given to market structure or competition. The driving force has largely been short-term fiscal gains. As a result, long term efficiency objectives were neglected. Chile's privatization programme, which commenced in the 1980s, illustrates this. The electricity company was privatized as a fully integrated body, which has made it difficult for new firms to enter the market, even the potentially competitive generation market, on account to the incumbent's entrenched monopoly The situation is similar in telecommunications. A recent attempt to correct this by opening up the long-distance segment to competition resulted in a 40 per cent-70 per cent drop in price.

The speaker argued that achieving long term efficiency in this sector is vital both from an equity perspective but also to ensure the competitiveness of the tradeable sector. Efficiently regulating monopolies is extremely difficult because of the asymmetry of information about those industries. There is also a risk of regulatory capture and neglect of consumer interests. The first goal has to be to get the structure of the industry right at the beginning. Where workable competition is possible it is preferable to regulation. Privatization should be used as a tool for improvement of competition. The most successful regulators will be those who ultimately eliminate the need for regulation.

It appears that this problem is not confined to Latin America. One commentator noted that in general, there was an inherent conflict between the desire to raise cash through privatization and using it as a vehicle to promote competition. In Italy, according to another speaker, similar debates over the objectives of privatization are occurring. The electricity industry is in the process of being privatized. There was a proposal that the electricity corporation should be sold as an integrated vertical monopoly and another that there should be an attempt to split up generation, transmission and distribution to improve the chances of competition at different levels of the industry. One possibility was to maintain the transmission network in public hands. Working in opposition to this idea is the fact that it is easier and more profitable to privatize the monopoly as a whole. It is recognized that breaking up the monopoly is difficult if one wishes to achieve an optimal competitive market structure. Another difficult issue is how to value the different parts of the company as separate entities.

With respect to regulation, Italy is looking to establish independent regulatory authorities (in particular for energy, telecommunications and transport). The aim is that they should be independent not only from the interests of the corporation but also from political influence. In the speaker's view the yardstick by which the success of such agencies should be judged is their ability to promote competition.

Under Italian and EU law, there is no automatic exemption from competition law for public utilities. These industries tend to comprise some activities which are essentially natural monopolies and others which are at least potentially competitive. In addition, the opening up of such activities to competitive performance is more likely to stimulate technical progress than regulation. There is a complementary role for both the regulatory bodies and for the competition authority in the treatment of these industries.

There was an interesting debate on the relative benefits of public and private ownership with one participant suggesting that privatization was not always an ideal solution to the problem of the utilities monopoly, since private companies would wish to operate the profitable parts of the industry and that in areas of less profitability consumers would be neglected. One answer to this is that where social responsibilities exist, there may need to be government subsidization but this should be transparent. It was also pointed out that technological progress continues to reduce the number of natural monopoly activities and thereby increases competitive opportunities. Moreover, even with public ownership, corporations do not necessarily act in the public interest. In conclusion, the consensus appeared to be that it was not so much government ownership but the degree of rivalry which was significant.

PANEL II

THE POLITICAL BACKGROUND TO THE ADOPTION OF A COMPETITION LAW AND ITS EFFECTIVE IMPLEMENTATION

Introduction

Having considered the reasons for having a competition policy, the debate then moved on to the political background to adopting competition legislation, including some of the practical problems of achieving sufficient consensus for the introduction of a competition law. A crucial part of this debate was what the optimal structure for a competition regime would be and what role and status the competition authority should have within government. It appeared from the discussions that achieving consensus for competition law requires the careful education and conditioning of the business community in addition to persuading politicians and getting the support of consumer groups.

It was generally recognized that the independence of the competition authority is an important component in establishing credibility but it is not always an easy task to achieve at the political level. Often political traditions play a role. In Sweden for instance, there is a long tradition of independent bodies so this was hardly an issue when the legislation was reviewed. In other jurisdictions this has been more difficult to achieve.

The need to condition the business environment - the Brazilian example

The Brazilian example was one of a long history of attempts, motivated by a variety of different factors, to develop a competition law -- none of which were effectively enforced. The source of the problem being not so much a failure to legislate but an absence of an overall competition policy orientation. An early attempt in 1945, was prompted by concern about the intrusion of foreign competitors. This law was later replaced by a constitutional prohibition against abuse of economic power. Criminal provisions were introduced but not used. In 1962, there was a further attempt to strengthen the law with an administrative enforcement and private action for damages. In 1964, conditions changed with a new regime, a new constitution and a strongly interventionist policy. Finally, in June of 1994 the latest law was introduced.

In spite of all this legislative activity, it is only recently that economic policies have ceased to impede competition by becoming less interventionist. Prior to this, concentration of industry was encouraged to promote development and industry was highly regulated. In fact, economic development was largely successful but long term protectionism helped to create a very oligopolistic market structure, and reduced competition with the result that some industries have performed badly. Price controls were maintained and foreign competitors kept out of the market.

Since 1990, the trend has been to deregulate and to expose markets to foreign competition. However, these initiatives were only slowly put into effect. Where privatizations have occurred they were generally motivated by a desire to reduce the country’s budget deficit rather than to promote competition. Regulatory capture has also been a problem. The Competition Authority does not have the power to intervene or comment on other types of regulation. The swell of interest in a more active competition policy

in Brazil appears to be coming from consumer groups who are demanding fairer prices and better quality goods. Public action has been taken against regulated industries and local authorities for providing poor and expensive services and there have been civil actions for damages for anticompetitive behaviour.

Probably because of the price control tradition there has been a certain lack of consistency in the investigations undertaken by the Secretariat of the Ministry of Justice. Most cases have concerned infringements of price regulatory rules or of anti-inflation measures. Far fewer have involved investigations into cartels. Cases which the investigatory body find warrant prosecution are sent to an adjudicatory Council which is an independent body subject to judicial review. In spite of staffing limitations, it has in recent years improved its credibility by virtue of the transparency of its decisions and being sensitive to the differences between regulatory issues (including price control) and anticompetitive practices. Following an amendment to the law in 1994, the Council has been empowered to approve or disapprove mergers and to review anticompetitive agreements. One criticism made of the Brazilian law was that the exceptions which exist in the law make enforcement very difficult.

Phasing in Competition Law in the Netherlands

Recently, the Netherlands has moved to strengthen its competition law. The legislation adopted in 1956 simply covers cartels and monopolies. There is no prohibition system. Anticompetitive agreements are considered on a case-by-case basis. An agreement which potentially affects competition must be registered with the Ministry of Economic Affairs who then considers whether there is any conflict with "the public interest". Following investigation, the Minister may decide to prohibit all or part of the agreement and may act against monopolies if their conduct is deemed contrary to the public interest. The law does not explicitly define the term "public interest". Decisions on competition policy are made by the Cabinet and there is no independent authority.

The background to the change was that, traditionally, the Dutch social and economic structure has been designed to achieve consensus between employers and workers and this objective is reflected in the law. By the 1980s, it was clear that the model was not working well in all respects. This was demonstrated by the disproportionate number of cartel cases before the EC Commission which originated in the Netherlands. In view of the changes occurring in the EC as a result of the Single Market Programme there was a review of domestic competition policy. The first phase was introduced using existing law with general prohibitions for certain types of practices subject to a provision for exemptions on a case-by-case basis. (e.g. in 1993 a general ban on price cartels came into force). The result so far has been that cartels are being increasingly dismantled. This has been a useful learning experience for both industry and the administrators.

A second phase, begun in 1993, was the drafting and introduction of new competition legislation based on a general prohibition system which will be consistent with the provisions in the EC Treaty. It is hoped that this will come into effect in 1997. There is much debate now on the costs both of private restrictions and government policies and excessive regulation. A new programme of deregulation has also commenced.

This sequence of phases, in the view of the speaker, had the effect of allowing time to break down resistance from concentrated opposition, to gain public support from the less well informed and unified beneficiaries and in general stimulate debate on the desirability of competition policy. Interestingly, competition policy was introduced prior to deregulation. Competition policy had the advantage of being known to business through EC law. There is however greater resistance to interference with public bodies. Nevertheless, the acceptance of competition policy has itself enhanced the acceptability of deregulation.

The motivation for change is not entirely clear but the most important element appears to be that macroeconomic solutions (such as cut-backs in the public sector, tax cuts, wage controls, etc.) proved insufficient to stimulate competition in the labour market and in the goods and services markets.

The need to educate the constituency and to consult - the Canadian example

The Canadian experience indicates how the adoption of a competition law may be stalled by the failure of government to recognize the need to build consensus. In fact, Canada had had an antitrust law since 1899 but this law was fairly limited. It reflected the particular concerns of a country which is geographically very large but has only a sparse population. The apparent dichotomy for Canadian competition policy makers was how on the one hand to favour large-sized national firms (which they believed were required to withstand competition from abroad - particularly the United States) while at the same time, introducing a competitive climate. The notion that large firms were required arose out of a concern to protect the small domestic market. This in itself illustrated a misunderstanding, firstly, that the domestic market was "a market" in every case (ignoring exports and imports) and, secondly, that firm size in all cases indicated the existence of economies of scale.

The early law was largely ineffective against monopoly abuses and anticompetitive mergers. Although anticompetitive acts hurt business as well as consumers (especially as the majority of transactions are in fact between business) the business community feared that any strengthening of competition law would reduce efficiency. The Government reviewed the law and in 1971 introduced a new bill which was designed to deal more effectively with anticompetitive practices. However, due to the failure of the government to consult or give notice this act was not passed until 1986! Business, the media and the legal profession condemned the Bill.

There were a number of factors which contributed to the stalling of the Bill. One was the political process and the way in which the Canadian cabinet functions. Resistance came from business, media and the legal community.The media was at the time a concentrated industry with multi-media ownership and the legal community too were not disinterested in maintaining the status quo. The primary problem was the failure by government to have advance discussion to try to reach a consensus among businesses which generally favoured the act. The Bill was criticized for a long time as being "too academic".

In 1986, the Act was finally passed as a result of a change in the political climate. The business community had begun to recognize that there were inefficiencies in the economy, negotiations for NAFTA had commenced and the government had finally engaged in a long process of consensus-building.

Where to look for support for competition law - the UK example

The Canadian example demonstrated the need for consensus-building but the question is who should one look to for support? A participant from the United Kingdom addressed the question of how to garner political support for competition law and some of the stumbling blocks which exist. In the political context, it was argued, it is insufficient to merely have a technocratic interest in competition law. It is necessary to have the backing of a political constituency. Generally, competition laws come into being because there is some strong motivation -- for instance concern about the behaviour of cartels. The three possible sources of interest are - consumers, labour and business. Although consumers benefit from such a law and could potentially represent such a constituency, in both the United Kingdom and elsewhere, consumers may be distracted from recognizing this fact, focusing instead on those laws which directly protect consumer interests. Trade unions similarly are more concerned with labour legislation. This leaves the business community which is often hostile to introduction. However, if a law is introduced, there is also the risk that it will be ineffective because it has been captured by business interests.

There are certain features of competition law generally favoured by business and not in any way damaging to the system. For instance, the guarantee of transparency in decision making by the publication of reports while ensuring confidentiality of business secrets. Other concessions to business may be more controversial. In the United Kingdom for example there is no system of fines because it was argued that fines might act as a deterrent to aggressively competitive behaviour. At the same time there is considerable flexibility in the law which allows the investigation of a wide variety of practices. The political environment is also important.

Where to look for support - the Italian example

The Italian experience reflected some of the issues discussed by the participant from the United Kingdom. Italy was relatively late in adopting competition law. Price controls were for a long time regarded as a means of controlling market power. In reality however, price controls were mainly used as a means of controlling inflation. Public ownership was also prevalent. Attempts in the 1950s to introduce competition law were scuttled by failure to agree on the scope of the legislation, in particular its application to publicly owned companies. As in the Netherlands, one of the motivating forces and an aid to its adoption, was consistency with EC Law.

As in the UK example, the three sectors of society which potentially may benefit from competition law are consumers, producers and organized labour. It is not always easy to convey this fact. Certainly, consumers are assisted because increased rivalry improves quality of goods, encourages innovation and lowers prices. Producers also may benefit but it takes a while for them to appreciate that such law is not only a sword against business but is also a shield against abusive behaviour. This is only effective where competition enforcement is transparent and when they have confidence in the confidentiality of the system.

In Italy, the competition authority has used its ability to comment on new legislation to forward competition arguments. What is currently being proposed is that in new legislation for regulated industries and privatized industries, there should be provision for the regulatory agency to have a statutory requirement to consult with the competition authority.

The "politicizing" of competition law - the US example

In the United States, the case made for competition policy at the political level was not that which an economist would argue but it nevertheless had a strong influence on the way antitrust law was perceived. At the time antitrust law was introduced, the political goal was to ensure small entrepreneurs could enter the market without being blocked by the abusive behaviour of the large trusts which existed at the end of the 19th Century and which exercised not only economic but also substantive political power. Early Supreme Court cases spoke of making sure that "small dealers and worthy men" could participate in the market. This ideology remains today in the perception that antitrust law will guarantee that someone with a good idea or something to sell will be able to enter the market without being squeezed out by the big players.

As far as the empirical evidence in support of competition law is concerned, it is difficult to measure the precise impact of competition law on markets but it is possible glean relevant information from the studies done in the deregulation of certain markets (such as the airline industry, the break up of AT&T, the background to the IBM case and comparative studies of those large industries which were broken up and those which were not). In addition, there are other comparative studies such as the OECD comparative study of the telecommunications industry and a similar report by the World Bank on the electricity industry.

PANEL III

SUBSTANTIVE PROVISIONS OF COMPETITION LAWS

Introduction

The purpose of this session was to compare different approaches to competition law. For instance, how broad the scope of the law should be, whether certain sectors or activities should be exempted and the different categories of violation which exist.

It was agreed that ideally competition law should apply to all sectors of the economy and to all economic agents, including government enterprises which are engaged in commercial activities. However, it was recognized that there are areas where co-operation may be preferable to competition. Examples of this include collective bargaining agreements on wages and other working conditions and sectoral exemptions, for example where insurance companies share risks (although not where they agree to set premiums). On the issue of territorial scope, one participant making a plea on behalf of business interests, pointed out that the territorial impact of the "effects doctrine" could mean that businesses were faced with a multiplicity of forms and investigations originating in different jurisdictions and that greater international harmonization of competition policy and processes was desirable.

There was also considerable discussion about whether it was preferable to base the law on a prohibition or abuse system. Practice varies considerably from country to country, although there were strong arguments expressed in favour of the prohibition system. Another topic raised was whether in most countries there was a clear distinction made between violations which were regarded as *per se* offences and those treated on a rule of reason basis. Some participants suggested that the distinction between the two was not as great as it first appeared since a certain amount of evidentiary proof was still necessary to establish a *per se* offence. Others argued for maintenance of the two categories and pointed out that the degree of severity between the types of offences was sufficient to warrant such a difference in treatment and that the evidentiary requirement was distinct.

Linked to this issue was a discussion on resale price maintenance (RPM). Many jurisdictions treat RPM as a *per se* offence. Most participants tended to support this approach but there was at least one who took the view that in some instances RPM may be justified and therefore supported a rule of reason approach.

There were also differing views on using an authorization or clearance system. Some participants believed that authorization procedures were a waste of resources and recommended a simple prohibition system leaving the onus on the parties to the agreement to determine whether or not their restrictions were anticompetitive. Others saw them as a useful monitoring tool. The most difficult issue was the criteria to be applied in making the assessment, in particular how to balance competition against other public interest considerations.

Finally, the question was raised as to whether merger control was desirable and if so, whether to use a mandatory pre-notification system or a voluntary system. Generally, it was agreed that merger control was useful as a preventative measure. One participant went so far as to suggest that decentralization of

economic power was necessary not only for the sake of economic efficiency but also for the sake of democratic political order.

United States - the underlying basis of competition law

The session began with a lead speaker from the United States who identified what she regarded as the three crucial principles of competition law, namely:

- the consumer welfare/economic efficiency basis of competition law;
- that competition law should protect the process of competition and not competitors; and
- the importance of analysing a particular restraint in the context of the prevailing market conditions.

The idea that the primary goal of competition policy is economic efficiency is one that has been reached after much debate in the history of American antitrust law. Historically, competition laws have been used to meet other objectives such as the protection of small businesses or concern for employment. The current view is that however important these goals may be, they are not the purpose of competition policy. It is preferable that such concerns be dealt with separately through other legislation. In order to have a coherent and predictable competition regime it is necessary for competition legislation to focus on the economic efficiency objective.

The protection of competition rather than competitors is a notion which permeated much of the case law. An example of a case where this issue arises is where a distributor complains that a manufacturer has unfairly terminated a distribution contract. The distributor alleges that the termination is an anticompetitive action. However, if in essence all the manufacturer has done is simply change distributors, the competitive structure of the market is unaffected and there is no role for antitrust law. Similarly, predatory pricing cases frequently turn out to be simply instances of highly competitive pricing. As another participant pointed out, this principle is one that has been developed over time.

The third principle is the importance of market analysis in determining a violation. This is an important concept in rule of reason analysis. Analysis of the market is necessary to determine whether a particular restraint is anticompetitive in effect and whether it is outweighed by efficiencies in the particular case.

The concept of "abuse" in Brazilian law

Brazil has recently amended its law in an attempt to strengthen its effectiveness. A Brazilian academic discussed briefly some of the particularities of Brazilian competition law and, in particular, spoke about the development of the legislative approach to the abuse of a dominant position.

Early legislation, adopted in 1962, defined, as offences, the abuse of a dominant position and certain restrictive practices which eliminate competition in the market, in whole or in part, by means of conventions, agreements or concentrations. The text of this statute listed practices which were deemed to be an abuse of economic power or a restriction on competition. The doctrinal writing and jurisprudence on the law tended to treat this list as definitive. There were no remedies for practices which fell outside the list. As a consequence, competition cases were fairly limited. The revised law of 1991 and its subsequent amendments modified this list so that the practices which are specified are given only as examples, thus widening the scope of the law.

Under the new law, there is only an abuse of economic power where there is actually an effect on the market. In the context of this law, the notion of "abuse" is similar to the notion of "excess". This means that even if a particular business practice would be legitimate in itself, it may amount to a breach of the law if as a result there is an anticompetitive impact on the market. However, the concept of "fault" in the case of abuse is not the classical concept but the modern concept of "social fault". The notion of abuse of economic power in Brazil is different from the notion of a "tort". So that under Brazilian law an abuse can be a *per se* breach of the law. We remove from notion of abuse all moral elements and take into account only the effects of the abuse. There is a constitutional presumption which deems the domination of markets, restriction of competition and the arbitrary increase of profits to be a misappropriation of the exercise of economic power.

Why adopt a prohibition-based system? A view from Sweden

When Sweden recently changed its law it was decided to transfer from an abuse based system to a prohibition system. This was seen as one means of strengthening competition in the face of a decline in economic growth. A Parliamentary Commission was established to consider what changes were necessary. It concluded that in spite of Sweden's economy being open to international trade there remained a severe lack of competition in many sectors of the economy.

Why choose a prohibition system? In practice the abuse system meant that the full burden of proof to establish that a particular agreement or concerted practice had negative consequences and harmed the public interest rested with the competition authority. Few cases ever reached the court and those that did were seldom won by the authority. As a result, competition law did not gain the respect of the business community. Rather than risk difficult court cases, the competition authority chose to try and negotiate with businesses to remove restraints. The problem with this was a lack of transparency, coherence and therefore legal certainty. Another reason for choosing a prohibition system was its familiarity for those companies exporting to the EC and United States.

What should be the formulation and scope of such prohibitions? Most jurisdictions have prohibitions on horizontal restraints such as price-fixing, market-sharing, bid-rigging and limitations on production. Vertical restraints on the other hand tend to be treated on a rule of reason basis. In some systems there is a *per se* prohibition for certain pernicious behaviour which means effectively that the only proof required is of the existence of such behaviour. In Swedish law however, there is a requirement that the anticompetitive restraint must have an appreciable effect on competition. There are thresholds (in terms of market share and turnover) which have to be met. This effectively exempts certain behaviour where the parties are small and medium-sized businesses, which do not have the economic power to adversely affect market conditions. The correct level for these thresholds is a matter for debate, as is the question whether a distinction should be made between severe and minor infringements. With respect to vertical restraints, the approach in Sweden is to be less lenient than is the case in some other jurisdictions because local markets tend to be highly concentrated so the risk of market foreclosure is higher.

In answer to a question regarding the structural analysis of markets in cases of alleged abuse of a dominant position, it was explained that under Swedish law a concentrated market structure was not of itself conclusive of dominance but rather a litmus test of where dominance might be found. In any even, it is the *abuse* of a dominant position which is at issue not simply having a dominant position.

Treatment of competition violations under the new Mexican law

Under the new Mexican competition law, all economic agents are subject to the law. The concept of "economic agent" is not defined in the law but will have to be refined through practice. There do exist some exceptions to this general rule, principally in relation to certain strategic sectors which have been

constitutionally reserved to the State. The law does however apply even in these sectors to those economic acts that are not an integral part of the strategic activities. Associations of workers are also exempted but only with regard to the protection of labour interests. In addition to its enforcement functions, the competition authority also issues opinions on government activity having an impact on competition, including legislation and administrative acts.

Like many other jurisdictions, Mexico has a prohibition system. The distinction made in the law is between "absolute" monopolistic practices and "relative" monopolistic practices. Absolute monopolistic practices, are essentially horizontal restraints (e.g. price fixing) and are regarded as *per se* offences. The majority of cases are treated as relative monopolistic practices and these are largely vertical restraints. The test for anticompetitive effect requires an analysis of the impact on the market and proof of the market power of the perpetrator(s). Finally, consideration must be given to whether there are positive effects on the market which outweigh the impact of the restrictions. With respect to mergers, a preventative approach is taken requiring mandatory prior notification of mergers above a certain threshold. The aim is to avoid undue concentration of market power. The competition authority is required to respond to a merger notification within a specific time period. Failure to take action within that period will result in automatic clearance of the merger. Provision is made for penalties to be imposed for breaches of the law and additional penalties may be imposed according to the degree of damage to competitors.

Dealing with large business conglomerates and cross-shareholdings in Korea

The Korean competition law was enacted in 1980. It was drafted with reference to the law of other market economies such as the United States, Germany and Japan but contains some provisions designed particularly to deal with local problems. One particular problem was that the price mechanism system pre-supposes a certain degree of pre-existing competition. However, when the law was introduced, most domestic markets were highly concentrated and the main political preoccupation was to ensure that prices were stabilized. As a result, the legislation was drafted with provisions aimed at preventing dominant firms from imposing unreasonably high prices. The other issue was how to address the problem of the large Korean business conglomerates. Should they be broken up -or regulated in some way? In the end, the legislation was drafted with provisions intended to prevent excessive concentration of power and these provisions have been strengthened subsequently.

The question of cross-share holdings between conglomerate corporations in the Korean context raised a more general question during discussion about whether in general there should be provision in competition legislation which would allow an authority to examine the acquisition of minority shares in competing companies. Interlocking directorships in competing companies are disallowed in many jurisdictions. In addition, some jurisdictions provide for investigation of minority share acquisitions within a set time period. It is of course a matter of judgement what level of share ownership will allow the holder strategic influence over the decisions of a competitor.

In Korea, the distinction between *per se* offences and rule of reason is clear. In theory at least, abuse of market dominance and resale price maintenance are *per se* offences while other unfair practices are treated on a rule of reason basis. In practice things are different. Certain types of cartels for instance have to authorized by the Commission so those which are not authorized are deemed to breach the law.

As far as the scope of competition law is concerned, the law does contain exemptions for the agriculture, fishing and mining sectors. In addition, there is a broad exemption for any act which is justified by other laws or regulations. In practice, the dividing line for what is exempted is somewhat blurred. Lately, this issue has become tied into the debate on privatization and deregulation. The interaction between industrial and competition policies has evolved with the changing structure of the economy and in the view of the speaker, a wise government would be one which optimizes this interaction to further accelerate

development. Part of this strategy should be to apply competition law increasingly to the regulated sectors and to constrain the exemptions.

German Competition Law

Germany has had an active competition law for some time. Its underlying principles are not dissimilar to US law although the text of the law is very different. In addition, one of the express objectives of German law is to ensure competitive structures in the economy. It is considered that for the sake of coherence and non-discrimination, competition law should be applied to all sectors of the economy. The definition of "enterprise" in German law is broad enough to cover publicly owned enterprises and government activities which impact on production or distribution. This can be particularly significant with regard to public procurement. Even in these nominally "exempted" sectors, it was argued, there should be at least a complementary role for competition law (for instance in cases of abuse of market power). The speaker also supported the use of the "effects doctrine" with regard to the extraterritorial scope of legislation as necessary to the proper enforcement of the law.

The speaker also supported the prohibition principle, including outright prohibition for practices such as bid-rigging, collusive tendering, market-sharing, quota cartels. In German law the rule of reason approach is used to analyse other types of horizontal and vertical restraints. This participant did not agree with the view that there should be an automatic exemption for restrictions contained in agreements between small and medium-sized firms, but rather that these should be considered in their market context.

In Germany, competition offences are treated as civil offences and there are no criminal proceedings as in jurisdictions such as the United States. Private actions are possible. With regard to fines, the speaker emphasized the need to create disincentives to abuse. As an example, a comparison was given between the fines imposed by the EC Commission on cement producers which amounted to 240m ECU ($300m) across 33 producers. This meant that the German market leader was fined approximately $20 million compared with fine imposed by the German competition authority which was about four times that amount.

During the discussion there was a debate on the issue of whether "conscious parallelism" in oligopolistic markets should be treated as an offence. One participant argued that it should not, since the element of intent is missing. It was noted that in German law however such cases are covered. The rationale being that to exclude such cases for lack of clear intent could result in a loophole in the law and that efficiency in markets should not be sacrificed to certainty.

Competition Law cannot be an island - a view of Spanish Competition Law

One lead speaker expressed the view that however excellent a competition law may be, unless it is properly enforced, it is useless. Where there is no political commitment, few fines imposed and a lack of clarity about the role of the competition authority, the law will be completely ineffective. Competition law should not be an island in the sea of other legislation. The notion of free competition should permeate all other laws. If competition law is isolated it will fail. In this regard, regional arrangements such as the Treaty of European Union can also be very important.

Spanish law combines a prohibition system with provision for authorization. The reason why there is no application of the rule of reason analysis is that Spanish law is based on Roman law which requires proof of culpability. Therefore, it was regarded as inappropriate to allow discretion to the authority since it was thought to lead to legal uncertainty. In fact, the authorization system attains much the same ends but is more expensive and it is debatable whether it provides any greater legal certainty. An argument sometimes made against the authorization system is that it can tend to turn the competition authority into something resembling a regulatory agency rather than an enforcement agency.

In Spanish law, provisions relating to abuse of a dominant position are regarded as especially important as they are the often the only means to intervene in legal monopolies where deregulation has not taken place. With respect to the regulation of mergers, Spain has a system of voluntary prenotification which in the speaker's view is valuable but might be improved by being a mandatory system. One particularly useful addition to Spanish competition law are the provisions which exist on state aids.

One of the issues raised was whether the law should refer to criteria other than economic efficiency objectives. The view expressed by one speaker was that in jurisdictions where competition law has a longer history and is a generally pervasive principle, it may be preferable to have such criteria in separate legislation. However in other cases, it may be preferable to have them in the competition legislation where, if they are applied at all, they are applied by the competition authorities. It was also recommended that generalized provisions against "unfair" competition should be, if possible, avoided since they do tend to contradict provisions designed to promote competition.

PANEL IV

EFFECTIVELY ENFORCING COMPETITION LAW

Introduction

The focus of the final session was on the problems of enforcing competition laws. In particular, the nature and functions of the various institutions involved and their position within government, procedural aspects, detection of anticompetitive behaviour, decision making and sanctions.

The main theme of discussion was that it is not possible to judge the effectiveness of competition law simply by considering its text. It is the extent to which it is enforced, the types of procedures which are used and the vigour of enforcement which determine its effectiveness. Examples from different economies showed a variety of experience and highlighted certain common themes, notably the need for transparency, confidentiality and independence of decision making. It was emphasized that not only should the law itself be transparent but also the behaviour of the authority should be clear, consistent and predictable. A clear separation of the functions of investigation and adjudication was thought necessary, whether both functions were performed by a single body or by different bodies. Another important part of transparency was the publication of cases and proceedings of the competition authority.

Effective Enforcement

What is meant by "effectiveness" of enforcement? One measurement is the extent to which the competition policy regime acts as a deterrent to anticompetitive behaviour. It is not possible for the system to consider every possible agreement or conduct so the extent that businesses consciously take into account competition rules in planning their business transactions is important. A question related to deterrence is how reliably breaches are detected, prosecuted and, for serious violations, severely punished. Accordingly, the enforcement agencies need to have the necessary powers to acquire evidence to verify compliance and to satisfy the administrative or judicial tribunal which makes the final determination of violation. Another factor is the extent to which the enforcement agency is able to act without being constrained or unduly influenced by factors which are inconsistent with the fundamental consumer welfare-enhancing objectives of competition policy.

It was also pointed out that recourse to the competition authority must be easy. There are a variety of means by which this is done. In most jurisdictions there is provision both for the authority to take cases on its own initiative and also in response to a complaint by an individual or group. For instance, in Canadian law, there is a provision that any six residents can make a complaint to the Director and the Director must make some sort of response.

Institutions

There was a lively debate on the number and type of institutions which should be established for enforcement. There were mixed views on whether there needs to be separate institutional bodies for investigation, prosecution and decision making. It was agreed that the system had to contain checks and balances which would guarantee due process and protect the rights of defence. However, there appeared to be several models by which this could be accomplished. For example, one model was to have a totally integrated body whose decisions then may submitted to a court on appeal. An alternative system involved a body which prepared action for prosecution in the normal court system.

This led to a discussion on whether, given the economic analysis involved in adjudicating competition cases, it was necessary or at least preferable to refer them to a specialized tribunal or whether the normal court system was competent to deal with such cases. In the United States for instance, it is the courts of general jurisdiction which hear antitrust cases. In support of this system, it was argued that competition law is not alone in requiring a degree of economic or other specialist knowledge. As the judiciary becomes better acquainted with hearing such cases their level of knowledge will increase. In the US system, antitrust matters even go to jury trial. One participant explained that expert testimony on competition matters as in other matters often comes down to the credibility of the witness concerned. Juries although inexperienced in technical areas may nevertheless be able to assess the credibility of witnesses and whether the facts presented support the testimony presented. This system appears to have worked well in the States where there is a high level of private enforcement.

In contrast, Canada has a specialized tribunal which was chosen in order to provide the flexibility of having non-jurists on the tribunal. One of the concerns that underpinned this decision was that, even if judges could be educated to deal with economic issues over time, there would be a danger during the transitional period of bad decisions resulting in unfortunate precedents being set. This perhaps reflects the fact that antitrust matters have not had such a high public profile in Canada compared to the United States. It was recommended that where a specialized tribunal is established it should not necessarily be restricted to a set number of people. Instead one could have a roster with some permanent members and others who can be added so that the number of people hearing a case can vary with the complexity of the case and the nature of the problem adjudicated.

In Sweden, a compromise solution was sought. When decisions have been made by the competition authority, cases may be appealed to the Court of First Instance in Stockholm which has a special section advised by economic experts. At the next level, the Court of Appeal has a particular section specialized in competition law and consumer issues.

In France, the problem of educating judges in economic analysis is partly solved by the fact that some advisors in the competition authority are magistrates who, after their term expires, return to the general judicial system, bringing with them the expertise and analytical tools acquired. As a result, the judiciary is becoming increasingly well informed on competition matters. However, without a lively system of private action the process of education both of judiciary and the legal community is likely to be somewhat limited.

Different levels of enforcement - the US example

The first of the country examples discussed was the US system, in which there is a spectrum of enforcement mechanisms. At the federal level, there are two enforcement agencies - the Antitrust Division of the Department of Justice (DoJ) and the Federal Trade Commission (FTC). The existence of two bodies with overlapping functions is largely a result of historical factors. At the state level, there is enforcement both of state anti-trust law and in some cases, federal antitrust law. A significant feature of the law is the ability of private parties who have been injured as a result of violations of the law to bring suits themselves

either for injunctive relief or damages (in the US treble damages are available). There is also the possibility of class actions and other devices designed to facilitate and encourage private actions. The availability and use of private actions is considered to be a key component of the deterrent effect of the law and is not conditional on any government action having taken place. However, in cases where the DoJ has taken a successful case against a firm, a party bringing a private case against that firm on the same facts need only prove injury and not the violation itself. Private actions are not common to all jurisdictions. Different jurisdictions use different types of enforcement solutions which generally reflect the type of legal culture and traditions which exist.

In the United States, there is a variety of different types of cases which may be brought. For instance, in addition to private actions for damages, public criminal cases are brought for serious *per se* violations of the law such as price fixing, bid rigging and market division. The fines for such violations are heavy and may amount to as much as $ ten million for a corporation and jail sentences of up to three years for individuals. The risk of individual liability is regarded as a very effective deterrent. In addition, government agencies can sue for injunctive relief in the Federal Courts. There is also a pre-notification system for mergers. There is an increasingly active civil enforcement system for rule of reason cases, where injunctive relief is the norm. The factors which are taken into account in deciding enforcement priorities include the economic impact, the deterrent effect of the case, its value as a precedent and what enforcement alternatives there are.

Finally at the international level, co-operation in antitrust cases is becoming increasingly important as investigations frequently involve international markets requiring the acquisition of evidence from abroad and the need to co-operate with counterparts abroad. This is an area in which there is expected to be much further work in the future.

The Internal Organization of the Competition Authority - the Finnish example

One of the factors which can affect the quality of investigation is the internal organizational arrangements within the competition authority. There is no one "right" model and countries with a history of enforcement have generally, through trial and error found a solution which is satisfactory to them. The lead speaker from Finland described as an example, the development of the current arrangements in the Finnish Office of Free Competition.

Up until 1988, Finland followed the Swedish model of enforcement which at that time had two authorities with divided responsibilities. The arrangement proved unsatisfactory for a number of reasons both in Finland and in Sweden (where it has also subsequently been changed). When in 1988, the new Office of Free Competition was established, the assumption was that the investigatory staff would be split into teams according to market sectors, following the model used in a number of other jurisdictions. However, this model proved unworkable given the lack of specialist sectoral expertise which would make this type of arrangement useful. In addition, there were concerns that the arrangement would lead to market capture. In 1992, when the competition law was overhauled, replacing the former abuse-based system with a prohibition system, there was an accompanying reorganization of the Office.

The Office is now an independent investigatory body with 50 staff, considering about 350 cases per year. Once investigations are completed they go to the Competition Council for adjudication. Priority is given to cases which affect foreign trade either through imports or exports. Investigations are organized in terms of types of restriction -- horizontal, vertical, market dominance and government regulations. The drawback of this arrangement is the possibility of overlapping investigations into cases involving several different types of offence requires a certain amount of co-ordination between investigating teams between them and the companies concerned. On the whole however, the Offices believe that the benefits outweigh this disadvantages. Although there are some features which only exist in relation to a particular product or service markets, there are considerable similarities in the types of problems which arise across the board.

This makes it easier to cross-refer a particular case with other similar cases both in the domestic jurisdiction and those in other EEA jurisdictions. The Office apples a "one-stop-shop" principle to investigations which means that the same case officers deal with the matter from beginning to end.

The establishment of a new competition authority in Taiwan

The Taiwanese competition law came into force in 1992, in the context of considerable social and economic changes including a trade liberalization and globalisation policy. The objectives of the law are to protect consumer rights while ensuring fair competition and the promotion of economic stability and prosperity. The Fair Trade Commission (FTC) is responsible both for policy formulation and for the investigation and disposal of cases. The system provides for both administrative and judicial enforcement of the law. Where violations occur, the FTC requires companies to rectify unlawful behaviour within a specified time limit. In the event of a failure to meet this requirement, the FTC can levy fines until the violation ceases. The Courts have jurisdiction over matters such as monopolization, unlawful collusion and breaches of certain intellectual property rights and may in appropriate circumstances impose prison sentences and levy fines.

In their approach to concerted practices, the FTC have taken the view that certain types of collaboration are not anti-competitive and in some cases do contribute to market stabilization. The government has therefore granted exemptions to some price quoting behaviour by certain small and medium sized enterprises. In recent years, the government has increased public construction resulting in expanded public purchasing. Unfair trade practices which might affect demand side competition are subject to review by the FTC. The FTC has a duty to publish a list of those companies deemed to have market power - i.e. those which control at least 20 per cent of the market. The FTC has established a special industrial market group to investigate such enterprises. There is also considerable debate going on concerning the application of the competition law to certain government regulated sectors.

Since 1992, the FTC has conducted a considerable number of investigations including those into government regulated sectors with signs of improvement in price competition. Given the increasing predominance of trans-national transactions their significance to the economy, the FTC give some priority to these cases, giving them particular care and expeditious treatment.

Enforcing competition law by stages - the Korean experience

Like most other developing countries, Korea is experiencing drastic changes in terms of size of the economy, its structure and market behaviour. In response to these changes, competition law has been introduced and enforcement developed and strengthened in stages. In the view of one participant, this gradual approach may be a viable alternative to the introduction of a full-scale competition law by countries with similar development experiences.

According to an UNCTAD report on competition policy, the process of introducing a competition law can be divided into a number of stages. Three different types of technical assistance are provided according to the stage of development. At an early stage, it is necessary to provide introductory seminars bringing together experts with the aim of sensitizing the government to the need to introduce competition legislation. Once the government has been persuaded to introduce legislation the next step is to provide advisory services to assist in drafting the legislation. The third step is to provide advice on the establishment of an enforcement authority and train officials responsible for implementing the law. The Korean enforcement authority has worked to implement these steps.

The first competition law introduced in Korea was "The Price Stabilization and Fair Trade Act 1976", which was in fact primarily designed to regulate prices rather than encourage competition. It

controlled only a limited type of practices and was enforced by a small staff. It nevertheless proved the starting point of the current competition regime. The small Fair Trade Section which was established within the Ministry carried all three types of technical assistance, described above -- by making the public more aware of the role of competition legislation, by conducting studies and through public relations activities. The Section also drafted new legislation - the "Monopoly Regulation and Fair Trade Act" adopted in 1980. At the same time, a new enforcement authority - the Fair Trade Commission was established. The role of this agency was further strengthened by an amendment in 1990, which gave the authority an independent role and empowered it to make determinations on competition cases. Since then there have been other amendments to the law, expansion of resources and a developing independence of decision making.

There are seven Commissioners at the FTC. To ensure the quality of enforcement there are particular requirements which any Commissioner must fulfil. For instance, he or she must have either have had at least 15 years' experience as a judge, or as a professor or in consumer protection advocacy. To ensure independence of decision, once appointed, the Commissioner cannot be arbitrarily removed during his or her term of office. The Commission takes independent decisions but is nevertheless accountable to the Minister of the Economy, and this provides one of the mechanisms for co-ordinating competition with other economic policies. In addition to enforcing competition law, the FTC also has a broader mandate to comment on other government regulation. Enforcement is accomplished through both administrative and judicial means. The FTC investigates possible breaches and complaints referred to it and takes corrective measures which are subject to judicial review. The FTC can refer cases to the Court which could result in criminal sanctions involving fines or imprisonment. Civil actions for damages may only be taken after administrative action undertaken by the FTC.

With respect to international co-operation, there have been few cases where the FTC has found the need to co-ordinate with other authorities but given the increasing globalisation of markets it has sought to strengthen relations with other authorities and relevant international organizations.

Enforcement in France

A lead speaker from France talked about several issues relating to enforcement of the French competition law, introduced in 1986. One of the issues to be decided with the introduction of this legislation was the form of sanctions to be imposed. In the French legal system there is the option of adopting penal and/or administrative sanctions. The conclusion reached was that in general it was more appropriate to apply administrative sanctions. There were two reasons for this. The first was that penal procedures are somewhat long and while they certainly provide effective protection of the rights of defence they are somewhat cumbersome and inappropriate used in the context of most economic violations. The second reason was that decisions in competition cases require analysis both from an economic and from a legal perspective. In France, most criminal judges do not have training in economic analysis. Therefore, it was considered that administrative proceedings would be more appropriate. The one exception to this is that penal sanctions can be used to complement administrative sanctions in cases where the failure by a company to comply with competition law can be primarily attributed to the actions of a specific individual or individuals.

The next issue discussed was the independence of the Competition Council. Up until 1986, all competition cases had to be referred for investigation by the Minister of the Economy. However, this system had certain disadvantages, in particular because any action of the Minister might be imputed to have political motivations. Therefore in 1986, the system was changed. The Competition Council was created comprising a number of judges, lawyers and prominent economists. The independence of the Council is assured through a number of mechanisms. It has been established by a specific statute setting the conditions of its membership and operation and matters can be referred to it for consideration by a wide range of people including -- businesses, professional organizations, trade unions and local authorities. The Council can conduct investigations into complaints and by its own initiative and has the power to set penalties.

Procedures before the Council are adversarial and this is seen to assist in protecting the rights of defence. Complaints may be made to the Council by businesses or by the Minister. Decisions by the Council must set out the reasons for decision in detail and may be appealed to the Paris Court of Appeal. Finally, the Competition Council may give advice to the government by request and can co-operation with foreign authorities for cooperation on specific cases and to improve procedures.

SUMMING-UP

Mr F. Jenny
Chairman of the OECD Committee on Competition Law and Policy

I will try and summarize what was said during the workshop. We raised a lot of very important questions about competition policy, the way it should be set up, the rationale for it and the way it should be enforced. We have perhaps provided a few answers. We also had a few laughs and thoughtful comments and images and a very lively discussion on the issues raised. I think this was the perfect formula for what I consider to be a successful workshop and quite an achievement for a first workshop of this type. Rather than an official summary, let me just give you a summary of my own impressions.

The first major question addressed was why we were having this meeting. In other words, why is the question of competition policy in dynamic non-member economies (DNMEs) relevant and why should we devote a workshop to this issue? This question was really inspired by the fact that a number of the DNMEs who have achieved dynamic growth in their economies do not have a competition law. What therefore is the need for competition law in these countries? This issue is raised particularly in view of the fact that most of these countries have an open economy -- at least in the sense of having strong export industries. Without going through all the examples, it is quite obvious that a lot of countries have achieved impressive levels of development without recourse to competition law.

Mr. Khemani and others tried to answer this basic question by explaining that what is crucial in the first instance to development is not so much competition policy (although we will return to issue of competition policy) but firm rivalry. When one looks at the development of some of the DNMEs represented at the workshop, it is quite obvious that the efficient sectors tend to be export sectors where firm rivalry is very extensive. The same theme was taken up by Charles Oman who added that firm rivalry not only has static but also dynamic implications which are important to development. We therefore at the end of this session came back to a revised notion of the question -- that is -- if firm rivalry is essential to development is it necessary to have a competition law and policy or is an open economy sufficient?

The answer given by various participants was that it is in fact often very difficult to have an open economy in the first place if one does not have a domestic competition policy. With respect to the role that it plays, one participant suggested that one useful role is to "keep other branches of the government honest!" In other words, to prevent them from being captured by private interests. This may be particularly important where international trade cannot do the job, such as the case with non-tradeable goods or where government might be tempted to erect barriers to protect local producers, or simply because a nation with a well thought-out competition policy may be better placed to discuss problems of global competition with the governments or competition authorities of other nations.

Ms. Widegren offered evidence from the Swedish experience about the way in which attempts to build up national monopolies or a concentrated domestic industry in the age of the global economy could be, if not self-defeating -- at least an elusive quest. Mr. Van Gent, taking the example of the Netherlands, demonstrated that in spite of the fact that the Netherlands was an open economy, lack of competition policy had contributed to widespread cartels and that reforms were currently being put in place to try and remedy

this. Canada was also given as an example of a small economy in which competition policy had contributed to economic development.

An interesting exchange of experience occurred between participants from Malaysia and Thailand on the issue of the legitimacy of competition policy in a developing economy with respect to the banking sector. On one hand there was the view that national banks should be protected or at least that foreign banks should be constrained from having significant market power so that they would not reap all the benefits of domestic demand. Whereas, the alternative position was that insufficient competition and lack of openness in the local banking sector might lead to abusively high interest rates and financial costs which would be detrimental both to businesses and other consumers.

From these discussions emerged the idea that one of the very useful roles for competition authorities is to keep an eye on the rest of government, including intervening in sectors of the economy which are typically regulated by governments. Industrial policy may be justified in certain cases but it should be open to review. Competition law is, among other things, a countervailing power to the possibility of regulatory capture.

The advocacy role of competition authorities was a constant theme during the debate. A number of countries have introduced specific provisions in their competition laws to ensure that such advocacy is a statutory right and not simply an ad hoc arrangement. For countries contemplating new legislation, it appears that one of the suggestions which came out of the meeting was to consider the inclusion of such a statutory provision.

After this, the discussion shifted from the desirability of competition policy to its substantive effect. In this context, we turned to privatization and deregulation as a pre-condition to an effective competition law. There was a lively discussion on the merits or otherwise of public versus private firms, in which Mr. Valentino expressed the feeling that it is unwise to be too dogmatic on the issue. On the question of whether to adapt industry structure to ensure that competition law could do its work, there seemed to be agreement on several points. Firstly, that privatization is not a panacea and that one should not rely on it exclusively. Secondly, that the substitution of private monopolies for public monopolies is not the answer since it may create as many problems as it solves. Thirdly, what is of paramount importance in privatization is to establish structural competition, or as Mr. Khemani put it to organize the conditions for rivalry among firms. On this point, an example was given from Chile about the difficulties one faces if such conditions are not established prior to privatization of a monopoly. As several speakers mentioned, this is not an easy task since selling a monopoly intact makes the firm more attractive to private investors and there may be fierce resistance to its being dismantled.

To sum up the argument to this point, if one accepts that there is a need for competition policy and assuming that some sort of competition law is desirable to assist in its implementation, the next question to be tackled is how to create the political momentum for the adoption of such a law. We heard of various experiences, including those in Canada and the United Kingdom, where there were long delays in the adoption of relevant competition laws because there was no support from the constituencies where one might expect to find it. Sometimes there may be little interest on the part of consumers and little understanding of the issue by businesses.

What was clear from discussions was that it is necessary to build a consensus and that this has to be built through discussion and negotiation. This is something which was criticized as lacking in the Canadian experience, for example. One participant also pointed out that for competition law to be respected once implemented there needed to be a build-up of consensus beforehand. As an economist I would say that competition is a public good, everybody desires it but nobody wants to pay for it. That's the problem of establishing a competition law!

There is therefore, a need to consult with all types of interest groups, in particular business, labour, consumers, in order to ensure that their views are reflected in the legislation or at least taken into account. During later discussion on enforcement, for example, attention was called to the fact that the rights of defendants needed to be taken into consideration. This is one example of a provision which would enhance the acceptability and ultimately the likelihood of adoption of such a law.

Another point which was raised was that pressure in favour of competition law may arise out of economic circumstances, such as the desire to become more competitive at the international level, or the need to harmonize law in the context of entering into an international free trade agreement with partners which have competition law. The experience of Mexico was given as an example of where this occurred.

One of the points which were raised was that in many countries competition laws have developed gradually over time without the sudden introduction of a fully-fledged law. Some participants pointed to the value of this in terms of building consensus.

So, whether the pressure for competition law arises as a result of external pressure or through consensus the next stage that we reached in our deliberation was, assuming one is going to adopt a competition law, what would be the substantive provisions of this law?

We had a very interesting discussion on the question of substantive provisions. This was led off by a participant from the United States who suggested that there were three principles on which competition policy should be based, namely: that competition law should be geared toward maximizing consumer welfare; that it should be designed to protect competition and not competitors; and, finally, that competition law should allow for sophisticated analysis of markets.

One particularly interesting question which was discussed was whether or not exemptions should be written into competition law or should be the result of sector specific legislation, outside the ambit of competition law. Different solutions to this problem were proposed. One proposal was for a pure competition law with no exemptions written into the law. Mr. Fernandez-Ordonnez, expressed the view that from his experience in Spain, the fact that the legislation ensured that the competition authority had an automatic say in what was to be exempted actually helped limit the number of exemptions since they had control over the way the law was interpreted. This example seemed to suggest that perhaps exemptions should be explicitly the responsibility of the competition authority and therefore written into the competition law.

There was also a very interesting discussion on the legal underpinning of competition law. More precisely, whether or not competition law should be based on a prohibition system or a faults based system. This debate is particularly familiar to Latin countries (including France) but may be less relevant to Anglo-Saxon countries which have a different legal tradition. It appeared that the majority of participants believed a prohibition system was preferable, perhaps because it is easier to enforce and would lead to more legal certainty, thereby being more efficient in the economic sense.

This discussion led us inevitably to the issue of what type of prohibition should exist for what type of practices. Should there be "per se" prohibitions or "rule-of-reason" prohibitions? There were distinctions drawn between naked anti-competitive behaviour, justifying a per se approach and other behaviour, particularly in the context of a vertical relationship, which may or may not be anti-competitive and which has to be considered within the context of prevailing market conditions.

One of the important issues addressed was whether there is a universal model of competition law which could be applied in all DNMEs. The answer was basically that there is no universal model but there may be universal principles which could be applied. One astute comment made was that competition law should not be an island in the set of national laws. In other words, competition law has to be related in each country to the legal framework and particular economic climate of that country.

There was quite a lot of agreement on some of the general principles discussed. One was that competition law should be based on the concept of efficiency. Also, as I mentioned earlier, competition policy should be based on a prohibition system and that it probably should draw a distinction between the treatment of naked horizontal restraints and other anti-competitive practices. There should be a wide definition of the economic agents which are subject to competition law and that the definition should include publicly owned enterprises and professions, including lawyers! Merger control was also seen as necessary because of the preventative role it can play in maintaining competitive market structures. It is also desirable for there to be provision in the law allowing the competition authority to have an advocacy role within government. One interesting comment by a participant (but which was not discussed generally) was the suggestion that competition law should contain provisions relating to state aids, since this may be a factor in preventing the harmonious development of competition.

It was also mentioned that there were guidelines on the establishment of competition laws which might be useful in the work done within the OECD and UNCTAD.

One of the things that competition law should provide for is transparency in enforcement by the competition agency. Moreover, the agency should be insulated as far as possible from political pressure and be accountable through judicial review of its decisions. One participant pointed out the usefulness of the publication of annual reports on the competition agency's activities as an important method of ensuring transparency and accountability. Another stressed the need for a broad public information campaign so that the purpose and activities of the agency would be well understood.

Finally, as regards sectoral coverage, participants generally felt that competition law had to be broadly applied to all sectors to be effective. However, as we are aware, the dictates of other regulations and policies, such as agriculture, transportation, energy, telecommunication often lead to provisions which exempt these sectors from the full force of competition. It appears relatively rare, however, that entire sectors are excluded from the application of competition law. There is usually at least a residual role for competition law even in "excluded" sectors and in addition the competition agency will often have the means of putting forward the competition perspective to the regulators of these industries and thereby have an influence on the final decision.

The last subject of discussion was the question of effective enforcement. It was repeatedly stated that no matter how good the competition is, the issue of enforcement is crucial. It also was clear that there are different models for enforcement of competition law. There was debate over whether it is necessary to have a specialized judicial tribunal or use the normal court review system on competition matters. The key question was whether the economic analysis which is required to make an assessment in a competition case was a sufficient reason to exclude competition enforcement from the regular court system. There were a lot of differing views on this issue.

On a personal note, I think firstly, that we tended to emphasize differences in the institutional setting and I think that those differences are not necessarily as great as they appear. Secondly, the institutions which are established, cannot be completely divorced from the general legal background of a particular country. It is therefore to be expected that there should be some differences among countries relating to the fact that they have different legal systems. The enforcement apparatus of competition law should, at least to some extent, relate to and be consistent with the broader legal context.

One could not leave an international workshop like this without mentioning the internationalization of competition policy. We are all aware, in the wake of the Uruguay Round, that there is a proposal to bring competition policy firmly within the framework of international negotiation, notably within the WTO. We have discussed some of the possible approaches to dealing with anti-competitive behaviour which extend beyond the frontiers of one country. All we can really say at the moment is that there is a growing feeling that existing international arrangements for cooperation in competition need to be strengthened to

meet the challenges of globalisation. Certainly, a lot more work needs to be done to identify the problems associated with the extension of existing international machinery in the competition policy area.

Finally I should just like to say that although we have not been able to deal in-depth with all of the competition policy issues raised over these last two days, I still think that this workshop has been of great value. A number of participants have made proposals for follow-up meetings and I am sure that these will be carefully considered by the Secretary-General's Office. I look forward to future meetings of this type.

BACKGROUND PAPER

OECD Secretariat

Introduction

One of the striking features of the last decade of economic reform in both OECD and non-OECD countries is the increased interest shown in competition policy[1] as a means of improving economic performance. This policy emphasis is seen particularly in countries which have been moving from a centrally planned to a market economy where the adoption of competition laws, along with liberalisation of trade and investment, has been viewed as an important part of the reform process. It is however also apparent in recent measures adopted in many OECD countries to strengthen their legislative and enforcement tools to promote competition, whether directly by introducing new competition laws or by deregulating, privatising or in other ways opening up sheltered sectors of their economies to market forces. Many non-OECD countries other than Central and East European countries are also now exploring the need for a competition policy to contribute to maintaining in many cases already impressively high economic growth rates.

Competition policy is of course but one set of policy measures. Its main concern is with improving the structure and performance of markets in order to increase the overall efficiency of the economy and ultimately increase consumer welfare. It is thus in rivalry with and at the same time complements industrial policy, trade policy and some industry-specific regulatory policies which essentially share the same objectives.

The purpose of this background note is to analyse the specific role of competition policy in relation to these other policies and to describe the basic features of the policies chosen in OECD and other countries to achieve the efficiency and subsidiary objectives aimed at. While some convergence has taken place as regards choice of policy there remain considerable differences between countries in relation to both substantive and procedural rules for implementing competition policy, reflecting both different economic and legal structures.

The objectives of competition policy

A review of OECD countries' laws reveals that the majority of countries consider that the main objective of competition policy is to protect and preserve competition as the most appropriate means of ensuring the efficient allocation of resources[2] by acting against anticompetitive practices and by intervening to prevent monopolisation, abuses of a dominant position and anticompetitive mergers. In other words, the primary but frequently not the only objective is to promote economic efficiency, however this is measured. There are many different kinds of efficiencies - allocative and productive, static or dynamic, which are reflected in different countries' laws.

There is also frequent reference in many competition laws not to efficiency but to consumer welfare as being the main objective as opposed to producers' or overall welfare. Some countries also display in their laws quite different alternative or additional goals. These may be essentially economic (eg. the EC Treaty which refers to the pursuit of free trade) or may be directed towards socio-political goals

such as employment, pluralism, regional development or the protection of small and medium-sized enterprises. Merger control in many countries usually involves a multi-criteria assessment of particular mergers going beyond its pure impact on competition and efficiency. In some jurisdictions the notion of unfair competition is also incorporated in the competition law to protect competitors and consumers against deceptive or fraudulent practices.

Leaving aside these secondary objectives, current thinking among academics as well as competition officials would seem to favour the competition/efficiency objective alone as the best yardstick for evaluating firms' behaviour rather than trying to include many different economic or social objectives in the equation. This of course does not exclude consideration of such factors in the framework of the application of other policies. But, it is argued, competition policy should not be asked to consider such factors.

One important area which is growing in significance for competition policy is whether and to what extent it should apply to natural monopoly or regulated sectors where competition does not, or is believed not to, function effectively. The relationship between competition policy and other government policies will be examined in the next section.

Competition Policy and its Relation to Other Economic Policies

Competition policy's aim of targeting the anticompetitive conduct of private (and to a more limited degree) public enterprises to ensure that market operators compete effectively may bring it into conflict with a whole range of other policies.

Rather than describing all the possible interactions that occur, three significant examples of such interaction are mentioned, reflecting the focus of work by the OECD Committee on Competition Law and Policy in recent years; namely: the relationships between competition policy and other types of regulation, with intellectual property rights and with trade policy.

Regulated Markets and Competition

Recent years have seen widespread regulatory reform and the privatisation of many publicly owned enterprises. These reforms have been undertaken as a result of an increased awareness and evidence of regulatory failure. Not only do markets fail to function but regulation often does not achieve its objective of correcting the market failure.[3] In addition, there have been changes in technology and a better understanding of organisational structure and behaviour which have changed competitive conditions in particular markets and hence the rationale for direct regulation is called into question.

This process of regulatory reform does not eliminate the need for an effective competition policy. Rather it reinforces the need for it and provides new challenges for its implementation.

Reasons for Regulation

As discussed above, where markets do not function adequately, there may be a need for government regulation to ensure the adequate provision of goods and services at reasonable prices.

There are three main instances of market failure: natural monopoly, externalities and asymmetric information. Natural monopoly arises in sectors characterised by declining costs of production so that there is room for only one firm to exploit available economies of scale. Typically, natural monopolies occur in industries characterised by large distribution networks with substantial fixed costs, such as gas, electricity, water and railways. In practice, however, it is as rare to find examples of industry-wide natural monopoly as it is examples of perfect competition. Even if some parts of an industry have natural monopoly characteristics others may be potentially competitive. For example electricity supply consists of natural

monopoly in transmission but potential competition in generation and the supply of user equipment. Telecommunications was for a long time considered to be a natural monopoly at least for the basic telephone service, whereas value added services and the equipment market are competitive. The creation of new networks for voice transmission has even eroded the monopoly of the basic service.

Market failure can also occur in markets which are structurally competitive but where there are important externalities (e.g. where the full social costs of production are not reflected in the price of the goods or services). A chemical product whose manufacture causes pollution is one example of a negative externality. Some form of regulation may be needed to ensure that the polluter pays the full cost of his pollution.

Competitive markets also assume a degree of equality of information between consumers and suppliers. Where there is asymmetric information, because the goods or services are purchased infrequently or information costs are high then consumers may not have the requisite knowledge to make a rational choice when purchasing. Therefore intervention in favour of the consumer may be necessary to improve the quality of the information made available.

Forms of Regulation

Government regulation can take a variety of different forms. Structural regulation is designed to control which firms may undertake particular activities. It can be used, for instance, to limit entry into the industry to prevent excess capacity or to maintain activities in a market which are not profitable but which meet social requirements. Conduct regulation targets particular activities, such as pricing policy. Price control also comes in a variety of different forms, from the setting of actual prices, formula price fixing or the setting of minimum or maximum price thresholds. Another form of control is through public ownership.

Basis for Regulatory Reform

Over the last two decades, there has been a growing perception that public enterprises were performing badly. To ensure that domestic production survived and developed, governments intervened to regulate and "nurture" industries. Studies demonstrated that over-regulation contributed to poor performance, by providing insufficient incentives to firms and their managers.

There are a number of reasons for questioning the rationale and effects of regulation. For instance the basis for the market failure may have been incorrectly diagnosed or the steps taken to rectify the problem proven to be inadequate or disproportionate to the problem. Regulators may have been disadvantaged by the fact they were not close enough to the commercial operation to effectively meet changing market conditions or were faced with conflicting commercial and social goals with inadequate guidelines. (e.g. a regulator may have problems establishing a price mechanism which is flexible enough to respond adequately to changes in demand and costs). This is particularly so if the market is expanding or changing rapidly. In addition, the costs of administering the system in some cases were seen to outweigh the benefits to consumers.

Technological change has had an important influence on regulatory reform, sometimes transforming industries which appeared to be "natural" monopolies into competitive ones. For example the telecommunications sector has undergone considerable changes brought about in part by changes in technology, such as the introduction of satellite, microwave, cellular radio and cable and computer networks. These alternatives have partly eroded the natural monopoly of the traditional communications network.

Another factor which has hastened the removal of much unnecessary regulation and the privatisation of many enterprises and industries is ever growing budget deficits. Governments have

becoming increasingly concerned with reducing unnecessary regulation and subsidisation for purely budgetary reasons.

For example, it may be possible to improve performance by introducing market-type solutions in particular segments of a monopoly industry by contracting out particular activities to the private sector or by withdrawing the government monopoly granted to a particular enterprise and allowing in new entrants.

With sectors which demonstrate a mixture of monopoly and contestable market features, the policy challenge is to find the right combination of regulation and openness to possible competition. This may involve restructuring the enterprise into separate entities so that competitive activities are separated from those of the monopoly to avoid the danger of cross-subsidisation. Once the separation occurs, it is easier to identify those activities for which public financing is justified while leaving other activities to the play of market forces subject to the application of competition law to safeguard competition.

Other industries such as airlines, energy, transport, broadcasting, banking and insurance have also, for various historic reasons, become regulated or state controlled although they manifest many of the features of contestable markets. The trend in many countries has been to reassess the rationale for regulation of these industries and in many cases open them up to some degree of competition.

The argument in favour of removing regulation where it is inefficient applies only to regulation of prices, output, level of services and entry and exit (economic regulation) and does not imply that all forms of regulation are unnecessary. There is a range of non-economic and social regulations in areas such as health, safety, environment which affect competition in all sectors. These latter forms of regulation are not the target of policies aimed at improving efficiency, though even in these areas there is frequently scope for more competitive solutions to be adopted.

Competition policy and intellectual property[4]

At first sight it would seem that a competition policy concerned with the wide diffusion of technology to promote innovation in new products and processes would conflict with the private right of intellectual property owners to exploit their commercial value. However, the protection of intellectual property such as patents, trademarks, copyright and know how is necessary to ensure against under-investment in new technology. Otherwise there would be no incentive for investment if everyone could free-ride on the technology developed by others and the industry would fail to deliver the required amount of innovation necessary for its development. Intellectual property rights therefore provide an exclusive legal right over the use of certain information. However, this does not necessarily mean that the rights holder will be able to exercise market power. Whether he can do so depends on the demand for the product which is the subject of the property right and the availability of substitutes.

The apparent dichotomy between competition policy and IPR protection can be reconciled with regard to long-term aims. The static inefficiency resulting from IPR protection (because of exclusive rights, a price can be charged for the innovation which is far higher than the marginal cost of transmitting the information) is justified to the extent that it fosters innovation, a wider range and better quality of products and processes. It therefore enhances the dynamic efficiency of markets.

The ownership of IPR is much like other types of property ownership. The owner may either exploit the rights himself or transfer the use of the IPR (usually through a licence) to others in exchange for a fee or royalty. The transfer may involve the entire bundle of rights or may be restricted in terms of the field of use. The licensing of IPR can have either pro or anti-competitive effects depending on the economic context and the nature of the restrictions imposed by the agreement. Hence the need for competition policy review of licensing agreements.

Licensing agreements can exist horizontally between competitors or vertically. Horizontal agreements are by their nature more likely to be suspect in competition terms. The greatest risk is that the licensing agreement will be used as a cover for cartel arrangements to fix prices, limit output or divide markets. On the other hand, competing firms may enter into agreements to exchange complementary IPR for the purpose of developing new technology with pro-competitive effects.

Vertical licensing agreements play an important role in expanding production and distribution into new territories and therefore can be instrumental in the promotion of competition. The danger is where the arrangement is to reinforce cartel behaviour among competitors or to raise barriers in the market against other entrants beyond what is inherent in the substance of the IPR itself. Typical examples of such provisions are: tied purchase arrangements (where the licensee is forced to by inputs not covered by the IPR from the licensor or his nominees), tie-out arrangements (where the licensees are forced only to use the licensor's technology), restriction on use of technology once the IPR has expired, grant-back provisions requiring the licensee to assign all improvements and innovations without charge and market sharing requirements. This list is by no means exhaustive. The degree to which such provisions are anti-competitive in practice of course depends on the extent to which they enable the particular licensor to exercise market power.

Hence a case-by-case analysis is needed to distinguish between the pro and anti-competitive uses. IPR might for example be used by a firm as a means of non-price predation. A firm may use legal proceedings in bad faith, ostensibly to protect legal rights in intellectual property, but in fact as a means of burdening rivals with heavy litigation costs. Other practices include using IPR to protect secondary products or products not actually covered by the agreement.

The relationship between IPR and competition enforcement is not a new area but it is one which appears to be attracting greater attention. For instance, the US Department of Justice has recently circulated a draft of new guidelines for the licensing and acquisition of intellectual property[5]. In general, the guidelines start from the view that intellectual property is comparable to other types of property (while recognising that there are important distinguishing characteristics), that there is no presumption that IP licensing creates market power and that in general licensing is pro-competitive. It then goes on to explore the nature of possible antitrust concerns and give practical examples of how particular licensing arrangements would be analysed under US antitrust law. Licensing arrangements that may raise antitrust concerns include restrictions on goods or technologies other than the licensed technology and provisions that penalize licensees for dealing with suppliers of substitute technologies.

Trade and competition policies

A concern which is shared by trade and competition policy makers alike is that the benefits of the globalisation of trade, namely more efficient production and marketing, lower prices and improvements in quality, could be lost unless market access through competition is preserved and enhanced. In recognition of the significance of this issue, the OECD has undertaken a programme of work to explore some of the interrelations between trade and competition policies.

In 1994, a Joint Report by the OECD Committee on Competition Law and Policy and the Trade pointed out that -

"Increasing globalisation of business may reflect the success of trade policy but also creates new challenges...certain business practices may frustrate trade liberalisation and may create barriers to market access..."[6]

The reason for this lies in the fact that where these restrictive practices go unchecked they can act to block the entry into the market of imported goods and services, notwithstanding the removal of barriers to trade at the border. As a result, the potential stimulus from international competition is lost.

Domestic firms may deliberately enter into cartel arrangements or exercise market power to protect local markets from foreign entrants thereby depriving domestic consumers of cheaper or alternative products. These arrangements may or may not be facilitated by government regulations which favour such protection. Economies which lack the tradition and legal powers to attack restrictive arrangements may also find that their markets are subject to abuses which originate from outside their territories. Foreign businesses are able to exploit the lack of regulatory control on domestic markets without necessarily passing on the benefits to the local consumers. In this sense therefore, competition policy can influence the effectiveness of trade policies.

As domestic markets are becoming increasingly affected by international factors, competition policy needs to be adapted to take them into account. For example, while price constraints in vertical relations are generally condemned, it is commonly recognised that certain types of non-price vertical restraints may be efficiency-enhancing and assist firms, including foreign firms, in gaining access to markets. Too restrictive a competition regime on vertical arrangements might, for instance, deter companies from making investments in local distribution networks. Too permissive an approach could result in market sharing, disguised price constraints and other undesirable practices.

Horizontal relationships and their treatment may likewise have an effect on trade. Certain hardcore cartel practices, particularly those involving price-fixing, bid-rigging and market-sharing are almost universally condemned by competition authorities. Other types of arrangements tend to be assessed according to whether they have an adverse impact on competition and the extent to which this is outweighed by other positive contributions to the economy on a case-by-case basis.

Many competition laws tend to take a lenient view of export cartels as a matter of general policy. The reasoning behind this is that efficiencies can be gained through pooling skills and resources and spreading risks especially for small and medium-sized firms. Exporting countries tend to take the view that, to the extent that they enable firms to export where they might not otherwise be able to do so, export cartels are pro-competitive. On the whole, this has remained the consensus although the view is increasingly coming under attack especially where the cartel supplies a significant share of the world market or where it has negative effects on the local economy (eg. where it cloaks a parallel domestic cartel or prevents new firms entering the market). One suggestion made in a recent study is that export cartels should demonstrate that they do not adversely affect competition in the home market and that they serve to overcome barriers in importing countries.[7]

A significant reason for export cartels remaining a general exception is jurisdictional. Unless there is an anticompetitive effect on the domestic market the basic jurisdictional requirement for the application of the law is lacking; countries argue that it is not within their jurisdiction to examine possible anticompetitive effects which occur in other countries.

Import arrangements among firms for the purpose of coordinating the importation into the country of particular goods can assist firms in sharing the costs of importation and may allow them to benefit from discounts for bulk purchase. However, import cartels affecting prices or conditions concerning sale in the domestic market may have anticompetitive effects on the domestic market and therefore are less likely to be tolerated.

Another area of potential conflict between trade and competition policy lies in the different standards applied to treatment of allegedly low-priced imports. Anti-dumping measures are frequently used to keep out such imports based on an assessment of injury to domestic enterprises rather than an assessment of their impact on competition generally which is the competition standard for evaluating predatory pricing[8].

Voluntary export restraints (VERs) either arranged between private companies or between governments and exporters to "voluntarily" limit exports for a period of time affect domestic competition. Following the Uruguay Round, pre-existing public or government sponsored VERs and other safeguard

measures are to be phased out. One concern has been that government sponsored safeguards may be replaced by private industry to industry arrangements. Such agreements would have both trade and competition policy implications. Likewise voluntary import expansion arrangements (VIEs) which are designed to assist in the opening up of particular markets also raise competition and trade concerns.

Although there are areas in which trade policy and competition policy may come into conflict, there are equally areas where the aims of both converge. An effective competition policy has a positive role in opening up markets to trade. A credible domestic competition policy has therefore increasingly become a factor in bilateral and multilateral trade discussions.

It is sometimes suggested that for smaller economies, and in particular for those which are geographically close to larger markets or form part of an economic union, a liberal trade policy is sufficient to ensure competition and therefore that there is no need for a domestic competition policy. However, there are in many economies markets which, because of transport costs, consumer preferences or specialist requirements, remain essentially domestic or local. Common examples include fresh food, concrete and building materials and many types of professional services. A number of studies of OECD countries suggest therefore that a domestic competition policy is necessary.

Switzerland is one case it point. Switzerland, has always had a particular trade advantage thanks to its geographical location and its activities as a financial capital. Nevertheless, the 1993 OECD Economic Survey of Switzerland[9] indicated that a revitalisation of the Swiss economy was necessary and that this was dependent, at least in part, on structural adjustments in favour of a more efficient market economy. Accordingly, one measure which the Swiss Government is currently proposing is the reform of Swiss competition law.

Similarly, both the Dutch and the Danish economies are highly exposed to international trade. However in both cases OECD studies[10] argue that the domestic economies could benefit from more stringent competition laws particularly where domestic markets are not exposed to much direct import competition. In the Netherlands, work has commenced on the introduction of more stringent competition rules which will prohibit restrictive agreements and practices and the abuse of a dominant position by one or more enterprises.

The Convergence of Competition Policy

Convergence of national competition policies has been an ongoing process driven by various international developments principally related to trade liberalisation, economic integration and globalisation. In various international forums the exchanges of views on principles of competition law and their enforcement have led to substantial similarities in the emerging new legislation, as countries learn from one another. While it would be wrong to play down the differences that continue to exist, convergence has taken place in a number of important areas of competition policy - both substantive and procedural[11].

In the OECD, it has been possible to trace broad areas of convergence in competition policy and law to date.[12] There is general agreement for instance about the general direction of competition policy, the importance of transparency and non-discrimination in enforcement, the need for competition laws to be applied uniformally and universally throughout the economy with a minimum of exceptions, the importance of identifying barriers to entry into markets (although there remain marked differences in the identification and treatment of such barriers), mechanisms used for market definition and the treatment of horizontal agreements. The views on treatment of vertical restraints are more diversified.

At the enforcement level, national competition authorities are increasingly confronting cases with international ramifications, while businesses are increasingly finding their practices falling within several different jurisdictions. In the absence of agreement on principles and practices of enforcement, different

decisions are likely to ensue about similar practices. Differences in domestic competition policies can lead to confusion about what is acceptable or not in terms of competition law.

The OECD CLP Committee is actively encouraging further discussions about the analytical methodology, encouraging comity among jurisdictions, the sharing of and methods of obtaining information, developing agreement about core principles, the application of a flexible, economics based, case-by-case approach to most types of restrictive business practices, the review and filing of merger notifications and examining publicly sanctioned monopolies.[13]

In addition to OECD work, various initiatives aiming broadly at convergence have been taken in many other international forums and in bilateral and regional arrangements relating to competition.

The Political Background to the Adoption of a Competition law and its Effective Implementation

The preceding sections were concerned with exploring some of the reasons why competition policy is necessary to an efficient market economy. The second half of this paper deals with the introduction and enforcement of competition policy -- central to which is the adoption of an effective competition law. The political context of new legislation is an important issue but one which is seldom discussed. Proposed legislation, regardless of how carefully thought out or well drafted, runs the risk of being waylaid by vested interest groups or failing to gain sufficient political support.

It has already been mentioned that competition legislation has been introduced in some countries as part of a wider economic reform programme, which may include reform of company law, deregulation and privatisation. This approach has the advantage that although the benefits of competition and the market economy are appreciated, the need for a competition policy may not be so obvious. Some interest groups may view it as another form of government regulation of business and therefore indistinguishable from possibly previous forms of government regulation which were in the process of being dismantled. As part of a package, it is easier to place competition policy in the context of necessary structural reforms as a policy designed to monitor firms' behaviour in a more light-handed manner.

There are however possible pitfalls with this approach since the success of the adoption of competition legislation may stand or fall with the rest of the programme regardless of its individual merit. In addition, there can be pressure for the competition legislation to encompass provisions dealing with other regulatory problems whose objectives are not the same as those of competition policy.

In every economy there are vested interest groups which oppose the introduction of new competition laws. To some extent, the degree of that opposition is determined by the general level of familiarity with the aims and purposes of competition laws. Enterprises operating in international markets will necessarily be exposed to the competition laws of countries which have such laws and will therefore not be finding anything unknown if legislation is introduced domestically. Enterprises operating purely in domestic markets may be more suspicious of the purposes of competition law.

To give one example, a characteristic of the Irish economy is its dependence on an export market with its major trading market being the rest of the European Union. Prior to the introduction of new legislation in 1991, the competition legislation which existed was limited in scope. The new Irish Competition Act was modelled closely on the competition provisions of the EC Treaty. Political and business support for the Act was eased by the familiarity of a number of sectors of the economy with EU competition law. The greatest adjustments had therefore to be made by the non-traded sector which had been largely isolated from this influence.

The lack of exposure to competition and to competition policy in the non-traded sectors is a common theme and often a major source of opposition. Historically, even where competition laws applied

widely to most sectors of the economy, the professions and a number of other major service industries (e.g. finance and insurance) were largely exempt, being subject either to self-regulation or direct government regulation, on broader public interest grounds related to health, safety or simply quality.[14]

Part of the task of introducing new legislation is convincing interest groups that exposure to competition (e.g. in terms of prices and advertising as regards the professions) is not synonymous with a loss of quality of service, nor does it imply that there should be no regulation in the consumer interest. Equally, most competition laws provide the opportunity for enterprises or persons to justify practices if they can demonstrate that benefits accrue to the consumer.

The professions are only one example of the interest groups which may require particular persuasion. In a number of economies, the promotion of domestic industry has resulted in industrial groupings or cartels, many of which have grown up with the support and encouragement of governments and tariff protection. It usually takes some time for such industries to adjust to thinking in competitive rather than co-operative terms.

Another important aspect of introducing new legislation is for governments to consult with all interest groups before and during the actual drafting of a bill and before submitting it to Parliament. An extensive and timely consultation process can play a key role in the adoption and successful enforcement of new legislation. Input from the business community, consumer groups, professional and trade associations, in particular, can be valuable in ensuring that the final outcome is workable and consistent with market realities.

There are often well-established paths of legislative consultation. In Sweden for example, the tradition is for extensive consultation. Prior to Sweden's new competition law coming into force in July 1993, a Parliamentary Commission was established to consider reforming competition law. This Commission comprised members of different political parties which facilitated political consensus once the draft reached the legislature. It held public hearings and was assisted by a several ancillary groups representing different sectors of the economy. A number of studies were commissioned.[15]

This review took about two years. By the end of that time there were other political factors at stake, namely the decision of the Swedish government to apply to join the EU and signing of the EEA Treaty, which affected the final form which the legislation took. The consultation process nevertheless played a significant role in the reform and was undoubtedly a factor in the final legislation being passed unanimously by Parliament.

Another important decision to be made in introducing competition legislation is the nature of the institutional machinery to enforce it. While some countries have established several different bodies with different functions in the administration of the law, there appears to be a growing tendency towards the establishment of a single independent competition agency which is largely insulated from political pressure, which has extensive powers to investigate, adjudicate and sanction anti-competitive behaviour and whose decisions are subject to judicial review. This tendency has the advantage of simplicity and is probably more cost-efficient in avoiding the need for time-consuming exchanges and consultations when several bodies are involved. It goes without saying that the competition agency needs to have adequate resources to be able to enforce the law widely and expeditiously. It is evident that not much of an impact can be expected from an agency with few resources and many functions.

A number of countries also provide for an important advocacy role for their agencies, which also requires appropriate resources. That is to say not only does the competition agency in these countries have the primary function of enforcing the competition law but it is also given a broader role to comment upon other rules and regulations, frequently of an industry-specific nature, to ensure that competition considerations are taken into account when establishing or reforming rules. Not all countries however have given such wide-ranging responsibilities to their competition agency.

Another more controversial decision that needs to be taken before the adoption of a competition law is whether a role should be provided for private enforcement actions. The main advantage of such action is that parties directly affected by anticompetitive behaviour can obtain direct compensation from the perpetrators, thereby increasing the deterrent effect of the legislation. The principal disadvantage is that it is difficult to evaluate some forms of anticompetitive behaviour from a private perspective. Some countries already do provide for private actions and a significant number are brought each year. In other countries however, little effective use is made of private actions, where there is some provision, due to their cost and/or to the lack of adequate private remedies.

The Substance of Competition Laws

In spite of apparent differences between countries' competition laws, it is possible to identify certain core principles and provisions which generally underlie an effective competition law. The first generally accepted principle is that the substantive provisions of the law should be clearly aimed at eliminating anticompetitive behaviour and not penalising pro-competitive conduct. Hence there is a need for precision in defining the practices which are deemed to be anti-competitive in all circumstances and those which may be so in only some situations.

The second basic principle is that for maximum effectiveness the law should be applied uniformly across all sectors of the economy with a minimum of exceptions.

The major forms of behaviour which form the subject matter of competition laws usually comprise horizontal and vertical arrangements, joint ventures, mergers and acquisitions and the abuse of a dominant position or monopolisation. Some laws also deal with unfair, deceptive or misleading practices though more usually these practices are dealt with in separate laws on unfair competition. Consumer protection provisions are also sometimes included.

Horizontal Agreements[16]

Horizontal agreements or forms of co-ordinated behaviour between competing undertakings are conventionally divided into two categories: those which constitute "hard-core" restraints such as price-fixing, output restraints, market division, customer allocation and bid rigging which can be normally expected to reduce or eliminate competition and to lack redeeming effects on economic efficiency and those which may not harm competition significantly or which may be positively pro-competitive or have beneficial effects which outweigh the anticompetitive effects.

In some jurisdictions, the former are considered per se offences, i.e. the violation is established on proof that the agreement exists, while the second category is considered under a "rule of reason" analysis to ascertain their likely impact in the circumstances of the individual case.

The types of agreement which typically are treated as *per se* offences are those which:

-- set prices, tariffs, discounts and other charges;

-- limit the quantity of output;

-- divide the market, whether by territory, type of good, type of customer or other means;

-- involve bid-rigging;

-- eliminate other undertakings from, or limit access to, the market.

Agreements which contain restrictions that are not per se offences are examined on a case-by-case basis to assess whether taken overall the anti-competitive effects are outweighed by positive effects, for instance, because they promote the development of new products and services, encourage investment or enhance inter-brand competition. Examples of such agreements which are generally subject to a "rule of reason approach" include:

-- the establishment of labelling and other product standards;

-- joint or restricted advertising or promotion;

-- exchange of some types of information (information about costs, current prices and sale conditions however will usually be deemed anticompetitive);

-- research and development;

-- specialisation or rationalisation agreements.

Some of the factors which are taken into consideration in assessing the effects of these agreements include the size of the firms involved (agreements involving firms which have little or no market power are in some laws given an automatic de minimis exemption), the number of market operators, the homogeneity of the products and the general competitive situation in the market.

Vertical Agreements[17]

Vertical agreements are those between independent undertakings which operate at different levels of the market (for example between a producer and distributor). Vertical restraints contained in such agreements vary a great deal in scope and their effects on competition depend on the particular context. Some vertical restraints for instance, while limiting intra-brand competition, may eliminate free-riding and thereby increase overall inter-brand competition. Others may be used as a vehicle for collusion at the producers' or dealers' level and thereby restrict horizontal competition. For this reason, analysis of vertical agreements implies a more subtle analysis than that for horizontal agreements and there are fewer clear-cut offences. Vertical agreements are therefore generally dealt with on a case-by-case basis or are exempted by category, where specific criteria are fulfilled.

One notable exception to this is resale price maintenance (RPM) (i.e. where the seller specifies the final price at which the downstream undertaking will sell to the customer). RPM is prohibited outright under most competition regimes subject to certain very limited exceptions -- notably for books). Recommendation of prices is usually not prohibited so long as it is not a disguised form of RPM. The treatment of RPM as a *per se* offence is not without its critics. There are arguments that RPM should be treated to a case-by-case analysis like other vertical restraints. However to date, this view has not prevailed in most jurisdictions.

Common non-price vertical restraints include the granting of exclusive territories (by geographic market segment), limitations on the category of customers to which the reseller may sell, exclusive selling or purchasing, tie-in provisions (which oblige the purchaser of one type of goods to purchase other goods from the same supplier) and full-line forcing (which obliges the purchaser to buy a complete range of goods from the supplier rather than the particular type he wants).

The positive or negative effect on efficiency must take into account the prevailing market conditions. A vertical restraint can enhance efficiencies in circumstances where there is a serious free riding problem (i.e. where an undertaking benefits from the efforts of another without contributing to costs). For instance, the grant of an exclusive territory can reduce the possibility that one retailer can free-ride on the reputation or promotional efforts of another. Often a vertical restraint will have both positive and negative

effects on competition and an assessment has to be made of the overall impact. For instance, a restraint that limits intra-brand competition may have little effect on total welfare if there is significant inter-brand competition in that market. In the absence of significant inter-brand competition, on the other hand, the restraint could allow the producer with market power to significantly raise prices.

From an enforcement point of view, it would be costly to screen all vertical agreements case-by-case to assess their effects. Hence guidelines have been drawn up or category exemptions adopted to screen out vertical agreements which do not have significant anti-competitive effects. Various tests or criteria have been developed for this. The first is a market share test. Where the parties to an agreement have only a small market share in the relevant market(s), then even if a non-price vertical restraint causes some foreclosure of the market it is unlikely to significantly increase entry costs and deter entry. The second test looks at entry conditions. Even if the parties have a non-negligible share of the market but entry to the market in which they operate is relatively easy then the agreement is unlikely to have significant anticompetitive effects. Where these tests are not met then a more detailed examination would be warranted.

Some of the other relevant issues to be considered in making an assessment of non-price vertical restraints include:

-- whether one of the parties is a new entrant or is already established but attempting to enter a new market;

-- the nature of the product or service and the extent to which the restraints contribute to the production or distribution - of the product or service (e.g. aftersales service, special sales advice) or to the efficient transfer of know-how or intellectual property;

-- the duration of the agreement;

-- what the effect would be on the market if a particular practice was prohibited e.g. would there be less investment in research and development?

-- if the agreement is part of a network of agreements, what will be the overall effect?

Abuse of a dominant position/monopolisation[18]

Provisions against the abuse of a dominant position or monopolisation are common to most competition laws. Dominance or monopolisation occurs when a firm has an economic position which would enable it to behave independently of its competitors. Dominance does not preclude the existence of some competition but does imply that the dominant firm is able to have an appreciable influence on the market, i.e. the power to raise prices without losing market share. There are three stages of analysis to determine whether a firm is monopolising a market or abusing a dominant position:

(a) The definition of the relevant market

First, as in all areas of enforcement, it is necessary to define the relevant product and geographic market. The product (or service) market is defined in terms of the product(s) which are substitutable. Factors which help determine the product market include: the physical properties of the product, end use(s), price, elasticity of demand in response to a change in price and supply side substitutability. The geographic market defined by the area in which it can be expected that the products might compete in the short term.

(b) Identification of a dominant position.

A firm is dominant if it has substantial market power. This has to be assessed in the context of the particular market concerned. A low market share would suggest little or no market power. A high

market share does not necessarily result in market power. Other factors in this assessment include: the size of the market shares of other firms in that market, entry barriers to the market (such as costs of entry, government regulation, supply arrangements, "switching costs" for buyers, transport costs), evidence of strong vertical integration, control over distribution systems, control over intellectual property and the likelihood of entry and strength of potential competitors.

(c) Abuse of a dominant position

Abusive conduct by a dominant firm broadly includes behaviour which interferes with the competitive process and in particular attempts to eliminate or restrict actual or potential competition. Examples of such conduct include predatory pricing to drive out rival firms, refusal to supply, tied sales, limiting access to network facilities, price discrimination, vertical restraints and raising costs for rivals.

Markets which may be particularly vulnerable to the abusive exploitation of market power are those which have been heavily regulated in the past and which leave the incumbents with well-entrenched market power even after the regulatory framework that established that market power has been removed.

Mergers and Acquisitions

Mergers and acquisitions are important to market dynamics. They are a means by which firms can take advantage of available economies of scale, expand into different product and geographic markets, move into different stages of production or acquire access to technology and know-how as a complement to existing operations. Moreover, the threat of possible takeover may provide an incentive for better company management.

Notwithstanding the arguments in favour of mergers there are certain instances where the result may be detrimental to competition in the relevant market. This is much more likely to be the case for horizontal mergers than for vertical or conglomerate mergers but even so, relatively few horizontal mergers are challenged. The presumption of a negative effect on competition arises where the firms concerned have a significant market share, where the market is highly concentrated and where the market conditions are such that the likely effect of the merger is to create or strengthen dominance or otherwise substantially lessen competition.

Vertical mergers may sometimes also be detrimental to competition if they have the effect of foreclosing competition in upstream or downstream markets. Even conglomerate mergers may harm competition in some circumstances although the arguments as to the circumstances in which this is likely to harm competition are more controversial.

From an enforcement perspective, the characteristic problem of merger control is that once the transaction has occurred it may be very difficult to limit any adverse effects except by the fairly clumsy method of divestment. Most jurisdictions therefore opt for a pre-emptive form of control whereby parties must seek the approval of the competition authorities before completion. Notification is clearly not necessary for all such transactions and there is generally a screening process based on the size and market shares of firms participating in the merger before undertaking a detailed assessment of the likely effects on competition.

Enforcement of Competition Laws

At the national level

While the adoption of a competition law is a necessary first step towards the establishment of competition policy, the effective enforcement of the law is equally important. Enforcement agencies have

a significant role in interpreting the often general substantive principles in concrete cases and, along with any other institutions involved in enforcement, making significant decisions about the effects of particular practices on competition in the particular case. Precedents established by enforcement action become an important guide to enterprises on the actual policy being pursued. Mention has been made of the need for appropriate institutional machinery, preferably an independent agency enjoying considerable independence to enable it to focus on applying the law. This does not mean that it should not be accountable. Most laws require the agency to submit annual reports to the Minister with responsibility for competition policy or to Parliament. In addition, decisions made by the competition authority are subject to review by other administrative or judicial bodies in all countries.

The question of adequate resources must also be addressed. The competition agency must evidently be given adequate resources to carry out its functions. Otherwise it will lack credibility. Both these issues are uncontroversial, though the appropriate degree of accountability and level of resources are a matter of debate in the light of other government priorities.

The essential first principle of competition law enforcement as for any other policy, must be that decisions are taken transparently, fairly and consistently. For enforcement to be transparent, the law itself has to be well known to businesses and its provisions well publicised. This can be achieved initially through the distribution of leaflets and the holding of seminars on different aspects of the law. Subsequently, after a period of enforcement, guidelines are often issued on what is acceptable or unacceptable behaviour in areas where case-by-case analysis is necessary. Such guidelines must also be backed up by publicity on decided cases to illustrate enforcement activity.

Many competition authorities also emphasise compliance with the law rather than prosecution, preferring prevention rather cure. Such methods would seem to be particularly useful in relation to mergers and acquisitions where per se rules are not possible. Procedures for giving informal guidance to firms planning to merge are widely used in many countries and frequently avoid the need for formal, lengthy investigations, costly for both the authority and the firms involved.

Enforcement agencies recognise the need not only to be fair and consistent in decision making but to ensure that they are seen to be so, particularly in their unbiased treatment of businesses (whether domestic or foreign, large or small, government regulated or private) and as respecters of confidential business information.

As noted in section IV above, there is a wide diversity of powers given to competition authorities in relation to investigating, prosecuting and sanctioning anti-competitive behaviour. In the interests of the principle of the separation of powers, some countries have chosen to separate the investigative from the adjudicative and sanctioning functions by giving powers to an administrative agency to perform the investigatory function while leaving it to the courts or to a specialised tribunal to decide and impose sanctions. Others have vested both types of powers in the main administrative agency, albeit subject to judicial review.

Closely linked with the choice of an administrative or judicial system is the issue of whether certain offences should be criminal or subject to administrative proceedings and fines. Most countries appear to have opted for the administrative system of enforcement.

One practical issue to be resolved is whether it is necessary to have one investigatory office or a number of regional offices. It is a matter of pragmatic judgement how this is organised, based on factors such as the geographical size of the country, the number of major business and/or political centres exist and budgetary questions. In general the larger and more disparate the business community is, the stronger the argument for having regional offices to deal with regional issues. For instance, Chile has a "Regional Preventative Commission" for each regional capital and a "Central Preventative Commission" to consider matters relating to the Santiago metropolitan area and cross-regional or national issues. The use of regional

offices as a matter of administrative convenience should not be allowed to affect the way in which geographic markets are defined during investigation.

The internal workings of the administrative authorities are another issue for debate. Some authorities prefer to divide their investigations according to sector in order to benefit from in-depth knowledge into particular markets. Others prefer to divide their resources up according to type of practice to maximise experience about particular offences.

As well as appropriate powers to investigate possible anticompetitive behaviour, including search and seizure powers, on-the-spot investigations and the like, which are not available to all competition agencies, it is evident that an agency which has been given adjudicative and sanction powers should be able to impose appropriate penalties on infringing firms. How to determine the appropriate level is a delicate enforcement matter, however. Fines are the most common sanction. They evidently need to take account of the severity of the practice, including the length of time it operated, as well as the size of the offending firms. One method used in the European Union is to relate the fine to the turnover of the firms involved.

International enforcement of competition laws

The last few years and particularly the year since the conclusion of the Uruguay round have given rise to various suggestions for facilitating the application of national competition laws internationally and for establishing new international machinery to cope with the internationalisation of markets. Many of these suggestions are not new but can be traced back to the early post-War period. But there appears to be a growing belief that something else is needed to cope with the increasing number of competition cases arising which affect more than one country. What this something should be is still very much a subject of international debate.

The suggestions made include:

-- a more expansive use of national legislation when harmful anticompetitive effects are felt on the national market;

-- increased use of bilateral agreements to facilitate cooperation between competition agencies;

-- strengthening the OECD 1986 Recommendation on cooperation between Member countries on restrictive business practices affecting international trade; and

-- the establishment within the new World Trade Organisation of new rules and machinery to investigate and resolve disputes in the competition policy area.

All these suggestions raise substantial issues relating to sovereignty and jurisdiction as well as substantive issues of differing views on the principles of competition policy as well as the procedures for enforcing the laws. While countries generally agree on the usefulness of international cooperation to investigate anticompetitive behaviour, these differences would appear to be a serious obstacle to further measures at least of a multilateral nature.

In the enforcement area, for example, there are significant practical enforcement problems associated with applying competition laws to undertakings not located within the enforcing country's territory (e.g. how to obtain information necessary for the investigation, how to serve process on the foreign firm if it does not have a local subsidiary). As discussed in relation to convergence, this is a subject on which the OECD and other international forums are continuing to work.

Notes

1. There is no internationally agreed definition of competition policy but in accordance with the practice of the majority of OECD countries it is taken to mean the body of laws and regulations governing business practices affecting competition, principally horizontal and vertical agreements between enterprises, abuses of dominant positions, monopolization, mergers and acquisitions. Some jurisdictions also include aids and subsidies to enterprises, the regulation of prices of monopolies and demonopolisation under the general policy heading of competition policy.[See Interim Report on Convergence of Competition Policies (Interim Report), OECD, 1994, Annex, p. 8].

2. See Interim report, op.cit., p. 8.

3. For a more detailed analysis of the relationship between competition and deregulation see: Regulatory Reform, Privatization and Competition Policy OECD Paris (1992).

4. For further details and a comparative study of OECD countries, see Competition Policy and Intellectual Property Rights OECD, Paris (1989).

5. US Department of Justice Antitrust Guidelines for the Licensing and Acquisition of Intellectual Property, Preliminary Draft July 29, 1994.

6. Trade and Competition Policies, Joint Report by the Committee on Competition Law and Policy and the Trade Committee, OECD/GD(94)63, paragraph 1.

7. Obstacles to Trade and Competition, OECD, Paris (1993), p. 92.

8. For an analysis of OECD countries' rules on predatory pricing as well as a suggested common method of analysis, see Predatory Pricing, OECD(1989), especially pages 81 to 83.

9. Switzerland OECD Economic Surveys, Paris (1993).

10. Denmark OECD Economic Surveys, Paris (1993) and Netherlands OECD Economic Surveys, Paris (1993).

11. See the Interim Report, op. cit. pp. 8 to 18.

12. Idem, paragraph 14.

13. Interim Report on Convergence of Competition Policies, op. cit.

14. A report by the OECD's Committee of Experts on Restrictive Business Practices stated "Experience ... indicates that actions to promote competition in some professions do not necessarily jeopardize the quality of services provided and that many traditional practices excessively restrain competition and may promote the interests of the profession and not the public". [Competition Policy and the Professions, OECD, 1985, paragraph 274].

15. These included for example: one by the existing competition authorities into the level of competition in 61 markets (chosen either because they had come to the particular attention of the authority or were subject to a sector-specific regulatory regime); a review of competition within local government (with particular reference to procurement); a study into the effect on competition of trading relationships with major trading partners; a paper on the relationship between competition and standardization; a review of the structure of the competition authorities (resulting

in the streamlining of the enforcement structure) and into legislative procedures (including sanctions).

16. There are different definitions of an agreement but most jurisdictions have adopted broad definitions to cover not only formal written agreements but also tacit arrangements and concerted action.

17. See also Interim Report, op. cit., pp. 13-14.

18. See Interim Report, op. cit. pp. 14-15.

CONTRIBUTION OF COMPETITION POLICY TO ECONOMIC DEVELOPMENT: THE CASE OF MEXICO

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The Motives for a New Competition Policy: The Case of Mexico

Competition Policy in Mexico: Background for Mexico's new competition policy

The onset of the external debt crisis in 1982 marked a critical turning point in Mexico´s economic policy. Left behind was a model of economic development which, in order to generate rapid economic growth to improve social welfare, relied on a growing participation of the State in the economy and neglected the efficient operation of companies and markets. To achieve this goal, especially when the international economic situation was unfavourable, the government had to rely increasingly on instruments such as public expenditure, foreign debt, commercial protection and price controls. The 1982 crisis demonstrated the enormous vulnerability which the adopted growth model had to external shocks. The project did not make the country stronger and more independent. On the contrary, the economy had become extremely dependent on variables such as petroleum prices and international benchmark interest rates. That is extremely dependent on the volatile world commodities and financial markets. In this context, it was essential to put the country´s finances on a sound footing, which meant that it was not possible to support an ambitious subsidy policy and therefore necessary to rationalize the structure of prices in the economy. There was a gradual elimination of the large existing subsidies, the prices and tariffs of the public sector were adjusted and the government looked for alternatives that would give greater transparency to the economy, thus inducing more efficient decisions from economic agents.

Hence, in 1983 began a process of structural change, which continues to this day. This process has had two pillars. On the one hand, and mainly at the beginning of the programme, public finances had to be put on a sound footing since it was extremely important to strengthen the Government's ability to control macroeconomic variables. In order to achieve this goal, both the Government's size and its role in the economy had to be redefined. On the other hand, the Government has sought to use markets in order to promote a more efficient economy. The Government has little by little withdrawn from its role as active participant in the markets (as producer) and allowed market forces to deal with the allocation of resources. In fact, the stabilization programme which seeks to create a more stable macroeconomic environment backed by healthy public finances, price stability, coherent exchange rate and a progressive debt reduction is anchored in microeconomic policies: trade liberalization, privatization of state-owned companies, sectorial deregulation and liberalization of the foreign investment law.

Microeconomic Reform Aspects

Trade liberalization

Trade liberalization, after Mexico's entrance to the GATT in 1986, was accelerated in 1989. Its purpose was to foster the correction of relative prices in the economy. Distortions caused by non-tariff

barriers were eliminated when quotas and permit schemes were replaced by tariffs in a system that had both the level and the dispersion of the tariffs reduced. The coverage of import quotas drastically dropped from 92 per cent in 1985 to 20 per cent in 1990, while tariffs decreased from a weighted average of 24 per cent down to 13 per cent. Likewise, price controls in the domestic market were reduced in a gradual but sustained manner. The North American Free Trade Agreement can be seen as part of this process of economic opening.

External competition, fostered by trade liberalization, does not reach each and every market. In every economy of the world, the service sector is one of the sectors which happens to be less exposed to the competition fostered by trade liberalization. This sector takes an important share in the Gross Domestic Product. In Mexico, the service sector represents 66 per cent of the GDP and accounts for 60 per cent of the total work force. To a certain extent, deregulation and foreign investment liberalization were frequently intended to make sectors such as transport, communications and finance more competitive; however they were not enough.[1] On the other hand, although trade liberalization has permeated the economy as a whole, it has not had the same impact on the various industries. Furthermore, there are entry barriers to the domestic market which trade liberalization does not eliminate. These barriers may be caused by high transportation costs, by regulatory barriers such as norms and standards policies, by macroeconomic policies such as dual exchange rates and by monopolistic practices from companies in the country.

Foreign investment

Also, and as part of the economic opening process, the legal framework of foreign investment was modernized. The 1993 Law clearly defines individuals and activities subject to the new legal framework and opens up new sectors to foreign investment. This law eliminates both export requirements of firms with foreign direct investment and limitations on imports. The new law creates a more transparent and less discretionary framework and promotes the entry of new competitors to the domestic market on an equitable basis.

Deregulation

The purpose of the Government, behind the deregulation policy, was to stimulate economic activity and achieve a more efficient allocation of resources. Quite often, owing to bureaucratic red tape, legal requirements to establish new companies could take almost a year. Frequently, access to preferential credit, incentives and tax deductions favoured big-sized firms. Among the sectors most affected by the deregulation during recent years we can list the financial sector, the automobile industry, trucks and buses in federal highways, textile, petrochemical and electricity industries. The new laws on technological transfer on patents and brands are also important examples. Moreover, deregulation has also reached the certification of mercantile transactions and custom houses.

Privatization

The privatization period of state-owned enterprises began in 1982, when the Government owned 1155 companies. Through different means such as liquidations, mergers, transfers or sales of such companies, by 1991 the Government came to own a little over 200 companies. This process implied a significant reduction in the relevance of the public sector in terms of employment and production. At the same time, privatization was an important, short-term, fund source for the Government.[2] During the privatization, efficiency as well as other public interest criteria were considered; however the objective of putting public finances on a sound footing was overriding. Thus, it was not always considered convenient to modify the monopolistic structure of the market when a company was privatized. In the near future, the economic rationale of maintaining private monopolies in regulated sectors must be evaluated, no matter whether or not they are the result of privatization.

Towards the Design of a Competition Policy

The reforms mentioned were the core of the process of structural change until late 1992. During the last two years, the bases to renew and strengthen the sustainability of the process of structural change, which the economy still requires, have been reinforced. In December 1992, the Government issued the Federal Law of Economic Competition (FLEC) and created the Federal Competition Commission (FCC) to watch over its enforcement. The FCC sets the bases to guarantee the permanency of the effort which the Government should maintain to achieve a more efficient allocation of resources with a fair participation of agents in the market. This should enhance the support from society for the undergoing structural changes.

The enactment of the Federal Law of Economic Competition represents a significant change in the way the Government intervenes in the economy. Intervention associated with direct controls is left behind and replaced by an approach which primarily seeks to enhance the self-regulating capacity of the markets, and in special cases, direct intervention to impose sanctions so as to put a stop to concentrations and practices which tend to monopolize markets.

The FLEC explicitly states the Government's position as regards its commitment to protect the process of free competition and thereby to give economic agents certainty and confidence. The FLEC recognizes that markets by themselves do not necessarily operate well and that monopolization is a recurrent problem which ought to be confronted.

Objectives of the FLEC

The single objective of the Law is to bring about an efficient operation of markets. Having one objective is convenient for several reasons. It simplifies the analysis and the decision making within the FCC. This is important as competition policy is a complex matter with significant grey zones which need a conceptual analysis and a deep, empirical investigation. It also brings about a more transparent administrative process and allows the corresponding authorities to be accountable in a more precise manner. In addition, the possibility of having conflicting interests between objectives is ruled out and competition authorities become isolated from political pressures. It is preferable to achieve objectives different from economic efficiency through the use of other Government alternatives and instruments.

Although equity is not an objective of the law, an important by-product of the implementation of competition policy is to improve the distribution of income. The FLEC penalizes anticompetitive practices which limit the participation of economic agents in the market. Competition policy tends to eliminate the market access restrictions caused by monopolistic practices. This levels opportunities among agents. Even if, at the beginning, both big and small companies may infringe the law, world-wide experience suggests that usually the bigger companies are the ones which more often engage in monopolistic practices. Better opportunities for small and medium-sized companies tend to improve, in the medium-term, the distribution of income. This is because stronger medium-sized and small firms, usually labour intensive, increase the demand for labour and raise employment. This leads to higher wages in these firms and a reduction in the spread of wages paid between large firms and medium-small firms. Because of this, competition legislation only attains the goal of increasing efficiency, but may also improve income distribution as a by-product.

The Relevance and the Limitations of a Competition Policy

Competition policy reveals itself as an important part of microeconomic policy. An effective competition policy should have two complementary front lines. On the one hand, it should respond and evaluate the cases filed by the parties. On the other hand, it should lead a pro-active policy which promotes competition in the economy. Nevertheless, and even if competition policy is understood in a broad sense,

which promotes the design of regulatory schemes and the operation of competitive markets, such policy has important limitations.

There are several reasons which explain why a competition policy, by itself, is not enough to attain the goal of economic efficiency. Laws do not have retroactive effects. Thus, in Mexico, the preventive attitude of the law regarding concentrations will incidentally have effects in the future. Owing to a lack of a competition policy in the past, markets today have concentration levels which inhibit their efficient operation. Competition policy must try to prevent companies in these markets from engaging in monopolistic practices.

Since the beginning, the FLEC considered that the various legal rulings may occasionally create multiple restrictions on the participation of new competitors and generate a legal background which at times could seem ambiguous and inclined to create monopolistic situations. Because of this, the FCC issues an opinion on the adjustments made to the Government's administration programmes and policies when they are contrary to competition and free market participation. It may also issue an opinion on proposed laws and regulations concerning competition and free market participation aspects and regarding laws, regulations, agreements, circulars and administrative procedures. Likewise, it may establish coordination mechanisms to fight and prevent monopolies, concentrations, and illicit practices. The change in the regulatory framework will be fundamental if competition is to be strengthened in a large number of services such as telecommunications, the financial sector, and the health and transportation sectors. Consequently, the competition authority should issue an opinion regarding the conditions which are necessary so that there is competition in these markets.

There is not only a problem of excessive regulation in key sectors (which have undergone substantial deregulation, as has already been discussed), but rather one relating is the promotion of regulatory reform which would foster competitive conditions in certain key sectors. The FCC thought it pertinent to work together with the various Government Ministries responsible for the identified sectors. It was thought that: "Competition policy should not be a substitute for adequate regulation. It is necessary for regulating authorities to work in coordination with the FCC, as if this is not so, the competition authority will not be able to attain the expected results. It is essential for regulating authorities not to issue resolutions, circulars or any other kind of dispositions which prevent or limit the participation of new competitors or create exclusive advantages for a selected group".[3] Thus arose the need to have a coordination policy between competition policy and the regulating policies in the different sectors of the economy in order to strengthen competition criteria employed by regulating authorities in the process of licensing, granting public permits and authorizations. This cooperation could prevent concentrations and monopolistic practices and could create regulations which duly consider competition criteria.

From among the examples mentioned in the next section we find important elements which are common to all and which are perhaps indicative of some of the challenges involved in competition policy. Two sectors discussed are connected with problems concerning network economies. We point out that from the presence of network economies, it does not follow that there are significant scale economies. The concept of natural monopoly in each of these and other sectors which are vital to the competitiveness of the country has been superseded by the technological progress in telecommunications and computing systems. Such progress allows access and use of the network by several competitors.Thus, in markets with network economies technological progress seems to have made vertically integrated corporative structures unnecessary. We agree with Porter when he says that one of the most important tasks for competition policies is to guarantee a healthy competition at a national level,[4] mainly in the sectors which have a bearing on the productivity of the whole economy.

Certain FCC's Experiences Set Out to Achieve Greater Competition

An example from the competition authority's participation in the reform of the regulatory framework. The case of telecommunications.

In 1990 the Government of Mexico privatized Telmex, the Mexican telecommunications monopoly. Telmex' concession title[5] established that the exclusive right to render long-distance services would end in 1996. Four years after privatization, the development of this company has been limited, and, even though there has been an expansion in the service, there still is a large unsatisfied demand.[6] The quality of the services and the ability of the company to repair failures in the system has caused this company to accumulate the greatest number of complaints from consumers.[7] Likewise, the variety of products offered in the market is reduced and costs are high.

With a view to improving this state of affairs and at the same time owing to the great static and dynamic importance of the telecommunications sector in an economy which seeks to become competitive at an international level, the FCC carefully investigated the sector and concluded that the opening to competition in this sector was the best means to meet the objectives of greater growth and quality, as well as the objective of reducing costs. As to the design of the opening process, the FCC resolved to make use of its power to issue an opinion concerning competition, in order to participate together with the corresponding regulating authority, with the Ministry of Communications and Transportation and with other authorities from the Federal Government. The experience of working together with other agencies and consulting with specialists demonstrated that the FCC was able to play an important role within the Government. The natural separation between the FCC and this sector gave the FCC a more general, long-term perspective.

Until some years ago, telecommunications included a set of different services such as telephone, telegraph, radio and television. The swift technological advance in this sector makes the regulating frontiers artificial among these services. Digitalization in every service, that is, the transformation of voice, image and data signals in a sequence of zeros and ones means that all such activities are transmitted in the same manner. On the other hand, optical fibre makes the transmission capacity almost unlimited. Furthermore, wireless technology development or "personal communication systems" promise to lower prices of cellular telephones to a fifth of their present cost and to allow such communication anywhere, anytime.

Telecommunications are essential for the development of economic activity. They are an intermediate input of the utmost importance in many sectors, such as the financial, health, education and transportation services, among others.

Our Nation's opening-up process needs to emphasize, increasingly so, the factors which determine competitiveness. Our North American Commercial partners' telecommunication networks and services are among the most efficient in the world. The possibility of setting up companies, for example, between Monterrey and San Antonio will largely depend on the quality and price of telecommunication services. In order to attract direct foreign investment it is essential to have modern and inexpensive telecommunications.

The telecommunication revolution directly promotes society's welfare. It eases the access to the labour market for those whose time availability is limited, allows individuals to choose the place where they wish to live, and upon reducing migration risks and costs, facilitates mobility. With the purpose of contributing to obtain top benefits in the opening-up of competition in telecommunications, the FCC examined the existing regulatory framework in Mexico, the opening proposal from the private monopoly, Teléfonos de Mexico, as well as the experience accumulated by countries such as Australia, United States, Finland, Japan, New Zealand, the United Kingdom and Sweden and dealt with various companies. Based on the above, the Commission declared that:

-- vigorous competition in this sector encourages its swift development, and helps in the fulfilment of universal service objectives planned by the Government;

-- the number of competitors must not be limited, either for long distance or for local communication;

-- both for long distance and for local service, Teléfonos de México should allow, in time, interconnection between competing companies in every technically feasible point and not only in a restricted group of them. This allows every route to be open to competition;

-- competing companies must be able to decide whether or not to interconnect to Teléfonos de México's network. This liberty promotes investment and infrastructure development. On the other hand, it allows the existence of medium-term, self-regulating interconnection tariffs, reducing the need for tariff controls from the authority.

-- companies must be able to compete in national and international long-distance services, thus avoiding the existence of exclusivity agreements which give a captive market to certain companies.

-- the regulation must offer fair conditions to every competitor, no matter what its size. Thus, all competitors including Teléfonos de México should pay the same interconnection costs. With this in mind, there must be an exact and transparent accounting of interconnection costs.

-- Users must be able to previously subscribe to a company in order for them to be able to discriminate between quality and price of several competitors; that access must be gained through dialling the minimum number of digits; and companies may offer complementary services to users (such as operator or invoicing adapted to the needs of the clients).

-- In order to avoid having artificial barriers to the entry of new competitors, concessions and permits must be granted to all interested parties, mainly on the basis of technical considerations which minimize discretionary margins. Moreover, concessionaries must be prevented from paying different utilization rates.

On the 1st of July 1994 the Government published the resolution concerning the opening to competition of long-distance telephony. This resolution takes into account to a great extent the recommendations made by the FCC. At present, it outlines the regulations which should apply to local telephony competition. The FCC is actively participating in the elaboration of these regulations.

It is worth also emphasizing the FCC's behaviour regarding two specific areas: the most important company and monopoly in the country, Petróleos Mexicanos and the finance sector.

The distribution of gasoline opened to competition

According to Article 28 of the Mexican Constitution, there are several activities reserved to the State. Among them, we have activities related to petroleum, railroads and social security. Thus the Constitution leads to the existence of State monopolies. However, constitutional reforms in the last few years have narrowed the scope of the activities that are strictly reserved to the State. On the other hand, the firms in these sectors have over the years sometimes expanded their monopolies to cover products and services beyond those reserved by the Constitution as a State monopoly. The case of gasoline distribution is an effort by the FCC to introduce competition in a market segment that was until recently exclusively covered by the state oil company (Pemex) although it is not an area strictly reserved to the State.

The FCC studied the gasoline market in Mexico and found that there were less than 4 000 gasoline stations in the whole country; that the geographic distribution of gasoline stations was not balanced and that very few gas stations had very important market segments. Service was of poor quality and there were no rules to open new gas stations. Moreover, existing regulations created artificial barriers to marketing complementary goods and services such as food and beverages inside gasoline stations; these restrictions also affected suppliers of equipment such as gasoline pumps or meters.

With the purpose of adapting the operation of gasoline stations to the framework of the new competition law dispositions, the FCC in coordination with Pemex worked out precise criteria for the establishment of contracts between Pemex-Refinación and those individuals who would be interested in participating in such activity, allowing a significant increase in the number of service stations.

To prevent possible anticompetitive practices, the FCC and Pemex-Refinación signed a consent agreement in June 1993 which sets forth the necessary conditions to meet consumers demands more efficiently. The agreement:

-- sets clear, simple and precise requirements for application and acquisition of contracts to operate new gasoline stations;

-- establishes Pemex-Refinación's commitment to enter into a contract with anyone interested in opening new gasoline stations, provided that they meet Pemex Refinación's technical, safety, environmental and image specifications;

-- eliminates restrictions on the number of gasoline stations that can be opened in a specific area, and any distance requirements that may exist between stations;

-- establishes that supply contracts between Pemex-Refinación and third parties may be freely traded in a secondary market provided that Pemex-Refinación is duly notified;

-- eliminates the subfranchising system, thus allowing the marketing of all goods and services in gasoline stations, other than alcoholic beverages or explosives, as well as liberalizing business-relations with third parties in the gasoline stations.

To inform the general public of these new provisions, Pemex-Refinación and the FCC published in July a "Simplified Program to Establish New Gasoline Stations" which contains simplified requirements and other elements and conditions.

Three important benefits derive from this agreement. First, as the number of gasoline stations progressively increases, gasoline consumers will have lower costs either because the waiting time at the gasoline station itself will be reduced or because the distances consumers must travel to access gasoline or other related products or complementary services will be shorter. Second, as competition among gasoline stations increases, the service will be better, widening the range of goods which individuals will be able to get. Third, there will be more opportunities for those interested in opening new gasoline stations. All this should be significant for millions of gasoline consumers in the country, for new goods and services suppliers and for new gasoline station operators.

As new gas distributors come into the market, it may be possible in the future to liberalize retail prices and thus introduce another element of competition into this market.

Introduction of Competition in Banking Credit Cards

Credit cards play a major role as a means of payment and credit. This is evidenced by the fact that the volume invoiced by credit cards is slightly over five per cent of the country's gross domestic

product. On the other hand, consumer credit granted through credit cards represented close to 75 per cent of overall consumer credit granted by the banking system in 1993.[8] Considering the significance of this product, the Commission investigated, ex officio, competitive conditions in the relevant market, partly as a result of its finding that the average commission paid by merchants for the use of credit cards seemed to be higher than the average in other countries,[9] partly by its finding that merchant commissions were the same for all credit cards; partly by its finding that the interest rates charged to cardholders were substantially the same among the largest issuing banks; and partly by its finding that profit margins on credit card operations are high, not only as compared to other countries,[10] but also as compared to other bank products in Mexico. These findings, of course, were not in themselves proof of anticompetitive practices, since for example, the level of merchant commissions might reflect the banks' operating costs which, due to the fact that for many years investments in computer hardware were not enough, could be relatively higher than in other countries.

The Commission started its investigation by studying conditions prevailing in other countries.[11] It was found that there are several credit card payment systems, the major ones being VISA and MasterCard; these systems make their best efforts to have their brands accepted as widely as possible, they facilitate interbank clearing of bills of sale, authorize operations, and provide a wide range of services to their affiliated banks. The Commission further found that the countries where merchants pay lower commissions are those with competing payment systems.[12] Likewise, the Commission found that payment systems such as VISA and MasterCard do not directly affiliate merchants nor issue cards. There is a separation between acquiring banks, issuing banks and payments systems. This structure permits each acquiring bank to set merchant commissions independently. As a consequence, acquiring banks compete in the setting of merchant commissions, issuing banks compete in the setting of interest rates charged to cardholders. On the other hand, payment systems also compete strongly in the markets. Such competition among systems has resulted in lowering merchant commissions and generated a continuous technological development which has reflected in new products, competitive prices, better quality and service.

There is no information exchange among acquiring banks or among payment systems, nor is such exchange required; this induces affiliating banks to compete among themselves and thus benefits merchants and cardholders.

By contrast, in Mexico there was no clear distinction among acquiring banks, issuing banks and payment systems. There are three local credit card systems, namely, Bancomer, Banamex and Carnet, which, at least when setting merchant commissions seemed to behave in a coordinated manner. Bills of sale among the three credit card systems were cleared by means of agreements which stipulated that the merchant commission belongs to the bank issuing the card. Because of this, the bank where the affiliated merchant deposits its vouchers did not receive any payment for transactions associated with the processing of credit cards, which limited incentives for these banks to compete for merchant commissions and this way contributed to lower them. As a result of this mechanism, the commission charged by the three credit cards to every merchant was identical. Similarly, interest rates charged by banks to cardholders showed important parallelism.

Finally, the Commission found that through certain clauses in the affiliating contracts, banks prevented merchants from offering discounts to their customers if they paid in cash, thereby limiting options to them and to their customers.

In order to solve this problem, in June 1994 the Commission executed a consent agreement with Banco Nacional de Mexico, S.A., Bancomer, S.A. and Banca Serfín, S.A., Grupo Financiero Serfín, as majority stockholder of Promotora y Operadora, S.A., the company which handles the Carnet brand. This agreement acknowledges, on the one hand, that although changes were occurring in the operation of credit cards, it was necessary to strengthen competition and prevent possible anticompetitive practices; and, on the other hand, that a transition period was necessary to adapt the operation of the payment systems to the new competition provisions.

As a result of the consent agreement, the banks operating credit cards undertook to eliminate the following:

-- information exchange among themselves aimed at, or resulting in, the setting of common or coordinated merchant commissions, or interest rates to cardholders;

-- within six months, any covenants from the membership agreements executed with merchants which prevent the latter from offering discounts to consumers who pay in cash;

-- within one year, any information regarding merchant commissions from the manual machines, which is presently printed on vouchers when such machines are used.

Conclusions

The FCC has been operating for a year and a half. Nonetheless, the experience we have obtained in this period may be useful to other countries. Undoubtedly, we are only at the beginning. One of the important tasks, which will require continuous effort, is to spread out and promote the understanding of the FLEC and its objective in order to generate in the country a competition culture. This will make the FLEC a better instrument since it would tend to reduce the emergence of anti-competitive practices in the country.

The fact that for Mexico it is important to have a strong competition policy does not mean that this is the case for other countries. The enforcement of the competition law needs highly skilled personnel capable of evaluating practices which require a complex analysis. There are important grey zones where economic theory has not yet been sufficiently developed. One of the practices which is difficult to evaluate, but which has been one of the most popular, is predatory pricing. In addition, emphasis should be placed on the fact that competition policy is not a substitute for adequate regulation. Furthermore, unless regulating authorities work in a coordinated manner with competition authorities, the latter's efforts would be frustrated. Thus, for example, if the regulatory authorities grant concessions on a discretionary basis to companies which are already in the sector, instead of granting them to new participants, it increases concentration and this cannot be prevented by competition authorities. Likewise if regulatory authorities issue resolutions, circulars and other legal instruments which in practice allow (or foster!) collusion among several competitors, or the carrying out of other monopolistic practices, not much can be done to counteract this through the action of competition authorities. Such actions, on behalf of the regulating authority, may be intended to improve the operation of the sector, but almost invariably they are actions which reduce consumers' welfare or overall economic efficiency.

Considering the above, we infer that in the future it will be of the utmost importance to achieve a coordination between competition policy and the regulatory policies in the various sectors. Therefore, it will be necessary, on the one hand, to include and increase the importance of competition criteria in the process of regulatory design by the different authorities: in principle the sector should be regulated only when there are structural reasons which prevent competition from achieving an efficient equilibrium. On the other hand, it is also necessary to strengthen the power which competition authorities have to intervene in the way concessions are granted and in the process of the regulatory framework.[13]

Notes

1. Examples of actions taken by the FCC in this sector are submitted in section III of this paper.

2. See ASPE ARMELLA, Pedro. *El camino mexicano de la transformación económica*. (The Economic Transformation Mexican Path) Fondo de Cultura Económica.

3. Federal Competition Commission's First Annual Report, 1994.

4. PORTER M., *The Competitive Advantage of Nations*, 1990.

5. SCT, *Modification to Teléfonos de México, S.A. de C.V.'s Concession Title*, August 1990.

6. In Mexico, the number of lines per 100 inhabitants is 8.8. This figure differs with the average 48.9 lines per hundred inhabitant in OECD countries. See OECD, Communications Outlook, Paris: OECD, June 1994.

7. Based on complaint statistics recently compiled by the Procuraduría Federal del Consumidor (PROFECO) [*the Consumers' Protection Bureau*], 84 per cent of all complaints received by this institution from November 1992 to February 1993 were against TELMEX.

8. Comisión Nacional Bancaria. Banca Múltiple. Quarterly Bulletin. October-December 1993.

9. Andersen Consulting. Bank Cards' Comparative Study. Mexico, D.F., 2 August 1993.

10. EVANS D. and R. SCHMALENSEE *The Economics of the Payment Card Industry*. National Economic Research Associate. 1993.

11. See Credit Card Services. A report on the supply of Credit Card Services in the United Kingdom. The Monopolies & Mergers Commission, 1989, where the Great Britain is concerned; for the United States see Evans and Schmalensee's paper (1993), and Andersen Consulting's paper (1993) for Venezuela, Colombia, Spain, Canada and the United States.

12. BALTO D.: *Access demands and payments systems joint venture*, Federal Trade Commission, 8 April 1994.

13. "Regulatory capture" arguments strengthen this point of view. For several reasons, authorities regulating specific sectors occasionally are "captured" by enterprise/companies (public or private) which operate in these sectors, in the sense that the regulation ends up by protecting companies already established, instead of allowing a competition framework which enables the entry of new participants.

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BEYOND TRADE LIBERALIZATION: DISTRIBUTION AND MARKET ACCESS

Mark Dutz and Sethaut Suthiwart-Narueput[1]

One of the conundrums faced by policy makers in recent years is that after several years of substantial liberalization of tariff and non-tariff barriers retail prices have not been reduced to anticipated levels. This has highlighted a major issue at the interface between international trade and domestic competition policy, namely, the extent to which different barriers to distribution and market access can prevent the convergence of domestic and international prices. Persistent price differentials or violations of the law of one price (LOP) appear to be widespread, both across countries and also within countries. The purpose of this paper, is to evaluate the case for intervention beyond trade liberalization, by examining the methodology for identifying the underlying cause of LOP violations and considering appropriate corrective measures.

What is currently known about LOPs?

In economics, the basic proposition behind LOP is that within a single market identical goods must sell at identical prices. Underlying this proposition is the assumption of arbitrage, namely that market participants have an incentive to buy goods where prices are low and resell them where they are higher. In conditions where there are no barriers to entry, the incentives for resale are exhausted only when prices are equalized. Since international prices are appropriate shadow prices for traded goods in perfectly competitive markets, deviations from LOP will result in efficiency losses. In practice, markets are not perfectly competitive. For an enterprise to be able to use price discrimination to solve its pricing problem, it needs to have a certain degree of market power, the ability to distinguish customers and to prevent resale. In such circumstances, price discrimination is likely. It may even, in some circumstances, be welfare-enhancing. For instance, where one of two markets will not be served if a monopolist was prohibited from charging different prices. For policy makers, the critical question is what types of price discrimination should be discouraged?

In industrialized countries, empirical studies indicate that LOP violations are widespread and significant. Less work has been done in developing countries. However, from the studies which have been undertaken, it would appear that while international trade liberalization has had an impact on domestic prices, important barriers to price equalization remain.

Conceptually, any LOP violation can be broken down into two components, that is, the within-country deviation around the average domestic price, plus the deviation between the average domestic and international price. The difficulty in terms of policy making is that it is not clear which of these

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1. This is a summary of "Competition Issues Beyond Trade Liberalization: Distribution and Domestic Market Access" by Mark Dutz and Suthiwart-Narueput of the World Bank, published in **Regulatory Policies and Reform in Industrializing Countries**, Claudio Frischtak (ed.) (forthcoming).

dimensions is more important in different country settings. In addition, it is necessary to examine the underlying reasons for the LOP violation. It is critical to determine whether lack of price convergence is caused by anti-competitive behaviour or simply by higher costs in a competitive market. As a first step it is possible to categorize LOP violations according to source, into those which are:

(i) induced by public policy (e.g. government regulations affecting the number of distributors, the product range or regional taxation);

(ii) induced by market power (e.g. where dominant enterprises maintain higher prices in particular markets by distribution agreements which foreclose markets);

(iii) induced by other causes (such as the perishability of goods or large cost differences in transportation).

To give such guidelines greater operational significance, further work should be undertaken into the frequency of the practices, the duration of their effects and what the overall magnitude of their impact is upon the market.

Policy Remedies

Once the cause of the violation has been identified and it has been possible to assess the extent to which violations are attributable to a particular source, one can then consider whether there is a case for corrective government intervention. The main areas of interest are those which are induced through government policy and those which are induced through market power. Other factors, such as enterprise sunk cost investment and transportation cost are outside the scope of this paper.

The effects of policy-induced distortions affecting trade or public restraints on competition are relatively well understood. However, in most business environments, there also exist different types of market failures and imperfections. Therefore, policy makers need to analyse carefully the impact of removing existing public restraints on competition to ensure that their removal does not make other distortions more pronounced. In addition it is important to consider how and when public restraints are removed as the method and sequencing of such a removal can have an impact on its success. This can be illustrated by examples of privatization of state-owned distribution companies and the removal of state-granted monopoly rights in distribution. For example, in China the fertilizer industry is protected by quantitative restrictions in the form of import licences, limited foreign exchange and the continued dominance of the state-owned company SINOCHEM. However, even if trade barriers were removed, there would exist a complex web of domestic price controls and cross-subsidization which would prevent international and local price convergence. The removal of these restraints would have to be implemented very carefully to avoid unexpected shortages of fertilizer and unnecessary disruption to the complex integrated system of food prices and urban wages to which they are linked.

Even when public policy distortions are removed, LOP violations may occur as a result of the exercise of market power and anti-competitive behaviour in distribution. In certain instances, private restraints might even manifest themselves more starkly when public restraints are removed. In addition, the weak implementation of competition policy could confer more de facto market power on established firms and induce more LOP violations. Distribution channels can be foreclosed by vertical integration, vertical restraints or other restrictive commercial practices. To assess the desirability for intervention to prevent this from occurring it is necessary to consider:

(i) whether the practice is anti-competitive;

(ii) if so, whether it has efficiency or other beneficial effects;

(iii) if so, whether such effects outweigh the anti-competitive effects: and

(iv) whether the likely benefits of the preferred means of intervention outweigh any costs associated with active policy intervention.

For a more in-depth study of the restrictive practices it is useful to use a classification scheme which examines in more detail the relationship between the upstream producer of the good or "Manufacturer", and the downstream reseller of the good or "Distributor". For the purpose of this exercise, it is helpful to classify the practices according to the target of the restrictive practice in order to assess the potential to restrict the entry or expansion of a manufacturer or distributor.

Upstream restrictions prevent one or more manufacturers from gaining access to a particular distribution channel (e.g. the Distributor is contracted only to handle the Manufacturer's products and not those of his local and foreign competitors). Downstream restrictions, on the other hand prevent one or more distributors from entering an existing market or allow an incumbent firm at that level to be forced out. The Manufacturer may for instance restrict distribution of his product to a single Distributor within a given territory and the Distributor might then be able to prevent other distributors from being supplied by that Manufacturer.

Vertical restraints can be used to enhance market power by facilitating collusion or enabling market foreclosure. A simple observation of prices is generally insufficient to ascertain the anti-competitive nature of the practice. It is more useful to examine the source of market power. First, it must be clear that competition at that level is impeded so that the restrictive practice is capable of having an anti-competitive effect. Restrictive practices by firms with little or no market power are unlikely to harm competition. Second, the firm(s) in question must enjoy some bargaining power in their relationship with enterprises at the other stage. Third, the restrictive practice must allow the firm or firms with market power to maintain or enhance their market power.

It also well known that some anti-competitive practices have efficiency effects but are nevertheless tolerated. For instance where they are necessary to promote investment (e.g. patents), improve distributive efficiency, increase sales, or spur research and development. By preventing other distributors from free-riding they may also encourage the provision of complementary services. Even the deterrent of market entry can have a positive welfare implication if, for example, the profit incentives are likely to generate excessive market entry relative to the social optimum. In such cases, the artificial inflation of costs could deter the unnecessary duplication of fixed entry costs.

Where is Intervention Justified?

Intervention has to be decided on a "rule of reason basis". Clearly, the need for intervention is greater where the anticompetitive effects of the practice are higher. In general, there should be no intervention if sales of the product increase as a result of the practice or if the practice does not raise the costs to potential entrants beyond what would otherwise be the cost of doing business. For downstream restrictions affecting intra-brand competition, intervention is less justified when there is a reasonable amount of inter-brand competition. In cases of upstream restrictions, intervention may be justified where independent entry into distribution is difficult particularly where the fixed costs of entry are relatively great. Intervention is also more warranted if the efficiency effects of restrictive practices are low (e.g. where there is less of a free-rider problem) or, for instance, where exclusionary practices are enforced by implicit threats of foreclosure.

Finally, it is necessary to consider the cost of intervention against what it can realistically achieve. The most positive forms of intervention can change the existing market structure, the prise and access arrangements, whereas ill conceived forms of intervention may have an adverse effect on business investment. The cost of intervention will differ substantially where there already exists a carefully crafted competition law supported by well-functioning investigation, enforcement and adjudication institutions from the case where these laws and institutions are non-existent or weak.

INTERACTIONS BETWEEN TRADE AND COMPETITION POLICIES

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Competition Policy and the Uruguay Round Agreements

As the GATT/WTO Agreements are a "single undertaking", any future agreement introducing competition principles into the system would logically be subject to the new dispute settlement mechanism of WTO. This would go a long way towards making such competition rules binding.

The Agreements of the Uruguay Round Final Act relate to competition policy issues in one way or another, but not in a comprehensive manner.

An important task which remains to be accomplished, if competition principles are to be introduced into the system, is the reconciliation of these Agreements with generally accepted principles of competition; and that is already an immense task, where many international organisations, with their experience in the area of competition, would have an important role to play, in building a consensus among countries and groups of countries (regional groupings) on the major issues.

Let us review some of the main issues.

The Agreement on Trade-Related Investment Measures (TRIMs) provides that these are inconsistent with Art. III (national treatment) and Art. XI (prohibition of quantitative restrictions) of the GATT, as listed in the Annex, (local procurement requirements, export performance, etc.). They are to be eliminated after two years for developed countries, five years for developing countries and seven for least-developed countries. It also provides for consideration, five years later, of whether it should be complemented by provisions on investment and competition. Major TRIMs were enforced by States trying to direct the activities of transnational corporations (TNCs) so as to avoid, inter alia, certain restrictive business practices (RBPs) ; countries abiding by this Agreement should at least have competition legislation and effective enforcement institutions. This is presently not the case for many developing countries, and for all the least developed countries (LDCs), which are presently unable to control RBPs. Furthermore, even in the more advanced newly industrialised countries (NICs) which have recently passed competition legislation, a certain period of training is needed for implementation to become effective: five years will be too short a period for most countries to be ready to face foreign investors once the Agreement comes into force for them.

The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs), Section 8, concerns anticompetitive practices in contractual licenses. It provides for consultations between Governments where there is reason to believe that licensing practices or conditions pertaining to intellectual property rights constitute an abuse of these rights and have an adverse effect on competition. It is stipulated, moreover, that remedies against RBPs imposed by dominant firms in licensing contracts are extremely thin: domestic competition legislation, even if effectively applied might be ineffective when it

comes to counter the new might of technology owners. Further study of the borderline between intellectual property rules and competition rules needs to be undertaken as a matter or urgency.

The revised Anti-dumping Agreement, and the issue of anti-dumping in general is closely related to competition policy, because the rationale in combating "dumping" is that States try to avoid the RBP of "predatory pricing" by enterprises, selling at lower-than-market prices in order to underbid and eliminate competitors, with a view to becoming a monopolist. Hence, the term "dumping" in trade-terminology could be a synonym for "predatory pricing" in competition policy. However, whether in the context of international trade (dumping) or domestic trade (predatory pricing), the practice is treated in a fundamentally different fashion. So much so that while an OECD report on competition argued that predatory pricing was very seldom encountered in real-life, major trading powers (United States, EU in particular) were applying their anti-dumping rules at full steam. However, in the context of Regional groupings, the European Commission does not apply anti-dumping redress against its member-States enterprises, such cases being subject to internal competition rules. The same seems to be true for the Australia-New Zealand Free Trade Agreement (ANZERTA), but not for NAFTA, where an anti-dumping system has been kept although Canada in particular requested that it be replaced by competition control.

As a result, the way dumping is treated in GATT/WTO and predatory pricing in competition policy is different, principles differ, as well as concepts. Moreover, in recent years, antidumping rules have been used in a way which has in effect increased dominant positions and monopolies in domestic markets shielded from outside competition. They may also have served to create export cartels in foreign countries which "voluntarily" restrain their exports to certain markets in order to comply with "undertakings" aimed at avoiding anti-dumping action in importing countries. The new Anti-Dumping Agreement tightens the conditions to be fulfilled for settling anti-dumping proceedings to avoid VERs and OMAs which are cartel like trade - restricting arrangements. However, much remains to be done if one is to reconcile the anti-dumping procedures as they stand now with action against predatory pricing under competition rules. For example, there exist thresholds below which anti-dumping action is not taken: 2 per cent dumping margin or 3 per cent of imports; such thresholds do not make sense in competition terms; the threshold should refer to the relevant market, which is the domestic market plus imports; and in some cases the world market.

The Agreement on Subsidies and Countervailing Duties is also directly relevant to competition policy, as subsidies can distort competition; the European Commission competition rules also cover subsidies.

The Agreement on Safeguards improves competition, as it specifically prohibits recourse to VERs and OMAs, "or similar measures" (such as compulsory import cartels and discretionary export or import licensing schemes) and provides that member countries shall not encourage or support the adoption or maintenance by public or private enterprises of equivalent non-governmental measures (Art. 11.2 and Art. 11.3).

The GATS Agreement contains a few articles dealing with competition issues, however, in a sketchy manner. For example, Article VIII relates to monopolies, aiming to ensure that they act consistently with MFN treatment and that they do not abuse their monopoly position. Art. IX also recognizes that certain RBPs in service sectors can restrain competition and provides for consultations among states in this respect, subject to business confidentiality.

Finally, although not part of the "single undertaking" of the Final Act, the issue of government procurement, which is still under discussion, is directly relevant to competition policy.

Work towards convergence and ultimately merger of competition and trade policies

As can be seen, the results of the Uruguay Round relate to competition issues in numerous ways, and a great deal of work needs to be done immediately to assess the results in terms of competition policy.

As a first step in the direction of converging trade and competition policies, we need to distil basic principles from existing international trade rules and from national competition policies, taking into account the universal trend towards liberalisation. Once these basic principles are elaborated, and consensus is reached, they could be adopted to become part of the GATT/WTO international trading system.

The second step would then be to confront the existing specific WTO Agreements with the basic principles of competition, and where necessary, to propose amendments to the existing WTO Agreements. The basic principles would be used as a prism to assess existing trade rules. As a result of the "single undertaking" in the WTO Agreements, the basic competition principles would be covered by the new WTO Dispute Settlement Mechanism, and they would thus become binding in the same way as the other Agreements of the international trading system.

During the whole process described above, other organisations should have the priority task of providing technical assistance, as well as advisory and training services to all developing countries and other countries in the process of making the transition to a market economy. Such assistance should be provided to both competition policy experts as well as to the trade policy negotiators of these countries.

TRADE AND COMPETITION POLICY

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Introduction

The importance of the linkage between trade and competition policy has been well recognized (Wu and Chu, 1994). The linkage is all the more important when trade and investment among nations become more liberalised. While competition is a dynamic force of change, it may also be a force of concentration. Winners will expand and are likely to use whatever means at their disposal to consolidate their turfs. Trade liberalization without safeguards for fair competition could be in danger of causing increasing concentration in some industries and less competition in the end. Should this be the case, world trade could eventually be eroded for these industries, running contrary to the original intention of GATT negotiations for freer trade. Consequently, the maintenance of competition is not only a supplement to a new world trade order, it should be part of the core, as it is a key to healthy survival of that new order.

The current trade issues are in general concerned more with the interest of national producers than with that of the consumers. By ensuring a competitive environment where producers interact according to fair rules and where the interests of consumers are adequately taken care of, the new world trade order will be more balanced. Many allegations against the abuses by transnational enterprises can meanwhile be resolved or clarified; as a result, the lack of confidence, justifiable or not, in these enterprises is more likely to be replaced by other more positive sentiments.

In the discussion of trade issues such as "dumping" or other forms of "unfair trade practices", attention has been traditionally focused on national interests in the narrow sense. The mere shift of focus from trade to competition policy represents a healthy movement towards the enhancement of national interests as part of the enhancement of global or collective interests. The removal of tariff and other barriers is one step, the redefinition of trade as transactions subject to competition rules would be another giant step forward.

Nations not only need mutual assistance in investigation, but also in taking remedial actions. Since sovereignty will be an issue here, it will not be easy to conclude agreements soon, but steps should be taken towards their conclusion based on the principle of reciprocity and cooperation.

While these reasons are relevant for global cooperation on competition policy, they are particularly important to the Asia-Pacific region. In the region, trade and investment has boomed during the past two to three decades, as the region was enjoying high economic growth rates unseen in the other parts of the world. Many existing multinational business of the industrialized nations moved into the area. The newly

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1. Thanks are due to Dr. Yun-Peng Chu and Dr. Mignon Chan for their assistance and comments.

emerging multinational business of the newly industrializing nations also became active. It seems that the need for a set of codes of international competition is rather real for this part of the world.

Bilateral and trilateral cooperation on competition policy has already started among Asia-Pacific countries. Australia and New Zealand have harmonized their competition laws and policies as part of the ANZCERTA deal. The NAFTA has some provisions regarding cooperation on competition policy. Multilateral cooperation has yet to begin but initiatives are being proposed. In the report of the Eminent Persons Group (EPG) of APEC, it was recommended that APEC "consider adopting a policy based on the existing models of international cooperation on competition policy". (1993, p. 43, Recommendation 6).

When mapping out the Report, EPG undertook very intensive discussions on the subject. In particular, there were concerns over the growing use of anti-dumping measures. That led to the EPG's recommendation in the Second Report (1994) that: "APEC create a task force on anti-dumping and restrictive business practices, to address antidumping practices and the impact of national antitrust laws on international trade with eventual expansion into the broader aspects of competition policy" (p. 21). This has been well received by the APEC ministerial meeting. Competition policy is also very much on the agenda of the Committee on Trade and Investment (CTI of APEC) in Jakarta this year. The CTI recommendation to include competition policy in the 1995 work programme has been approved by the APEC Ministerial Meeting.

However, the problem of trade and competition policies is very complicated and not well known. Some APEC members have not yet promulgated national competition laws. Others, such as the United States, have had competition policies for decades. Therefore, it is worthwhile to look carefully into the linkage between trade and competition policies and initiate discussion among government officials and experts so that international cooperation on trade and competition policy can facilitate trade and investment.

Linkage between Trade and Competition Policy

Tables 1 and 2 present a useful classification of the issues involved in the linkage between trade and competition policy according to the nature of activity involved (i.e. international or domestic with cross-border effects), and according to the party responsible for imposing barriers (i.e. government or private undertakings). Since the aim of competition policy is to regulate anticompetitive conduct of private and (to some extent) public enterprises in order to ensure effective competition, it may sometimes conflict with trade policies which have different goals. We will examine these barriers to competition imposed by government and by private undertakings respectively.

Barriers of Competition imposed by Governments

When barriers are directly or indirectly imposed by governments, through tariffs, non-tariff barriers (NTBs), subsidies or restriction on foreign investment, etc., the competition laws are usually not applicable. This includes international transaction/investment/business-practices, which are to be found in international trade, direct investment in foreign countries, as well as business practices such as horizontal or vertical restraints involving companies from more than one country, hereafter referred to as ITIB. Also included is another kind of activities such as domestic transaction/investment/business-practices with cross-border effects, hereafter referred to as DTIAB. This includes regulations, state monopolies, special privileges, licensing, etc.. The government itself, as an entity making and carrying out public policy decisions, is typically exempt from competition law. Exclusive right to entry and some other privileges granted to public or private undertakings (written into laws by the legislature) are usually beyond the reach of competition laws and their enforcement agencies.

In these cases, trade agreements, to the extent that they lower the barriers to entry, are useful in improving the environment for competition. Here the goal of trade policies is similar to that of competition

policy. For ITIB, actions include the reduction of tariff rates and NTBs. For DTIAB, actions include deregulation or the removal of barriers to entry into domestic industries, which previously might not have been open to any new entrant, domestic or foreign.

In these cases, the optimal policy is to let the trade talks, both bilateral or multilateral, continue, and to let the barriers to entry be further reduced. The result would be freer and fairer trade and investment and a better environment for competition at the same time. Therefore, this will facilitate the growth or trade and investment in the negotiating countries and in the world market as well.

Private dealings in ITIB that impede competition

With regard to private dealings in ITIB, international cooperation in competition policies is definitely called for, in at least three areas:

(i) Whereas trade agreements have removed or lowered many of the barriers to entry imposed by governments and by private enterprises, important private restrictions to competition (usually called restrictive business practices or RBPs in short) may remain unregulated, thus undermining the efforts towards freer and fairer trade. For example, a transnational company with substantial market power may impose territorial restraints along country lines on its dealers in order to enforce price discrimination. Another company which also has market power may coerce its customers in a country into buying exclusively its products by threats of adverse allocation in times of shortage.

In cases like these, the victims usually can file a complaint with a government agency or bring the case to court, if the country in which they reside has a competition law. But what happens if a foreign entity is found guilty? Is the country in question willing to apply its laws to that foreign entity? If yes, does it have the capability to do so? Extraterritoriality is the issue here. This often involves the question of national sovereignty which can lead to international conflicts or frictions. Consequently, international or regional cooperation is needed. Under the ANZCERTA, the problem is eliminated as both competition laws and their enforcement have been harmonized between Australia and New Zealand. Under the EC, the problem is taken care of by the European Commission which reviews all cases that have effects crossing the borders of Member countries.

(ii) Of the restrictive business practices that are currently regulated, some are regulated differently across countries, possibly leading to high uncertainty and cost borne by business. Merger is a good example. Usually cross-country mergers of a size above some minimum standards have to seek approval from all the authorities involved, each of which has a de facto veto power. This can create confusion and uncertainty. International cooperation is needed to reduce the transaction costs.

(iii) When trade talks do deal with abuses by private undertakings across countries, sometimes the penalties are so severe that they may in the end harm competition. Dumping is the most important case in question. In many trade agreements, anti-dumping duties can be imposed as long as the foreign supplier is selling at a price below its home level, and by so doing causing injuries to a domestic competitor. But maybe the foreign supplier is simply participating in a legitimate price competition. This often happens when a new and better technology is introduced and consequently the production cost declines significantly. This will increase competition and benefit consumers. The adoption of anti-dumping measures will evidently interfere with international competition. Here a domestic supplier may be using the anti-dumping procedure as a shield from foreign competition, instead of as a remedy for hostile and illegitimate price predation.

Here, more international cooperation is also needed. One possible way of cooperation is to bring competition issues into trade negotiations, and to modify the anti-dumping agreements accordingly. The GATT, as noted earlier, is doing just that. Another path is to substitute anti-dumping measures by the enforcement of competition laws that are made suitable to handle price predation across borders. However, this requires agreement among contracting parties.

Private dealings in DTIAB that impede competition

For private dealings in DTIAB, competition policies are usually directly applicable while trade policies are usually not. So the burden is on the former to maintain an environment favourable to free competition. Here there are also two possible areas for economic cooperation:

(i) Competition laws may be a barrier to international competition if they give a green light to domestic firms to engage in arrangements that do not restrict domestic, but will restrict international, competition. In the competition laws of many countries, for example, export or import cartels are either approvable under or exempt from competition laws. This is a violation of the principle of national treatment under GATT. We know that export or import cartels are not always anticompetitive, and countries need to get together to review their respective laws, and to revise them if necessary, if all other countries in the group are willing to do the same.

(ii) Competition laws may also be a source of "unfair competition" when the laws and their enforcement are different across countries, or when they are completely absent in others. Countries that have a stringent set of laws and a record of vigorous enforcement may argue that their businesses are subject to more regulation domestically than their counterparts in other countries, and may describe the situation as "unfair". How serious the situation really is is hard to assess. The first step for cooperation could be simply information gathering: to understand the nature of competition laws and their enforcement in different countries, and to make an inventory of the cases that truly occur, etc. If there is truly a problem, perhaps the countries can get together to agree to a few principles that would then be the minimal standard for all countries.

It is reported that competition policies will be included on the agenda in the post-Uruguay Round trade talks under GATT or WTO. It is therefore all the more important to understand the interaction between trade and competition policies and how the global market can be made more open or less as a result of negotiation with respect to competition policies. Agreements which would lower the barriers to trade imposed by governments should be strengthened. Agreements which may unduly hurt competition should be modified. Restrictive business practices in the global market should be effectively regulated through international cooperation on competition policies. Domestic competition laws should not give special permission to practices that affect the foreign, not the domestic market. The nature of competition laws and their enforcement in different countries should not be a source of unfair competition in the international market.

Recommendations

According to the above analysis, international and regional cooperation on trade and competition policy can proceed in the following areas:

With respect to the control of restrictive business practices across borders:

(i) to review existing cases, paying special attention to cases of cross-border abuse of dominant position and cartelization;

(ii) to study the possibility of establishing principles dealing with the extraterritorial application of competition law;

(iii) to study the possibility of establishing principles on cooperation on such matters as consultation, assistance in investigation and in remedial actions;

(iv) to study the possibility of establishing principles on the review procedure and the approval criteria for cross-border mergers.

With respect to trade policies that may have adverse effects on competition:

(i) to review current trade measures which may have adverse effects on competition, paying special attention to the issue of anti-dumping;

(ii) to study the possibility of making recommendations to deal with trade issues, with a view to modifying trade measures that are judged to have had adverse effects on competition, or substituting these measures with cooperation on competition policies.

With respect to possible overlooking of the international market by the competition laws:

(i) to review the clauses and the enforcement of the competition laws to see if they allow practices that do not restrict domestic but that may restrict international trade, paying special attention to export and import cartels;

(ii) to study the possibility of reaching an agreement on modifying existing laws or enforcement practices to remedy such biases reciprocally.

With respect to whether the lack of the competition law or that of its adequate enforcement constitutes a case of unfair trade:

(i) to review existing cases based on the above allegation;

(ii) to collect information on the competition laws and their enforcement;

(iii) to undertake a comparative study on the information and make recommendations.

Table 1. **Interaction between Trade and Competition Policies on International Transaction/Investment/Business-Practices**

Party imposing barriers to competition --- Nature of activities involved	Government		Private undertaking	
	Situation	Examples	Situation	Examples
International (cross-border) transaction/investment/business-practices	1. Competition laws are usually not applicable.		1. Many restrictive business practices are currently not properly regulated. Some countries resort to extraterritorial application of competition laws but this may cause international conflicts. Cooperation in policies is needed.	International cartels, abuse of dominant position
	2. Trade negotiations can lead to freer competition	Reduction in tariff, non-tariff barriers and subsidies	2. Of the restrictive business practices that are currently regulated, they may be regulated differently across countries, leading to conflicts and unduly high risks born by the business.	Transnational mergers
			3. Some cases are handled under trade agreements which, however, may have adverse effects on competition. The system needs to be revised.	Anti-dumping measures

Table 1(cont'd). **Interaction between Trade and Competition Policies on International Transaction/Investment/Business-Practices**

Party imposing barriers to competition --- Nature of activities involved	Government		Private undertaking	
	Situation	Examples	Situation	Examples
Domestic transaction/investment/ business-practices that have cross-border effects	1. Competition laws are usually not applicable		1. Many competition laws allow practices that do not restrict domestic trade but may restrict international trade. These should be modified in accordance with the national treatment principle under GATT, international cooperation is needed.	Export and import cartels
	2. Trade negotiations can lead to freer competition	Deregulation of the domestic market	2. Different contents and enforcement rules of competition laws in different countries may constitute a source of "unfair" international competition. International cooperation is necessary in the exchange of information, the review of cases or, it necessary, the establishment of a set of basic rules.	Domestic concerted actions not properly regulated will block the entry of foreign or other domestic firms to certain markets.

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THE POLITICAL BACKGROUND TO THE ADOPTION OF AN EFFECTIVE COMPETITION LAW - THE BRAZILIAN EXPERIENCE

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The Brazilian competition background

In Brazil, the first attempt to adopt a competition policy was made by the Ministry of Justice in 1945. At that time, industrial development had not yet started and the country's economy was mainly agricultural. Nevertheless, so many political reactions and legal obstacles were raised against the enforcement of the new law that it was soon revoked.

The same Minister made an effort to include an article in the Federal Constitution of 1946 which established that acts and conduct committed as an abuse of economic power would be punished by the law.

It took this constitutional rule five years to be enforced and only in 1951 a criminal law came into effect establishing penal sanctions for breaches of certain restrictive practices provisions. As the country did not have any tradition of prosecuting white collar crime, the law was little enforced.

Later in 1962, a new law was passed which focused on administrative enforcement, identifying the restrictive practices which were forbidden and introducing a merger control system. Private actions for damages were also encouraged.

Under the 1967 Constitution, promulgated during the military regime, the deterrence of abusive economic power was considered a principle of the economic order and any abuse that could lead to a dominant position, restriction of competition or excessive profits was punished.

After the military regime, a new Constitution came into force and free competition was considered a principle of the new economic order. In fact, under Brazilian Constitutional Law, free competition and free enterprise are complementary and both should seek to achieve social justice.

In 1990, a movement towards the liberalization of the economy was initiated and the competition law which had been in effect for nearly 30 years was considered inadequate to deter anti-competitive attacks on the market, which were likely to occur in an open economy. A new law was passed and institutional changes were made to enforce it more vigorously. A Secretariat was created under the authority of the Minister of Justice to investigate the restrictive practices and remit them for trial by CADE, the former competition body, which received the adjudicatory function only. Neither the new law nor the novel institution was successful in changing the pattern of competition enforcement.

In June 1994, another law was passed in the context of a new economic plan. Instead of strengthening the traditional body and making it into a single independent competition agency, a third body, one of the Secretariats of the Minister of Finance, was incorporated in the enforcement system to make it

more complex, costly and time-consuming. Enforcement still remains a problem due to the lack of experts in the three bodies involved in the investigation and control of mergers.

Competition though is not only a matter of efficient enforcement of the law. It is also important that economic policies be consistent with a free market economy.

Competition can be focused on two main aspects: first, on economic policies that can prevent distortions in the market and promote economic development and efficiency; and second, on the legal control of anticompetitive behaviour and concentrated market structures.

Competition policies

Under the first aspect, the State should adopt the correct economic policies to attain the development of competitive structures in the different industrial sectors or inhibit the incentives that move the firms towards oligopolistic structures.

Although Brazil has had a competition legislation for a long time, only recently have the economic policies adopted by the Government not impeded real competition. Until the beginning of this decade, there has been a strong intervention of the State in the economy, not only as an entrepreneur, creating public monopolies to promote economic development but also regulating nearly all industrial sectors of the economy.

The Brazilian model of development was based on concentration and therefore mergers were very much encouraged. It cannot be denied that the system was successful in achieving its aim: the promotion of the significant transformations in the industrial structure of the country rated Brazil in the eighties as the eighth economy in the world.

However, the protective policies adopted to promote the industrial development of the country were maintained for longer than necessary and access to national markets by new competitors was either totally blocked or made difficult by means of high tariffs which made foreign products highly uncompetitive.

Protectionism was partly responsible for the oligopolistic industrial structure in Brazil and the price control system adopted in the country for more than two decades inhibited competition enormously.

The authorities in charge of price control made certain practices official which are forbidden in a free market system. Agreements to fix prices and profit margins among firms were frequent and sometimes prices below those fixed by the Government were not allowed.

In the last decade, the country has gone through many economic plans whose main target has always been to fight inflation. Therefore, agreements among firms in the same industry to freeze prices for a period of time were organized under the supervision of the Government. In the long run, these agreements promoted uniform conduct patterns among competitors and if they succeeded in postponing a higher rate of inflation, they surely did not bring any advantage to consumers who were deprived of the benefits of competition, having to pay uniform prices for the goods they needed, no matter what their quality.

Throughout this period competition law has quite often been tried as a tool to fight price control mechanisms which have failed. This distorted function of the law adopted in the past still makes some authorities and politicians think that competition laws can be used as mechanisms to force firms to cooperate in keeping prices low in order to bring inflation down.

Since 1990, there has been a trend towards deregulation and liberalization of the economy and competition begins to play an important role. Tariffs have been reduced and domestic firms have been exposed to foreign competition and, in the absence of any control, prices have assumed their key function as a guide to productive investments.

Although privatization is also important for competition, it can be very harmful to consumers to substitute private monopolies for public ones. Unfortunately, privatization in Brazil has not had competition as one of its objectives and there has been a high level of concentration in the privatized industries since the main objective of the Government has been the reduction of the role of the State in the economy and the decrease of the public deficit.

A lack of industrial policies in important sectors of the economy has been responsible for the poor performance of certain industries which therefore cannot be open to foreign competition. Such sectors have been producing poor quality goods at a high cost. Instead of vigorous industrial policies aiming at quality and productivity to make Brazilian products competitive in foreign markets, the Government simply grants certain industries tax reductions and tariff protection in exchange for price stability and jobs preservation. The Brazilian car industry can be quoted as an example of such anti-competitive policies.

Reduction or extinction of tariffs for imports of certain goods has been very effective. Brazilian firms are bringing down their costs to compete more vigorously with foreign firms, and as a result consumers are benefitting from lower prices. Nevertheless, caution must be observed to avoid transfer pricing between subsidiaries or between parent and subsidiary, in which case price reductions would not result for the consumer, thus frustrating the aims of a liberal policy in favour of imports.

Bringing down tariffs however is not enough. Inefficient harbour and airport infrastructures can really be a problem to foreign goods and eventually curtail the expected effects of tariff reduction.

The deregulation process initiated at the beginning of the 1990s has been very slow and the effects have not been felt yet. Most rules take into consideration not the public interest but the interest of regulated industries and services and of groups who oppose competition. In the airline service for example, tourist agents who sold to the government were forbidden to give discounts to public bodies and agencies on the quantities of tickets sold. As a result tickets sold to government officials were done so at the tax payer's expense. The main objective of this prohibition was to protect the tourist agents who receive a fixed commission on the sale of each ticket, from which the discount would have to be taken. The case was taken to the Federal Audit Office who said that the discounts were legal and could not be forbidden.

In Brazil, the competition agency does not have the legal power to issue opinions concerning competition in the regulated industries and services. Therefore, regulation which is not necessary and which does not bring any advantage to consumers is still in effect to the benefit of interest groups.

Competition law

Under the second aspect competition laws should be enforced to deter anti-competitive behaviour harmful to competitors, consumers and contrary to public interest.

There is a growing feeling in Brazil that concentrated markets and regulation have worked together against the interest of consumers, resulting in higher prices, limited choice and poor quality. In fact, after the Consumer Code came into force in 1991, Brazilian consumers became very much aware of their rights as citizens and conscious of the value of their money. Firms had to improve the quality of their goods and services because consumers became very demanding and their organisations very active. Following the Brazilian experience one can really say that a consumer-oriented legislation has been responsible for the competition surge in the last four years.

Public prosecutors have been suing regulated industries and local authorities for bad and expensive services and have also initiated civil actions to recover damages for anti-competitive behaviour prejudicial to consumers.

Economic policies have to be addressed in a different way if competition is seen not only as a means to promote the efficient allocation of resources but also as a tool to promote consumer welfare. It may not be so easy for sectorial interest groups to get policies approved which do not bring real gains to consumers. On the other hand, public authorities would be less vulnerable to pressures exercised by such groups.

Government acquisitions, especially in the areas of health, transport and education, will have to look to the interest of the consumer and not only to the interest of the domestic industries or the Government.

Mergers and acquisitions

Merger agreements which contain restrictions or which are potentially anti-competitive must be notified to the competition authority before they are entered into or within 15 days after they are made.

There is a presumption that potential negative effects for competition arise when the merging firms account for 20 per cent of a relevant market or either party had in the previous year net sales of 50 million dollars.

In order to rebut such a presumption, the parties will have to show that the merger is not detrimental to competition. They will have to convince the authorities that they will achieve one or more of the following efficiencies: enhance productivity, improve the quality of goods or services, introduce innovations or promote economic development. Further requirements will then have to be met: the benefits the parties may obtain shall be equitably shared with consumers and the merger shall not affect a substantial part of the relevant market. Moreover, the merger shall be confined to the necessary limits to achieve the objectives aimed at.

In the analysis of each transaction, the agency will take into consideration the efficiencies that the parties want to achieve. There is a combination of legal and economic criteria established by the law.

Mergers which do not substantially affect competition and are proved to be efficient and to result in benefits for the consumer will not be challenged. Therefore joint ventures entered into by the parties to develop new technologies or promote relevant product innovation will probably be approved in spite of increasing the concentration ratio.

An analysis on a case-by-case basis will assess whether the transaction will create or enhance market power to the detriment of competition or whether the restriction is outweighed by benefits to consumers or positive effects on the market.

The Brazilian law is consumer welfare oriented. Therefore the efficiencies aimed at by the parties will be examined under such perspective.

The prime benefit of an integration of firms for the economy as a whole is its potential enhancement of efficiency. This efficiency though must increase competition and result in lower prices for consumers and not only financial gains for the parties. Put in this way the concepts of efficiency and competition are not contradictory and therefore most mergers will not be challenged if the parties can demonstrate that they will achieve the efficiencies aimed at as long as they fulfil the requirements mentioned above.

Anticompetitive behaviour - investigation and trial

The law also lists a wide range of horizontal and vertical restraints that are prohibited. These are only examples of restrictive practices but any other abusive conduct can be caught as long as it has the purpose or effect of achieving market power, deterring competition or obtaining abusive profits.

These practices are examined also on a case-by-case basis under the rule or reason analysis. There is no illegality per se under the new law.

A Secretariat is in charge of the investigation which can be initiated *ex officio* or by representation. The Secretariat has the power to issue cease and desist orders, but the final statement as to the existence of a violation is given by a Council composed of six Councillors and a President, appointed for a mandate of two years which can be extended for two more years.

If the Council finds a violation, the party can be fined and the Prosecutors will take the case to the Federal Court. They will sue for the fine imposed and for an injunction to cease the conduct.

The decisions of the Secretariat are subject to review by the adjudicative agency -- Conselho Administrativo de Defesa Econômica -- CADE. Once CADE has made a final judgement only judicial review is possible.

Enforcement policies

As a consequence of the price control culture, there is no consistent policy in the investigations carried out by the Secretariat. The sectors which are chosen to be investigated are those which appear not to cooperate with governmental policies to curb inflation or those which disobey price regulatory rules.

From 1992 to 1994, the Secretariat opened 211 investigations charging companies with excessive profits and only 71 cartel investigations were opened when it is widely known in the country that the firms still use the price lists that were used when price control was enforced.

Within this context, the pharmaceutical industry was responsible for 107 investigations. Many of the cases alleged making up products to circumvent price control. The cement industry was also investigated for tying arrangements and cartel behaviour.

These investigations have been carried out for nearly two years and have not so far reached the adjudicative body. One cannot therefore say whether there was really anticompetitive behaviour or whether it was just an attempt to recover prices frozen during the control period.

The adjudicative body in Brazil - CADE - is an independent agency whose decisions are reviewed only by the Judiciary. It is not subject to the influence and pressure of political decisions and can carry out its functions with autonomy. However, with the exception of the expertise of its seven members (six Councillors and a President), the agency lacks experts and well-trained personnel.

Even so CADE has had an important role since 1992 and has gained a lot of credibility due to the accuracy and transparency of its decisions and its ability to separate price control and regulatory issues from anti-competitive behaviour, refusing to apply the competition law in support of failing price control mechanisms.

Since 1992, CADE has decided 25 cases of restrictive practices. In thirteen of them, the firms were found guilty of anti-competitive conduct and had to pay fines which varied from US$ 130 000 to

US$ 1 000 000. In twelve cases, no abusive conduct was found in the behaviour of the firms investigated. In four cases, CADE found that the evidence was not conclusive and ordered further investigation.

The Council also issued its opinion in three consultations which were submitted to them regarding potentially anti-competitive behaviour.

After June 1994, the Council approved the power to approve or disapprove mergers and agreements which are examined by the Secretariat. Since then the Council has challenged one monopoly in the sector of synthetic fibres, ordering divestment, and has disapproved a case of pre-merger notification in the cement sector.

Conclusions

Structural arrangements in some sectors of the Brazilian economy will certainly have to be made and one cannot expect this to occur overnight. There are strong pressure groups which want to maintain the status quo. In fact, competition law in Brazil is seen by most production trade associations as an instrument to curb free enterprise. The country has no competition culture and the main concern of the economic authorities is to fight inflation. With this objective in mind many disastrous economic plans were tried in the last ten years which completely ignored competition and market forces. In such a context, high prices are seen not to be the result of lack of the play of competitive forces in the market but as artificial profit made by industries which do not want to cooperate with the Government in the policies to fight inflation.

The latest economic plan however seems to be based on different principles from the former ones. Prices are free and it seems that the real causes of inflation are being fought. Nevertheless little has been done in terms of competition. Although the Government seems to rely on market forces to make Brazilian industry more competitive, the abolition of tariffs has been very slow and firms are taking too long to adapt their cost structures and margins so that their products can compete with foreign goods.

The culture of price control however is present in the new law, which introduced a peculiar definition of abusive price. Power was given to a Secretariat of the Ministry of Finance to summon the firms to justify price increases. In case they do not satisfy the Ministry of Finance authorities with arguments that they might consider plausible, an investigation shall be initiated aimed at punishing the firm for abusive prices.

A new Government is taking power in the next month. It is important that competition policies are adopted together with other policies which may be established to keep inflation low, reduce the national debt and keep the State out of the markets of goods and services. There are promises in the liberalisation of the oil monopoly, telecommunications and electricity.

The privatization programme is said to be one of the priorities the new Government but care should be taken so that inefficient private monopolies, detrimental to the consumers, do not take over from the public ones. And here it is important that the Government does not surrender to pressure groups: those who look forward to private monopolies and the corporations of the public entities who want to maintain their privileges no matter law high the cost imposed on the tax payer.

Competition should really be the soul of the business and the policies introduced by the new Government should allow for market mechanisms to operate as fully as possible to achieve the efficient allocation of resources and improve consumer welfare.

SUBSTANTIVE PROVISIONS OF KOREA'S COMPETITION LAW

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Introduction

Various problems associated with heavy government intervention and the resulting market distortions in the 1960s and 1970s, coupled with the aftermath of the second oil crisis, prompted a reassessment of the past performance of the Korean economy and led to the general consensus that in the coming decades, the economy should be run by the unfettered functioning of market mechanisms. As the first major step in this direction, the Monopoly Regulation and Fair Trade Act (hereafter, the "Fair Trade Act" or the "Act") was enacted in December 1980 on the initiative of the Economic Planning Board. The enactment of the Act set comprehensive new "rules of the game" of the market -namely, free and fair competition. Therefore, this Act signified a fundamental change in government - business relations and was regarded as the economic constitution for a new era.

Although the Act was prepared with reference to many corresponding statutes of advanced market economies, especially those of the United States, Japan and Germany, two important Korea-specific issues appeared when the Act was being drafted.

First, the general principle of allowing the market mechanism to determine prices could not be upheld unless the market structure was competitive. Since the majority of Korean product markets at the time were monopolistic or oligopolistic in structure and price stabilization was regarded as the most pressing economic goal, this Act prohibited undue pricing activities of market dominating firms.

The second issue was whether or not the Fair Trade Act should be used as a legal justification for a direct attack on the concentration of economic power. Despite many different opinions that existed when the draft of the Act was under consideration, most believed that the chaebol (Korea's conglomerate business groups) issue should be somehow addressed. This was taken up in Article 1 of the Act, which identifies the prevention of "excessive concentration of economic power" as one of the purposes of the law. The amendments of the Act in 1986, 1990 and 1992 addressed this purpose to some extent.

Outline of the substantive provisions of Korea's competition law[1]

> The Article 1 of the Fair Trade Act states that:
> "This Act, by prohibiting abuse of market dominating power by business concerns and excessive concentration of economic power and by controlling undue collaborative activities and unfair trade practices, shall be aimed at encouraging fair and free competition, thereby stimulating creative business activities and protecting consumers as well as promoting a balanced development of the national economy".[2]

The Fair Trade Act was first amended in 1986 in order to reinforce the measures for mitigating the concentration of economic power, inter alia. In 1990, the Fair Trade Act was amended again in an

effort to strengthen the competition policy of the government. The third amendment of the Act in 1992 strengthened measures for mitigating economic power concentration as well as for making enforcement of the Act more effective.

With these three amendments, the provisions of the current Fair Trade Act forbid the abuse of a market dominant position, restrict business integration which would cause substantial injury to competition, prohibit holding companies and intercompany cross-ownership within a big business group, limit equity investments and loan guarantees of big business groups, forbid collusive activities, prohibit unfair business practices, and restrict unfair international business contracts.

The fourth amendment of the Act has been proposed this year and the draft bill is now submitted to the National Assembly for its enactment. The proposed bill includes among others; first, changes in the restrictions on unfair international contracts; second, strengthening the remedies against violations of the law; and third, changes in the restrictions on total equity investments of big business groups.

Prohibition of abuse of market dominant position

The Fair Trade Act forbids the abuse of a market dominant position. The market dominant position of a firm (or a business concern) refers to the situation in which either the market share of the largest firm is greater than 50 per cent or the combined share of the top three firms is greater than 75 per cent (one with less than 10 per cent shall be excluded from this sum). This provision applies to the markets with gross domestic supply totalling more than 50 billion Korean won in the previous year. The Fair Trade Commission annually designates the market dominating firms according to these criteria.[3]

The following activities of the market dominating firms are prohibited by the Act, as they constitute the abuse of a market dominant position: unreasonably determining, maintaining or altering the price of a commodity or the charge for services rendered; unreasonably controlling the sale of commodities or rendering of services; unreasonably interfering with the business activities of other business concerns; unfairly hindering the entry of new competitors; and disrupting the marketplace by substantially restricting competition or damaging the interest of consumers.

Restrictions on combination of enterprises

The Act restricts business integration by firms whose equity capital exceeds five billion won or whose total assets exceed 20 billion won, if such act causes substantial injury to competition in any line of commerce. If the Fair Trade Commission deems it necessary, exceptions may be granted, upon a close examination by the Commission, for business integrations aimed at rationalization or strengthening the international competitiveness of an industry.

A unique characteristic of the Act is that, in addition to the typical methods of business integration such as stock or asset acquisition, mergers and interlocking directorates, the Act treats the establishment of new enterprises as a method of business integration. This is a response to the fact that many more firms were newly established than merged in the rapidly growing Korean economy.

Repression of economic power concentration

In addition to the restrictions on anti-competitive business integrations, the Act also provides for several specific measures to mitigate the concentration of economic power, which include prohibition of establishing holding companies, prohibition of direct cross-ownership within a designated large business group,[4] restriction on the total amount of capital investment in other firms by the designated large business groups, and restriction on the voting rights of finance or insurance companies. As mentioned previously, all these provisions to combat or mitigate the concentration of economic power were introduced in the first amendment of the Act in 1986 and strengthened in the second amendment in 1990.

Among the provisions to mitigate the concentration of economic power by chaebol, capital investment regulation has been the most important. This regulation prohibits a company within a big business group from making an equity investment in other domestic companies in excess of 40 per cent of the investing company's net assets.[5]

The third amendment in 1992 added another restriction on big business groups. Member companies of the big business groups are now prohibited from offering guarantees on loans to financial institutions on behalf of other member companies in the same business group that exceed 200 per cent of the shareholders' equity. This figure of 200 per cent of the equity capital has been a ceiling for mutual loan guarantees since April 1993, though an interim period is allowed until April 1996.

Restrictions on undue collaborative activities

The Act prohibits any undue collaborative activities of firms, or cartels, which would substantially restrict competition in any line of commerce. The types of prohibited collusive activities include cartels on prices, sales conditions, production and sales quotas, customers and market areas, production facilities and equipment, specializations and joint ventures for collective management.[6]

However, the Fair Trade Commission can authorize, only exceptionally, cartels deemed necessary for achieving rationalization, overcoming cyclical recessions, facilitating industrial restructuring, enhancing competitive strength of small and medium-sized firms, and rationalizing terms of transactions.[7]

Prohibition of unfair trade practices

The Act prohibits unfair business practices, which include unreasonable refusal to deal or unreasonable discrimination of price and other terms of trade, unreasonable elimination of competitors, unreasonable inducement or coercion of the competitors' customers, unreasonable use of one's bargaining position in dealing with its trade partners, unreasonable restriction on terms and conditions of trade, and false, deceptive and misleading representation or advertising.

The types of and criteria for each of these unfair trade practices are determined and announced publicly by the Fair Trade Commission. In doing so, the Commission classifies the unfair trade practices applicable to all industries and those applicable only to particular industries or particular activities. If it is necessary for preventing any violations of the provision on unfair trade practices, the Commission may determine and announce publicly the guidelines to be observed by business concerns.[8]

Trade associations

The Act expands the same set of restrictions on undue collaborative activities and unfair business practices to trade associations and their member firms. In addition, the trade associations are prohibited from restricting the present or future number of members, unreasonably restricting members' business activities, and causing members to commit unfair trade practices and resale price maintenance.

Prohibition of resale price maintenance

The Act prohibits resale price maintenance. Exemption is provided however, for publications specified under the Copyright Act. In addition, the prohibition may not be applied to commodities which meet the following conditions: *(1)* their qualities can be easily recognized as being identical; *(2)* they are daily use by the general consumers; and *(3)* free competition prevails in their markets.

Restrictions on international contracts

The Act covers international agreements or contracts between Korean firms and their foreign counterparts, insofar as their undue collaborative activities, unfair business practices and resale price maintenance are concerned. The types of international contracts subject to review by the Fair Trade Commission include technology inducement agreements, copyright inducement agreements, and import agency agreements.[9]

Other provisions

All these legal provisions as listed above constitute the main elements of the Monopoly Regulation and Fair Trade Act, while the rest of the provisions in the Act are devoted to the establishment and organization of the Fair Trade Commission, the investigation procedures of the Commission, compensation for damages, exemptions from the Act, punitive provisions, supplementary provisions, and addenda.

These policy directions of the Fair Trade Act are manifested in greater detail and completed to some extent by the Enforcement Decree of the Act and other various regulations and rules which come under the titles of Rules, Guidelines, and Types and Standards, etc., and usually take the form of public notification or the Commission's manual.

The Act on fair subcontract trade

Another part of the Korean competition law is found in the Act on Fair Subcontract Trade of 1984 (hereafter, the "Subcontract Act"), which is also administered by the Fair Trade Commission. The Subcontract Act, incorporating and strengthening the related provisions of individual laws, was legislated to guarantee fair transactions, especially between large-order-placing prime contractors and small and medium-sized subcontractors, and to protect the subcontractors from possible unfair practices of the prime contractors in manufacturing and construction industries.

Overview of competition policy experience

Fourteen years have passed since the Fair Trade Act was introduced in 1980. The adoption of this new competition law in Korea was a natural response to the constricting environment brought about by the government-led economic system in the 1960s and 1970s. The competition law as accompanied by similar measures in the 1980s and 1990s to enhance the market function, such as import liberalization, privatization and, most important, deregulation. All these policy changes have been essential elements of Korean competition policy in its broader sense, and the basic principle underlying these changes was that the economy could be better run by the free market mechanism.

At the core of these changes has been the Fair Trade Act, as the Act purports to promote "fair and free competition", while other liberalization measures have performed the role of laying the basic groundwork for a well-functioning market mechanism. The policies in the past decade are deemed to have contributed significantly to transferring the government-led, heavily regulated economy of the past into today's freer market economy with greater emphasis on the autonomy and creativeness of the private sector. Competition policies initiated in the early 1980s also have contributed to preparing Korea for the international, bilateral or multilateral, trade talks for freer trade and investment which have started in the latter half of the 1980s and are still going on.

Deregulation toward workable competition

The introduction and enforcement of the Fair Trade Act and the implementation of such policy measures as deregulation, privatization and import liberalisation have made competition in many markets

"more workable".[10] This has been possible because these policy efforts of the Korean government have spread the then unfamiliar idea of free and fair competition to all sectors of the economy. Today, the importance of free and fair competition is advocated not only by general consumers but also by many entrepreneurs and government ministries other than the competition authority. It is also important to note that the trade, industrial and financial policy instruments of the 1960s and 1970s have been modified to better conform to the principle of free and fair competition.

Competitive market structure

Efforts have been made to make many markets more structurally competitive, through designation and regulation of the market dominating firms, restrictions on anti-competitive business integrations, import liberalization of the market dominating products and deregulation. These efforts, together with the overall expansion of the Korean industries and the resulting increase in the number of firms, contributed to improving the monopolistic structure of many markets. The evidence shows that the share (in number) of the "competitive markets" (for which the three-firm concentration ratio in terms of the shipment value is below 50 per cent) had increased from 26.1 per cent in 1981 to 35.2 per cent in 1987 and 36.3 per cent in 1990. Although the statistics show that the number of market dominating firms had shot up from 102 firms producing 42 commodities in 1981 to 332 firms producing 140 commodities in 1994, this increase is mainly due to the fact that the designation criteria for the market dominating firms and commodities have changed only slightly while most of the markets have expanded considerably.[11]

These efforts toward a more competitive market structure have been accompanied by the Korean government's commitment to deal with the economic power concentration by big business groups. The Korean conglomerates have been another important structural factor threatening meaningful competition in many markets. The first amendment of the Fair Trade Act in 1986, which introduced restrictions on inter-company equity investment within each big business group, has contributed to mitigating the concentration of economic power by the big business groups and improving their financial structure. The evidence shows that the share of the business groups in mining and manufacturing sector decreased from 40.2 per cent in 1985 to 35.7 per cent in 1992 (in terms of the shipment value).

Fair and free competition

The efforts against undue collaborative activities and unfair business practices have contributed significantly to augmenting people's recognition of free and fair competition and also improving the business firms' mode of conduct. For restrictive business practices which have violated the Fair Trade Act, correction orders and warnings have been issued. Surcharges have been imposed and complaints filed with the Attorney General for criminal prosecution when necessary. A particular emphasis has been placed upon monitoring and regulating unfair business practices of certain types and in certain industries, including those of department stores, bargain sales, free gift offers, etc. In addition, the enforcement of the Subcontract Act has contributed to reducing unfair subcontracts and protecting the subcontractors from unfair subcontracting practices.

Law enforcement activities

The competition law experience in the past can also be summarized in terms of the corrective measures taken by the government in enforcing the law. From 1981 to the end of 1993, the Commission took as many as 5 844 corrective measures. Statistics show that the majority of the actions were warnings, correction orders and recommendations for correction. Warnings have been issued in 4 175 cases and most of them have been for delayed reports or as an early warning against possible violations.

Types of corrective measures by types of violations: 1981-1993

Classification	Measure					
	Complaint	Surcharge	Correction order	Recommendation for Correction	Warning	Total
Abuses of Market Dominant Positions	-	-	11	3	5	19
Mergers & Acquisitions	1	-	2	-	367	370
Economic Power Concentration	2	15	30	8	61	116
Undue Collaborative Activities	1	3	25	27	54	110
Unfair Trade Practices	13	33	714	550	1 408	2 718
Unfair International Agreements	-	-	-	68	2 138	2 206
Prohibited Activities of Trade Associations	9	-	123	31	42	305
Total	26	51	905	687	4 175	5 844

Note: Includes resale price maintenance.
Source: *Kongjungkeorae Nyunbo*, Fair Trade Commission, 1994.

Scope and coverage of Korea's competition law

Scope of the Fair Trade Act

As compared with the subject matter of competition laws in other countries, which usually deal with such forms of behaviour as horizontal and vertical arrangements, joint ventures, mergers and acquisitions and the abuse of a dominant position or monopolization, Korea's competition law is broader in its scope.

In addition to these, the Fair Trade Act also deals with various types of unfair trade practices which include non-price vertical arrangements, anti-competitive elements of international contracts, and undue collaborative activities and unfair trade practices of trade associations. As pointed out earlier, the Act's provisions to cope with the problems associated with the economic power concentration by big business groups constitute an important and Korea-peculiar element of competition law. In addition, the Subcontract Act is also administered by the Fair Trade Commission, and can be regarded as a part of Korea's competition framework.[12]

Coverage of the Fair Trade Act

According to Article 2 of the Fair Trade Act, the industrial sectors subject to the Act are: *(1)* manufacturing, *(2)* electricity, gas and water supply, *(3)* construction, *(4)* wholesale and retail services, *(5)* lodging restaurants, *(6)* transportation, warehousing and communication services, *(7)* banking and insurance service, *(8)* real estate, leasing and business services, *(9)* educational services, and so on. The Act does not apply to the agricultural, fishery and mining sectors.

Exemptions

Article 58 of the Fair Trade Act states; "the provisions of this Act shall not apply to any act performed by a business concern or a trade association which is justified according to other laws or any orders issued under those laws". For example, the exercise of intellectual property rights pursuant to the Copyright Law, Patent Law, Utility Model Law, Design Law or Trademark Law are exempted from the application of the Fair Trade Act. Certain activities carried out by trade associations temporarily established for the purpose of mutual support among small businesses or consumers are also exempted.

However, the exemption issue is in reality much more complicated than what one can see from the above examples. First of all, it is by no means clear what Article 58 is all about, especially the meaning of the word "justified". More serious are the customary exemptions that are found in regulated industries, public enterprises, financial sector and so on.

Banks, for example, have been largely exempt from Korea's competition law enforcement, though they are now subject to expanded enforcement. It was not until very recently that the Fair Trade Commission began to apply the Act to some of the public enterprises. Exemptions of regulated industries from the application of the Fair Trade Act have also been widespread.

In fact, it is important to note that the issue of exemption from the application of competition law in Korea leads us to the evolving interaction between deregulation, privatization and competition policies.

Interaction between deregulation, privatization and competition policies: Lessons from the Korean experience

Both deregulation and privatization have great significance for competition policy. When an economy is managed by heavy government regulations and when public enterprises account for a high portion of production, competition law and policy cannot meaningfully govern the economy. Regulated industries and public enterprises are all different forms of government intervention and are usually exempt from competition law even where it exists.

Exemption of regulated industries and public enterprises from competition law in fact highlights the evolving interaction between industrial and competition policies along the path of economic development. Since regulations, public enterprises and competition policy are all acts of the same government, priority should be determined and exemption of one from the other is inevitable whenever there exist conflicts among different sets of policies. It is an important role of the government to decide which to exempt.

The Korean experience with government regulations and public enterprises shows that the interaction between industrial and competition policies has evolved into what it is today, as the Korean government kept modifying its development strategy according to the changing stages of industrialisation. Thus, the driving forces behind any changes in the interaction come from the structural changes occurring in the economy. A wise government is the one which timely optimizes the interaction in order to further accelerate economic development. We note that there is no universally accepted rule for the interaction between different economic policies, since the interaction itself is a policy choice.

Another lesson from the Korean experience is that a distinction should be made between the traditional scope for competition policy and its broader definition. It is important to note that deregulation and privatization are themselves important competition policies. If competition policy is meant to promote competition, then deregulation and privatisation are the most powerful tools to do so since they eliminate those sectors which are shielded from competition in an economy tainted with anti-competitive regulations and public monopolies. Thus, we observe that deregulation and privatisation pave the way for subsequent active competition law enforcement in its traditional form.

It is equally important, however, for the government to make efforts to apply competition law to regulated industries and public monopolies and reduce those areas exempted from competition law. This is particularly true, because deregulation and privatization cannot be completed with just one round of policy shifting. Korea is no exception in this regard, and during the last several years, the Fair Trade Commission has been trying to expand its application of the Fair Trade Act to regulated sectors and public monopolies. The Fair Trade Commission has been expanding the application of Article 63 of the Act, which requires any government body to consult with the Commission before introducing anti-competitive regulations. The Commission's present review of numerous laws and ordinances is also part of the deregulation efforts.

A comment should be made about the interaction between deregulation and privatization. In many cases, the monopoly position of public enterprises is maintained via government regulation, and privatization itself can mean a switch from a public monopoly into a private monopoly. Thus, privatization may not enhance efficiency as much as we expected if it is not accompanied by deregulation. It is important to note the complementarity between these two policy options; one enhances the internal efficiency of public enterprises and the other improves the market environment external to the firm.

Per se illegality and rule of reason

The distinction between *per se* offences and those treated on a rule of reason basis is often difficult to make in the case of Korea's Fair Trade Act. If we stick to what the legal provisions state literally, we can say that the abuse of a market dominant position and resale price maintenance are per se violations of the Act, while combination of enterprises (mergers and acquisitions, etc.) undue collaborative activities (cartels) and unfair trade practices are treated on a rule of reason basis.

The argument that the rule of reason applies to cartels and unfair trade practices is based on such clauses in their respective provisions as "... which substantially restrain competition in any line of commerce", or "... which is deemed detrimental to fair trade". The rule of reason approach indeed applies to the case of mergers and acquisitions, because exceptions may be granted, upon close examination by the Commission, for business integrations aimed at rationalization or strengthening the international competitiveness of an industry.

However, it is not fair to say that cartels and unfair trade practices have been treated on a rule of reason basis in Korea. Although the provision restricting undue collaborative activities prohibits cartels "which would substantially restrain competition in any line of commerce", cartels are nonetheless regarded as *per se* violations and exemptions are only given to those authorized by the Fair Trade Commission.

Unfair trade practices, especially those associated with non-price vertical restraints, were traditionally treated as *per se* offences, although the provision prohibiting them includes the clause,"detrimental to fair trade". We note that in 1992, the Fair Trade Commission explicitly announced its policy change of adopting the rule of reason for such vertical restraints as sales quotas, territorial restrictions and refusal to deal. The Commission found it necessary to conduct an economic analysis of the pro-competitive effects of inter-band competition vis-a-vis the restraint of intra-brand competition.

The argument that the abuse of a market dominant position is a *per se* offence is another example of the ambiguity inherent in the distinction between *per se* offences and rule of reason treatment, because the types of practices regarded as an abuse of a market dominant position are all described in such terms as "unreasonable", "unfairly", "unduly" or "substantially restricting competition".

Notes

1. For a more detailed explanation of the Fair Trade Act, see Report on Developments in Korea in Competition Policy in OECD countries 1992-1993, p. 333, OECD, Paris, 1995.

2. The policy objective cannot be fully achieved when the market activities are managed or controlled by government interventions. Thus, such liberalization measures as deregulation, privatization and inducement of foreign competition also constitute important elements of Korean competition policy and complement the Fair Trade Act in achieving its goal.

3. In 1994, 332 firms in 140 markets were designated by the Fair Trade Commission as market dominating firms.

4. The Fair Commission annually designates 30 largest business groups (in terms of total assets) and their member companies, in accordance with the provisions of the Enforcement Decree of the Act.

5. The proposed amendment of the Act, now submitted to the National Assembly for enactment, is to strengthen the present equity investment regulation by lowering the ceiling of 40 per cent down to 25 per cent. Exemptions from this regulation, however, are to be broadened, according to the draft bill, to include investments in SOC and the so-called core companies of each business group.

6. There are eight types of undue collaborative activities specified in the Act as violations when they substantially restrict competition.

   (1) deciding, maintaining or altering prices;

   (2) determining the terms and conditions for the sale of commodities or for rendering services, or payment of prices and charges thereof;

   (3) restricting production, delivery, transportation or sales of commodities or rendering of services;

   (4) restricting the sales territory of trade or customers;

   (5) hindering or restricting new establishment, expansion of facilities or installation of equipment for production of commodities or rendering of services;

   (6) restricting the kinds or sizes of commodities at the time of production or sale thereof;

   (7) establishing a company, etc., to carry on jointly or manage main sectors of business; and

   (8) hindering or restricting business details or activities of other business concerns.

7. The Enforcement Decree specifies the requirements for approving collaborative activity for *(1)* rationalisation of industry, *(2)* research and technological development, *(3)* overcoming a depression, *(4)* industrial restructuring, *(5)* improvement of the competitiveness of small and medium enterprises, *(6)* rationalization of the terms and condition of trade. The requirements thus work as minimum conditions that have to be satisfied when the Fair Trade Commission authorizes a cartel. The Enforcement Decree also specifies certain limitations on the authorization of cartels.

8. In the case of false, deceptive and misleading representation or advertisement, firms or their trade associations may introduce and apply a code called 'Fair Competition Code', which is up to the review and approval of the Fair Trade Commission.

9. The Enforcement Decree sets certain minimum standards of the notification requirement for each type of international agreement or contract. According to the proposed amendment of the Act, the notification requirement is to be totally abolished and instead, a review system based on voluntary requests is to be introduced. Thus, if a contracting firm requests that the Fair Trade Commission examine the legality of the contract, then the Commission is to review it.

10. Deregulation in Korea began in 1988 and the new administration inaugurated in 1993 has given top policy priority to a full-fledged deregulation. There were three rounds of privatization from the late 1960s until the late 1980s, and the new administration has embarked upon the fourth round of privatisation which, compared with the previous ones, is much larger in scale and more committed to pursuing the efficiency gains we normally expect from privatization.

11. The Enforcement Decree of the Fair Trade Act in 1993 following the third amendment of the Act in 1992 included the change in market size criterion to determine market dominance from "gross domestic supply of 30 billion won" to "50 billion won".

12. While consumer protection is one of the goals of the Fair Trade Act, it is also the subject matter of the Act on Consumer Protection, and is administered by the Consumer Protection Board which is affiliated with the Economic Planning Board.

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