

CITATIONS:**Bluebook 22nd ed.**

A. E. Rodriguez & Malcolm B. Coate, Limits to Antitrust Policy for Reforming Economies, 18 Hous. J. Int'l L. 311 (1996).

ALWD 7th ed.

A. E. Rodriguez & Malcolm B. Coate, Limits to Antitrust Policy for Reforming Economies, 18 Hous. J. Int'l L. 311 (1996).

APA 7th ed.

Rodriguez, A. E., & Coate, M. B. (1996). Limits to antitrust policy for reforming economies. Houston Journal of International Law, 18(2), 311-358.

Chicago 18th ed.

Rodriguez, A. E., and Coate, Malcolm B. "Limits to Antitrust Policy for Reforming Economies." Houston Journal of International Law 18, no. 2 (1996): 311-358. HeinOnline.

McGill Guide 10th ed.

A. E. Rodriguez & Malcolm B. Coate, "Limits to Antitrust Policy for Reforming Economies" (1996) 18:2 Hous J Int'l L 311.

AGLC 4th ed.

A. E. Rodriguez and Malcolm B. Coate, 'Limits to Antitrust Policy for Reforming Economies' (1996) 18(2) Houston Journal of International Law 311

MLA 9th ed.

Rodriguez, A. E., and Malcolm B. Coate. "Limits to Antitrust Policy for Reforming Economies." Houston Journal of International Law, vol. 18, no. 2, Winter 1996, pp. 311-358. HeinOnline.

OSCOLA 5th ed.

A. E. Rodriguez & Malcolm B. Coate, 'Limits to Antitrust Policy for Reforming Economies' (1996) 18 Hous J Int'l L 311 Export To:

Date Downloaded: Sat Sep 5 15:09:52 2026

Source: <https://access.heinonline.com/HOL/Page?handle=hein.journals/hujil18&id=321>

Terms, Conditions & Use of PDF Document:

Please note, citations are provided as a general guideline. Users should consult their preferred citation format's style manual for proper formatting. Your use of this HeinOnline PDF indicates your acceptance of William S. Hein & Co., Inc. and HeinOnline's Terms & Conditions: <https://help.heinonline.com/kb/terms-conditions/>. The search text of this PDF is generated from uncorrected OCR text. To obtain permission to use this article beyond the scope of your license, please use: <https://www.copyright.com>.

Please note: citations are provided as a general guideline. Users should consult their preferred citation format's style manual for proper citation formatting.

HOUSTON JOURNAL OF INTERNATIONAL LAW

VOLUME 18

WINTER 1996

NUMBER 2

LIMITS TO ANTITRUST POLICY FOR REFORMING ECONOMIES

A.E. Rodriguez
Malcolm B. Coate†

TABLE OF CONTENTS

I.	INTRODUCTION	312
II.	ISSUES IN ANTITRUST IN DEVELOPING ECONOMIES	317
A.	<i>An Overview of the Literature</i>	318
B.	<i>Background on Recent Antitrust Reforms</i> .	322
C.	<i>Recent Legislation</i>	326
1.	<i>Latin America</i>	326
2.	<i>Eastern Europe</i>	327
D.	<i>Demand and Supply for Antitrust Legisla- tion</i>	333

† Dr. A.E. Rodriguez is a Senior Economist in the Federal Trade Commission's Bureau of Economics. Ph.D. 1991, University of Texas; B.S. Ch.E. 1981, University of Texas. Dr. Malcolm B. Coate is a Deputy Assistant Director for Antitrust in the Federal Trade Commission's Bureau of Economics. Ph.D. 1980, Duke University; M.A. 1988, Duke University; B.S. 1977, College of William and Mary. The analyses and conclusions presented here are those of the authors' and do not necessarily represent the views of the Federal Trade Commission, any individual Commissioner, or the official position of any Commission Bureau. An earlier version of this paper was presented at the 1995 ASSA Conference Panel on Competition Policies in Emerging Market Economies sponsored by the Industrial Organization Society. James Zinser, John Barton, Barry Freeman, Mark Williams, Mark Dutz, Laura MacCleery, and Eva Almirantearena graciously offered useful comments.

III.	EFFECTS OF ANTITRUST ON INVESTMENT INCENTIVES	338
IV.	EFFECTS OF ANTITRUST ON COMPLEX CONTRACT . .	345
A.	<i>The Commitment Problem</i>	346
B.	<i>The Model</i>	351
1.	<i>Vertical Agreements</i>	352
2.	<i>Horizontal Agreements</i>	355
V.	CONCLUDING COMMENTS	357

ABSTRACT

In reforming economies antitrust policy has been advanced as a legal mechanism to safeguard developing markets from anticompetitive practices. Antitrust legislation adopted or proposed in a number of these countries has largely been modeled on current antitrust policies in developed nations. Due to special considerations affecting developing economies not observed in the developed world, strict enforcement of antitrust policy may have unintended negative consequences for pro-market programs.

We advance two interrelated arguments. First, we caution that vigorous antitrust enforcement may retard economic development due to its unintended effects on private market incentives. Active antitrust enforcement, we argue, often reduces incentives for firms to invest in a reforming economy. Second, we show how active antitrust policies may have adverse effects on the ability of firms to enter into long-term contracts. Excessive antitrust scrutiny may hinder growth by distorting the development of efficient contractual arrangements. We conclude that antitrust policies adopted in reforming economies should be strictly limited in scope.

I. INTRODUCTION

In recent years, a number of countries opened previously closed or state dominated economies to competition by introducing market-based reforms, while simultaneously adopting legislative measures designed to create, advance and protect a

market economy.¹ Governments revised or adopted competition legislation² as a complement to the privatization, restructuring, and deregulation policy measures.³ Since the collapse of the former Soviet Union, multilateral lending institutions and the antitrust agencies of developed countries have actively collaborated in the formulation and implementation of these antitrust programs.⁴

1. See generally Roger W. Mastalir, *Regulation of Competition in the "New" Free Markets of Eastern Europe: A Comparative Study of Antitrust Laws in Poland, Hungary, Czech and Slovak Republics, and Their Models*, 19 N.C. J. INT'L L. & COM. REG. 61 (1993) (examining the recent efforts made by many Central and Eastern European countries to institute market economies).

2. "[C]ompetition law (also referred to as antitrust or anti-monopoly law) which seeks to prevent anti-competitive business practices by firms and unnecessary government intervention in the market place." R. Shyam Khemani & Mark A. Dutz, *The Instruments of Competition Policy and Their Relevance for Economic Development*, in REGULATORY POLICIES AND REFORM IN INDUSTRIALIZING COUNTRIES (Claudio R. Frischtak ed., forthcoming 1995) (unpublished manuscript at 1, on file with the authors).

3. See generally James Langenfeld & Marcia W. Blitzer, *Is Competition Policy the Last Thing Central and Eastern Europe Need?*, 6 AM. U. J. INT'L L. & POL'Y 347 (1991) (examining the importance of competition legislation in economic reform in various countries around the world); Malcolm B. Coate et al., *Antitrust in Latin America: Regulating Government and Business*, 24 U. MIAMI INTER-AM. L. REV. 37 (1992) [hereinafter Coate et al., *Antitrust in Latin America*] (analyzing Latin American countries' antitrust policies employed in economic reforms). Earlier attempts to develop competition policies have been less successful. For example, in 1980, the United Nations (UN) General Assembly adopted a worldwide antitrust code which condemned cartel practices and called on each nation to legislate against them. Joel Davidow, *The Relevance of Antimonopoly Policy for Developing Countries*, 37 ANTITRUST BULL. 277, 278 (1992). This relatively unsuccessful initiative included the creation of a UN unit to provide technical assistance. *Id.*

4. See Mastalir, *supra* note 1, at 62-65. The World Bank, the U.S. Federal Trade Commission (FTC), the Antitrust Division of the U.S. Department of Justice, the German Federal Cartel Office, the Organization for Economic Cooperation and Development (OECD), and others have actively advocated the establishment of antitrust agencies and continue to provide assistance. See Kathleen E. McDermott, *U.S. Officials Provide Competition Counseling to Eastern Europe*, ANTITRUST, Fall/Winter 1991, at 4 (detailing the assistance provided by the U.S. and other countries to emerging Eastern European democracies in their transformation to market economies). Antitrust practitioners and scholars have advocated inclusion of antitrust policy as a recommended component of World Bank development policy or as an integral measure of liberalization programs. See Roger A. Boner, *Competition Policy and Institutions in Reforming Economies*, in REGULATORY POLICY AND REFORM: A COMPARATIVE PERSPECTIVE (Claudio R. Frischtak ed., forthcoming 1996) (unpublished manuscript, on file with the authors); Ralph Bradburd & David R. Ross, *Regulation and Deregulation in In-*

In this article, we argue that implementing an active anti-trust policy may be a premature step for reforming economies.⁵ The benefits of privatization may not be automatic, but may be dependent on the regulatory and competitive environment in which the newly privatized firms operate.⁶ Given its potentially significant influence on the post-reform competitive environment, the introduction of an active antitrust policy in reforming economies may run counter to the objectives of market liberalization.

Antitrust policy should have one goal: to define and enforce the competitive rules of the game. Antitrust regulations foster competition by supporting allocative efficiency with market-based pricing, rather than monopoly pricing, thereby preventing

dustrialized Countries: Some Lessons for LDCs (1990) (unpublished manuscript, on file with the authors); Khemani & Dutz, *supra* note 2, manuscript at 1-2; R. Shyam Khemani, The Administration of Competition Law and Policy in Transition Economies: The Case of Russia 2 (1994) (unpublished manuscript, on file with the authors) (paper presented at the Southern Economic Association Annual Conference, 1994); William E. Kovacic & Robert S. Thorpe, *Antitrust Law for a Transition Economy*, LEGAL TIMES, Aug. 2, 1993, at 41, 42 [hereinafter Kovacic & Thorpe, *Transition Economy*]; William E. Kovacic & Robert S. Thorpe, Antitrust and the Evolution of a Market Economy in Mongolia (Dec. 1994) (unpublished manuscript, on file with the authors) (paper presented at the 1995 American Economic Association meetings) (examining multiple competition laws enacted in Central and Eastern Europe and their abilities to discourage monopolies); Russell Pittman, *Some Critical Provisions in the Antimonopoly Laws of Central and Eastern Europe*, 26 INT'L LAW. 485, 487 (1992) [hereinafter Pittman, *Critical Provisions*]; F.M. SCHERER, COMPETITION POLICIES FOR AN INTEGRATED WORLD ECONOMY 41-42 (1994); Robert D. Willig, *Anti-Monopoly Policies and Institutions, in THE EMERGENCE OF MARKET ECONOMIES IN EASTERN EUROPE* 187 (Christopher Clague & Gordon C. Rausser eds., 1992); Clive S. Gray, *Antitrust as a Component of Policy Reform: What Relevance for Economic Development?*, in REFORMING ECONOMIC SYSTEMS IN DEVELOPING COUNTRIES (Dwight H. Perkins & Michael Roemer eds., 1991).

5. We use the term "reforms" or "reforming economies" synonymously with liberalization, privatization, or deregulation. Strictly speaking, these terms all reflect the return of property rights from government to private persons. For example, elimination of currency controls is a reinstatement of the right to alienate one's property. Privatization is a transfer of rights for which the recipient pays some transaction price. Both are examples of reforms.

6. See Brian Levy & Pablo T. Spiller, Regulation, Institutions, and Commitment in Telecommunications: A Comparative Analysis of Five Country Studies 25-27 & tbl. 3 (May 3-4, 1993) (unpublished manuscript, on file with the authors) (paper presented at the World Bank's Annual Bank Conference on Development Economies, 1993) (examining the effects of various developing countries' telecommunications antitrust provisions on their economies).

welfare losses due to anticompetitive behavior.⁷ Focused antitrust policy encourages investment by providing rules that define boundaries of competitive conduct and thus inspire confidence in the stability of the business environment.⁸ However, antitrust policy rarely remains focused.⁹ Theories evolve to determine whether various unilateral competitive actions are a form of "predation,"¹⁰ or whether particular vertical agreements

7. See Robert H. Lande, *Wealth Transfers as the Original and Primary Concern of Antitrust: The Efficiency Interpretation Challenged*, 34 HASTINGS L.J. 65, 72-74 (1982). Allocative efficiency as an antitrust standard has attained its preeminence with most mainstream economists only over the last two decades. *Id.* at 73. The U.S. Supreme Court explicitly addressed the economic grounding of antitrust in the mid-1970s. See ROBERT H. BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* 5, 8 (1978) (describing the Court's treatment of antitrust policy and the evolution of the Court's antitrust precedents). In a series of decisions, the Court tended to limit antitrust precedents so that conduct that served consumers was not unlawful. See generally *id.* However, it was not until the Reagan Administration that the enforcement agencies specifically tended to promote economic efficiency goals by protecting consumer welfare. See generally *id.*; Richard A. Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. CHI. L. REV. 6 (1981) (stating that "[t]he Supreme Court's standard for evaluating the legality of restricted distribution has oscillated from the Rule of Reason to per se illegality and back.").

8. Michael S. Jacobs, *The New Sophistication in Antitrust*, 79 MINN. L. REV. 1, 28 (1994); see also Herbert Hovenkamp, *Antitrust Policy After Chicago*, 84 MICH. L. REV. 213, 267-68 (1985) (stating that "antitrust laws can encourage efficient investment by protecting firms from strategic, inefficient advantage-taking by others").

9. We are hard pressed to find a better characterization of wayward antitrust decisions than the one advanced in Judge Bork's classic tome:

It would be overhasty to say that the *Brown Shoe* opinion is the worst antitrust essay ever written. The connoisseur of bad antitrust opinions must take into account *Fortner Enterprises I*, *Utah Pie*, *Sealy*, *Schwinn*, *Proctor & Gamble*, *Von's Grocery*, and many others, to cite only some of the most recent cases. Still, all things considered, *Brown Shoe* has claim to the title. It is not merely a bad case, it is also a trend setter—as if the poems of E. A. Guest had determined the course of modern literature.

BORK, *supra* note 7, at 210.

10. An example of predation is a strategy whereby a firm initially lowers its price such that no profit is being produced thus driving rivals out of business and scaring off potential entrants. When rivals exit, the predator now has a virtual monopoly, the firm raises its price. See Frank H. Easterbrook, *Predatory Strategies and Counterstrategies*, 48 U. CHI. L. REV. 263, 267-69 (1981) [hereinafter Easterbrook, *Predatory Strategies*; see also Janusz A. Ordover & Garth Saloner, *Predation, Monopolization, and Antitrust*, in 1 HANDBOOK OF INDUSTRIAL ORGANIZATION 537, 590-92 (Richard Schmalensee & Robert D. Willig eds., 1990) (dealing with a game-theoretic approach to analyzing predatory behavior). Like

are "facilitating" collusion. While these theories may have merit in certain circumstances, they may also hinder competitively neutral or procompetitive conduct. Thus, activist policy may adversely affect investment in developing economies.

Two approaches to evaluating the impact of active antitrust measures on developing economies are addressed in this article. First, enforcement may focus on successful firms which typically earn high returns (dominance based antitrust paradigm).¹¹ By targeting business success, this approach tends to reduce the returns to risk taking and innovation. Thus, the naive focus on short-run allocative efficiency may adversely affect the long-run investment needs of reforming economies.

Second, antitrust policy may fail to properly assess the efficiency benefits of contractual arrangements designed to minimize the likelihood of opportunistic behavior. We observe that activist policy generally tends to reduce the acceptable contracting horizons for firms wary of potential hold-up problems. Therefore, aggressive antitrust enforcement could limit acceptable contracting horizons and reduce the total number of

all game theory analyses, however, the results of predation models are sensitive to their underlying assumptions. *Id.*

Although it evolved along an often confused and tortuous road, current antitrust policy generally recognizes that vertical integration and vertical restrictions, such as exclusive distributorships, are not necessarily anticompetitive. See Posner, *supra* note 7, at 6-8. "Restricted distribution" refers to a marketing system in which the manufacturer places restrictions on competition between distributors or dealers who provide goods either to lower links in the chain of distribution or to the ultimate consumer. *Id.* at 6. This conventional vertical treatment of restraints and mergers in particular has recently come under attack by a group of economists claiming to advance a "Post-Chicago" approach to the treatment of vertical issues. See generally Michael H. Riordan & Steven C. Salop, *Evaluating Vertical Mergers: A Post-Chicago Approach*, 63 ANTITRUST L.J. 513, 515 (1995) (noting that while vertical mergers can be beneficial to market efficiency, such mergers can also raise concerns as to anticompetitive foreclosure, exchange of information, and evasion of regulation). These "Post-Chicago" views, in turn, have come under criticism by two FTC economists, David Reiffen and Michael Vita. See David Reiffen & Michael Vita, *Comment: Is There New Thinking on Vertical Mergers?*, 63 ANTITRUST L.J. 917, 919 (1995) (claiming that Riordan and Salop employ "a faulty analogy between vertical and horizontal mergers and would lead to systematic enforcement errors").

11. Coate et al., *Antitrust in Latin America*, *supra* note 3, at 53. Dominance theory condemns behavior as illegal only if a firm dominant in the area of trade performs the behavior and the behavior injures a protected group of consumers or business associates. *Id.*

contracts. This reduction in the number of contracts is likely to be detrimental to investment.¹²

The general theme of this article is that in analyzing arrangements between firms in reforming economies we should presume innocence. Truly effective market reforms require a recognition of institutional situations particular to reforming economies. Overlooking the special conditions prevalent in transition economies reduces the benefits of reform. Antitrust, with its predisposition to allege anticompetitive behavior, may be unable to discern legitimate efficiency gains. Overall, it is distinctly possible that extremely narrow antitrust policies may be optimal for the early stages of a country's development.

To set the background for the analysis, part II discusses a number of topical issues in the relatively novel field of antitrust in reforming economies. The reader may choose to skim these preliminary comments and begin reading the main arguments in parts III and IV. Part III contains a general overview of dynamic investment issues associated with an activist antitrust policy, and various adverse effects of such activism are discussed. Part IV applies a formal model and concludes that certain forms of antitrust scrutiny will impact negatively on a firm's incentives to contract. Lastly, we offer some concluding commentary.

II. ISSUES IN ANTITRUST IN DEVELOPING ECONOMIES

We commence the discussion by providing a brief review of the relatively sparse literature on the topic of antitrust in developing economies. Despite some reservations, it appears that the idea of antitrust or competition laws in developing countries boasts the general support of numerous well-known scholars, experienced practitioners, and sundry antitrust ex-

12. These are not the only instances in which the activities of competition agencies can distort the development of efficient systems of contract law. See generally Phyllis Altrogge, *Competition Policy in Agriculture and Food Processing: Some Lessons for Transforming Economies*, 18 WORLD COMPETITION L. & ECON. REV. 71 (1994) (examining the tendency among some competition agencies in reforming market economies to view contractual arrangements as creating market power, especially when one party appears to have greater bargaining power than the other). By taking the position that contractual arrangements create market power, competition agencies risk becoming mediators in ordinary commercial conflicts, and thus may indirectly jeopardize the development of an efficient system of contracts. *Id.*

perts.¹³ Thus, it comes as no surprise that antitrust policy has gained nearly universal acceptance.

An examination of actual legislation, published work, and other resources reveals that the efficiency-based antitrust paradigm appears to be the favored standard for antitrust theory in developing economies and is explicitly present in most legislation. However, the European Union's (EU's) concept of dominance is also present in several recent laws.¹⁴ Enforcement guided by the concept of dominance may, under certain conditions, contradict the efficiency-based standard. This dual approach to enforcement is described in section B. In section C, we present a brief review of recent legislation that it incorporates both enforcement concepts. Our discussion also compares and contrasts the laws in Latin America and Eastern Europe. Finally, section D advances some preliminary discussion on the determinants of antitrust legislation. Although the arguments as a whole are somewhat speculative, the analysis is intended to lay the groundwork for a possible deeper inquiry.

A. *An Overview of the Literature*

While the implications of antitrust policy remain a topic of heated debate, the idea of a regime of antitrust laws and policy in reforming economies has gained nearly universal acceptance. Recommendations by antitrust agencies and other commentators have largely reflected the current antitrust thinking in western countries.¹⁵ For example, an Assistant Attorney General for Antitrust has explicitly recommended that the reforming countries adopt "an antitrust framework along the lines of those

13. See, e.g., Langenfeld & Blitzer, *supra* note 3, at 350 (citing such noted scholars as M. HINDS, ISSUES IN THE INTRODUCTION OF MARKET FORCES IN EASTERN EUROPEAN SOCIALIST ECONOMIES 100 (1991); R. RAHN & R. UTT, THE NATIONAL CHAMBER FOUNDATION, REPORT OF THE BULGARIAN ECONOMIC GROWTH AND TRANSITION PROJECT ch. 2, at 8, ch. 4, at 18 (1990)). The authors list the basic elements of reform crucial for a successful transition to a free-market economy. *Id.* The list includes such phenomena as price liberalization, privatization, banking and fiscal reform; which, in conjunction with strong antitrust policy, are critical to the implementation of successful economic reform. *Id.*

14. See, e.g., Coate et al., *Antitrust in America*, *supra* note 3, at 50 & tbl. 1 (comparing the antitrust policies of 20 Latin American nations, among whom the concept of dominance is clearly manifested in six of the countries' antitrust policies).

15. See generally *supra* note 4 and accompanying text.

that have evolved in the United States and other OECD member countries as being the best way of securing and preserving competitive markets."¹⁶ Similarly, the Chairman of the FTC described antitrust as "largely an American-made product" and "one of her country's most successful exports."¹⁷ A noted economist and past antitrust regulator has stated that "[w]hile the fundamental importance and difficulties of these steps cannot be overstated, it would, nevertheless, be a serious error to omit anti-monopoly policy from the list of free-market essentials or to leave for last as an afterthought."¹⁸ Moreover, antitrust forms an important aspect of the recently negotiated North American Free Trade Agreement (NAFTA) between the U.S., Mexico, and Canada.¹⁹

Other commentators are more restrained. The *1991 Economic Report of the President* noted, "A basic antitrust law aimed at preventing cartel behavior by firms producing the same product and mergers that create monopoly is essential."²⁰ However, one commentator has raised two concerns linked to the applicability of antitrust policy for reforming economies.²¹ The first concerns the novelty of antitrust issues. Many countries have no antitrust tradition comparable to the decades-long U.S. heritage,²² thus possessing no coherent or relatively pre-

16. James F. Rill, *Competition Policy and Economic Efficiency: Providing the Framework*, in COMPETITION AND ECONOMIC DEVELOPMENT 59, 59 (Kurt Stockmann & Louis Emmerij eds., 1991).

17. *America's Antitrust Diaspora: Trustbusters, Inc.*, ECONOMIST, Nov. 9, 1991, at 84.

18. Willig, *supra* note 4, at 190.

19. See The North American Free Trade Agreement, Dec. 17, 1993, arts. 1501 & 1502, 32 I.L.M. 605, 663-64 [hereinafter NAFTA].

20. 1991 ECONOMIC REPORT OF THE PRESIDENT 210 (transmitted to the Congress, Feb. 1991).

21. See generally Joshua A. Newberg, *Mexico's New Economic Competition Law: Toward the Development of a Mexican Law of Antitrust*, 31 COLUM. J. TRANSNAT'L L. 587 (1994) (analyzing the contents, limitations, exemptions, and uncertainties within Mexico's Economic Competition Law).

22. See *id.* at 608. There are a number of idiosyncratic elements that may preclude American antitrust learning from functioning as effectively in different settings as they have in the United States. See William S. Comanor, *Antitrust in a Political Environment*, 27 ANTITRUST BULL. 733, 734-36 (1982) (arguing that to a large extent two sets of interests, the distrust of corporate power and the search for corporate legitimacy, provide the critical support for American antitrust laws). A deep historical distrust of corporate or business power or at times bigness itself is reflected in the antitrust laws of the United States. *Id.* at 734-35. Of course, the decentralization of decision making, the dispersion of

dictable modes of legal analysis for antitrust cases.²³ A second concern arises from the legal conventions of civil law systems. Historically, in contrast to the common law system, civil case law retains no precedential value.²⁴ Similarly, the ability of judges and administrative agencies to comment on or influence the development of legal doctrines is circumscribed.²⁵

A few authors oppose antitrust in reforming economies.²⁶

economic power, and the avoidance of political interference may lay equal claim to guiding policy as legitimate social objectives. See Robert Pitofsky, *The Political Content of Antitrust*, 22 CORP. PRAC. COMMENTATOR 1 (1980) (discussing noneconomic concerns that should influence antitrust laws and why noneconomic concerns are vital to effective antitrust policy).

23. Coate et al., *Antitrust in Latin America*, *supra* note 3, at 51-52 (discussing the difficulty of implementing antitrust legislation in countries without well functioning legal institutions); see also Newburg, *supra* note 21, at 608. This highlights the danger of what one might call the "transferability problem." See Peter H. Schuck & Robert E. Litan, *Regulatory Reform in the Third World: The Case of Peru*, 4 YALE J. REG. 51, 53 (1986) (recounting the "chastening attempt" to develop a program of regulatory policy in Peru). It neglects the cultural, institutional, and political obstacles to the implementation of an antitrust policy. See Spencer W. Waller, *Neo-Realism and the International Harmonization of Law: Lessons from Antitrust*, 42 KAN. L. REV. 557, 563 (1994) [hereinafter Waller, *Neo-Realism*].

24. JOHN H. MERRYMAN, *THE CIVIL LAW TRADITION* 46-47 (2d ed. 1985) (stating that the orthodox civil law view is that no court is bound by another court's decision, while in reality cases are cited by civil law lawyers and judges in arguing and deciding cases).

25. For several papers addressing economic analysis in civil law countries and raising concerns similar to those discussed by Newburg, *supra* note 21, at 606, see generally 11 INT'L REV. L. & ECON. (1991). Another commentator argues that neither the transfer of existing national laws nor the international harmonization of competition law offers any realistic prospect for the desired outcomes. Waller, *Neo-Realism*, *supra* note 23, at 603. U.S. antitrust law represents an unique social and historical construct of events and themes that may not be easily grafted into a foreign legal setting. *Id.* Thus, antitrust enforcement may be significantly more difficult for reforming economies. *Id.*

26. There is, of course, abundant literature criticizing antitrust in developed economies. *E.g.*, Lester C. Thurow, *Let's Abolish the Antitrust Laws*, N.Y. TIMES, Oct. 19, 1980, at C2 (arguing that the U.S. economy can no longer afford a legal system with antitrust laws). We can think of no reason why these criticisms would not apply to antitrust in developing economies. Ernest Gellhorn, *Distinguished Alumni Lecture - Regulatory Reform and the Federal Trade Commission's Antitrust Jurisdiction*, 49 TENN. L. REV. 471, 489 (1982) (analyzing the role of the FTC and enforcement of antitrust laws and concluding that the problems with antitrust regulation relate more to the actual antitrust policies than to any other source); Abigail McWilliams et al., *Antitrust Policy and Mergers: The Wealth Effects of Supreme Court Decisions*, 31 ECON. INQUIRY 517, 517 (1993) (measuring the impact of antimerger enforcement and finding that antitrust

Paul Godek, echoing classical objections to antitrust policy, has observed that most reforming economies are so relatively small that many relevant product markets cross national boundaries.²⁷ Within the broader markets, competitive forces ensure price discipline.²⁸ Accordingly, active antitrust enforcement is not necessary.²⁹ From another perspective, A.E. Rodriguez and

policy was binding during the 1960s and 1970s by lowering the value of targets in uncontested ongoing mergers; specifically examined was the impact and "ripple effect" which Supreme Court antitrust decisions created); Malcolm Coate et al., *Bureaucracy and Politics in FTC Merger Challenges*, 33 J.L. & ECON. 463, 468 (1990) (noting how political considerations impact merger enforcement and act as a public and private antitakeover devices).

27. Paul E. Godek, *One U.S. Export Eastern Europe Does Not Need*, 15 CATO REV. BUS. & GOV. 20, 20-21 (1992). For earlier contributors who offer this recommendation, see Michael Shefer, *Guidelines for Legislation on Monopolies and Restrictive Practices in Small Economies*, 15 ANTITRUST BULL. 781, 793 (1970); S.C. Littlechild, *Myths and Merger Policy*, in MERGERS AND MERGER POLICY 301, 306 (James Fairburn & John Kay eds., 1989). For a general criticism of antitrust, see DOMINICK T. ARMENTANO, ANTITRUST AND MONOPOLY: ANATOMY OF A POLICY FAILURE (1992) (rejecting virtually all antitrust enforcement); DONALD DEWEY, THE ANTITRUST EXPERIENCE IN AMERICA (1990); Thurow, *supra* note 26, at C2.

28. The influence of entry on economic performance has long been recognized by economic theory. See Harold Demsetz, *Barriers to Entry*, 72 AM. ECON. REV. 47, 47 (1982). Any excessive industry profitability that exists under the umbrella of protectionist policy cannot persist once new competitors are allowed entry. See *id.* at 49, 52. Entry should cause prices to fall to competitive levels. See *id.* at 52. Anticipation of entry may also exert sufficient pressure on market prices as competitors recognize the threat. Markets vulnerable to anticipated entry are known as contestable markets. See WILLIAM J. BAUMOL ET AL., CONTESTABLE MARKETS AND THE THEORY OF INDUSTRY STRUCTURE 4 (1982) (discussing contestable markets in practice).

29. Several authors argue that antitrust is appropriate in the case of goods and services for which no trade exists. ROGER A. BONER & REINALD KRUEGER, THE BASICS OF ANTITRUST POLICY: A REVIEW OF TEN NATIONS AND THE EUROPEAN COMMUNITIES 20 (World Bank Technical Paper No. 160, 1991) (stating that in areas affecting national rather than international trade markets anticompetitive laws are necessary). Due to substantial transportation costs, prospective imports could result in more expensive products than found domestically. See generally Demsetz, *supra* note 28 (discussing the influence of entry on economic performance). In addition, some goods and services, tradeable for the most part, on occasion do not trade due to subsidies, tariffs, or nontariff barriers to trade. See, e.g., Richard Blackhurst, *Trade Policy Is Competition Policy*, in COMPETITION AND ECONOMIC DEVELOPMENT 253 (Kurt Stockmann & Louis Emmerij eds., 1991); Emil Friberg & Celia Thomas, *Is Antitrust Obsolete?*, 25 J. ECON. ISSUES 617, 618 (1991) (stating that in addition to tariff barriers many goods and services have only a local or national market because of high transportation costs or, if a service, suffer from the cultural familiarity and

Mark D. Williams note that rent-seeking practices will tend to offset the benefits of an active antitrust policy.³⁰ Thus, reformers should focus on creating government institutions to thwart rent-seeking before moving to create an active antitrust regime.

Although some objections to active antitrust have been noted, antitrust law appears to have become an accepted policy tool in developing countries.³¹ The general practice so far appears to have been to transplant developed-world antitrust traditions into reforming economies.³² Indeed, in a number of cases, antitrust legislation incorporates legal standards from both the EU and the United States.³³ Unfortunately, these are not fully compatible and combining the different approaches may result in contradictory policies.

B. Background on Recent Antitrust Reforms

Recent antitrust laws adopted by reforming economies share the objectives of antitrust legislation in the United States, the EU, and most other western antitrust systems.³⁴ As a first approximation, antitrust laws seek to maintain the allocative efficiency of a competitive marketplace through provisions which prohibit certain forms of private conduct.³⁵

proximity problems). However, although some markets may be local, they may still not be immune from entry. For example, one commentator observes entry is often easy into service markets. Godek, *supra* note 27, at 20–21. Another notes that competition from foreign producers highlights the inefficiencies created by excessive regulation. Blackhurst, *supra*, at 254.

30. A.E. Rodriguez & Mark D. Williams, *The Effectiveness of Proposed Antitrust Programs for Developing Countries*, N.C. J. INT'L L. & COM. REG. 209, 214 (1994).

31. See Coate et al., *Antitrust in Latin America*, *supra* note 3, at 40; Waller, *Neo-Realism*, *supra* note 23, at 559 (discussing an international blueprint for antitrust law).

32. Waller, *Neo-Realism*, *supra* note 23, at 569 (discussing the work done by the American legal establishment and governmental institutions to develop American-style antitrust systems).

33. *Id.* at 570.

34. See *id.* at 569 (discussing the transferability of antitrust law).

35. Some critics claim that antitrust is another form of governmental regulation. See, e.g., BORK, *supra* note 7, at 7, 407 (explaining how many regulatory schemes allow antitrust to flourish within the gaps in the legislation). Judge Bork states, "[T]he protectionist, anticompetitive strain in the law has undergone a spectacular acceleration, bringing to pass . . . the 'crisis in antitrust.'" *Id.* at 417. There is some truth to Judge Bork's claim. The enforcement of the antitrust laws usually proceeds through indirect means of settlement rather than

A competitive market economy seeks to benefit consumers and promote the free flow of goods and services.³⁶ In general, markets present buyers with a choice of goods and services from independently acting suppliers. Naturally, if buyers had but one choice firms could price supracompetitively. In other words, with no potential or actual competitors to restrain them, a sole producer could restrict output and raise prices above cost.³⁷ However, given sufficient choice, buyers can purchase the most desirable products at the most attractive prices.³⁸ Such market-place decisions force suppliers to reduce their product prices to their costs.³⁹ In this way, the market provides a highly flexible system that is intended to assure that the price paid for a product reflects the true cost of resources to society.⁴⁰

The rationale for industry cartels—agreements among rivals to restrict output and raise prices—flows from the competition model.⁴¹ Recall that a single firm (a monopolist) could increase its total revenues by restricting output and raising prices. Firms in a competitive environment will quickly realize that they also can increase profits by taking the same action collectively.⁴² This behavior would deprive consumers of two major benefits of a competitive market: lower prices and increased output. Not surprisingly, the U.S. Congress sought to outlaw such conduct under the Sherman Act of 1890.⁴³ Likewise, the EU outlawed

enforcement of laws in court. For an empirical model that supports this conclusion, see Malcolm B. Coate et al., *Fight, Fold or Settle?: Modelling the Reaction to FTC Merger Challenges*, ECON. INQUIRY, Oct. 1995, at 537.

36. See Demsetz, *supra* note 28, at 52.

37. It is unclear if even this result holds in durable goods markets. See R.H. Coase, *Durability and Monopoly*, 15 J.L. & ECON. 143, 149 (1972) (arguing that in some circumstances, the competitive outcome may be achieved even if there is but a single supplier).

38. See Langenfeld & Blitzer, *supra* note 3, at 347–48 (discussing the effect competition has on pricing).

39. See Easterbrook, *Predatory Strategies*, *supra* note 10, at 277.

40. *Id.*

41. See ERNEST GELLHORN & WILLIAM E. KOVACIC, ANTITRUST LAW AND ECONOMICS 13–41 (1994).

42. See Coate et al., *Antitrust in Latin America*, *supra* note 3, at 47 (discussing price fixing).

43. The following contain the substantive provisions of the U.S. antitrust law: The Sherman Act, 15 U.S.C. §§ 1–7 (1994); The Clayton Act, 15 U.S.C. §§ 12, 13, 14–19, 20, 21, 22–27 (1994); 15 U.S.C. §§ 41–58 (1994) (creating the FTC). Together these acts lay out the basic framework of U.S. antitrust policy.

agreements among competitors in Article 85 of the Treaty Establishing the European Community (EC Treaty).⁴⁴

Allocative efficiency is not the only guiding principle of antitrust policy in the developed world. In the United States, for example, a second goal exists: to achieve an organization of industry that is as fragmented as possible in order to ensure, despite higher costs and prices, the survival of small firms.⁴⁵ In this context, antitrust policy serves to protect competitors and not competition. We should note that recent decisions appear to have been decided so as to promote consumer welfare.⁴⁶ Therefore, the efficiency standard tends to dominate the atomistic competition standard.⁴⁷ However, it is still possible to spot cases and enforcement initiatives that protect competitors instead of competition.⁴⁸

44. TREATY ESTABLISHING THE EUROPEAN COMMUNITY [EC TREATY] art. 85.

45. Lande, *supra* note 7, at 139 n.285; Alan A. Fisher & Robert H. Lande, *Efficiency Considerations and Merger Enforcement*, 71 CAL. L. REV. 1580, 1588 (1983).

46. Langenfeld & Blitzer, *supra* note 3, at 352.

47. *Id.* at 353. Operationally, an allocative efficiency standard suggests the following normative guidelines: Interventions should be limited to output-restricting transactions; competitive analysis begins by assuming that markets work well; business acts efficiently; and government intervention is pernicious. *See generally* Lande, *supra* note 7, at 86 (discussing Congress' goals in enacting antitrust laws).

48. Langenfeld & Blitzer, *supra* note 3, at 353 (describing how many governments have reconsidered their initial focus on dominance theory and have deemphasized this in favor of the protection of competitors); *see also* Donald I. Baker, *Reagan Administration Proposal Opens Debate on Treble Damages*, NAT'L L.J., May 9, 1983, at 22 n.20 (citing *Albrecht v. Herald Co.*, 390 U.S. 145 (1968), and *Utah Pie Co. v. Continental Baking Co.*, 386 U.S. 685 (1967)). To be sure, certain remaining rules of U.S. antitrust policy are clearly *not* grounded on an allocative efficiency standard. Langenfeld & Blitzer, *supra* note 3, at 367. These include the *per se* rule against resale price-making agreements, the rule against concerted refusals to deal (also known as group boycotts), and the modified *per se* rule against tying by firms with market power. *Id.* at 369. However, legal interpretations have evolved to the point where the treatment appears to reflect the influence of economic criteria which inevitably infuse an allocative efficiency flavor. Coate et al., *Antitrust in Latin America*, *supra* note 3, at 73.

Despite the *per se* proscription against its practice, current enforcement policy at least implicitly recognizes the efficiency rationales for resale price maintenance. *See The Reuters Financial Daybook*, REUTERS DAYBOOK, Nov. 1, 1995, available in LEXIS, News Library, US File, at *1 (describing an FTC hearing involving antitrust enforcement, efficiencies, and mergers as part of a series of hearings on global competition and the boom in innovation-driven

The EC Treaty's Article 86 embodies a dominance concept similar to the U.S. fragmentation goal.⁴⁹ Abuse of a dominant position, under this definition, generally includes any conduct which injures consumers or competitors, even if it is the type of conduct which would be lawful if done by a firm without a dominant position.⁵⁰ In a number of plausible enforcement scenarios, antitrust authorities in the EU can challenge perceived abuses of dominant positions against competitors.⁵¹ Such challenges may reduce legitimate pro-competitive efficiencies. Spencer W. Waller explains this apparent inconsistency by noting that the EU model differs dramatically from the U.S. system because it is derived from a fundamentally different premise.⁵² EU competition law must be understood in the context of the need to break down the national boundaries between member states and to complete the unification of the common market.⁵³ Dominance regulations tend to protect nondominant firms from aggressive and abusive competition when markets are opened to international competition.⁵⁴ Moreover, it limits the ability of large firms, especially those associated with particular countries, to protect their position from competition.⁵⁵ In effect, a dominance policy serves the political goal of consolidating interstate economic integration. However,

industries). In a similar vein, group refusals to deal, such as vertical dealing exclusivity arrangements, may have different purposes or may serve some public policy goal and are not condemned uniformly. Langenfeld & Blitzer, *supra* note 3, at 370. Indeed, although it is still commonly stated that such arrangements are judged by the per se rule, an applied treatment under a rule-of-reason standard could reflect a consistency with allocative efficiency goals. Coate et al., *Antitrust in Latin America*, *supra* note 3, at 48. Similarly, the per se label for tying continues to be used despite wide recognition that significantly harsher treatment is accorded the per se test for horizontal price fixing. *See id.* at 73. Strictly speaking, the test reflects a "truncated" or "structured" rule of reason with horizontal agreements in the absence of a clear efficiency. GELLHORN & KOVACIC, *supra* note 41, at 292-307 (on resale price (RPM)), 204-18 (on group boycotts), 326 (on tying).

49. EC TREATY art. 86.

50. Spencer W. Waller, *Understanding and Appreciating EC Competition Law*, 61 ANTITRUST L.J. 55, 71 (1992) [hereinafter Waller, *EC Competition Law*].

51. *Id.* at 56-61.

52. *Id.* at 56.

53. *Id.* at 55.

54. *See* Langenfeld & Blitzer, *supra* note 3, at 353.

55. *See* Waller, *EC Competition Law*, *supra* note 50, at 74 (discussing the ability of EC antitrust merger laws to block any concentration of activity which acts to create or strengthen a dominant firm's position within the community).

it is unclear if this use of the dominance concept is the most efficient way to achieve this important political goal.

C. Recent Legislation

Antitrust reform has largely centered in Latin America⁵⁶ and Eastern Europe.⁵⁷ This article will examine and compare antitrust policy in each.

1. Latin America

Although a number of Latin American countries have had antitrust laws on the books for years,⁵⁸ the policies were not generally enforced.⁵⁹ This record of poor enforcement started to

56. See generally Coate et al., *Antitrust in Latin America*, *supra* note 3 (detailing the adoption and scope of antitrust legislation and policy in Latin America). The term Latin America is used broadly to include Mexico, Central America, South America, and the Caribbean.

57. For an overview of Eastern European enforcement, see generally Pittman, *Critical Provisions*, *supra* note 4; Russell Pittman, *Merger Law in Central and Eastern Europe*, 7 AM. U.J. INT'L L. & POL'Y 649 (1992) [hereinafter Pittman, *Merger Law*].

58. Ley Orgánica del Artículo 28 Constitucional en Materia de Monopolios [Organic Law of Constitutional Article 28 regarding Monopolies], D.O., Aug. 31, 1934 (Mex.), amended by decree of Dec. 27, 1979, D.O., Jan. 8, 1980 (Mex.), repealed and replaced by Ley Federal de Competencia Económica [Federal Law of Economic Competition], D.O., Dec. 24, 1992 (Mex.). Argentina's antimonopoly legislation reaches back to 1919. Guillermo Cabanellas & Wolf Etzrodt, *The New Argentine Antitrust Law Competition as an Economic Policy Instrument*, 17 J. WORLD TRADE L. 34, 34 nn.1-2 (1983).

59. Coate et al., *Antitrust in Latin America*, *supra* note 3, at 44. After World War II, Latin America made a concerted effort to industrialize through an "inward-looking" national trade strategy. Enrique R. Carrasco, *Law, Hierarchy, and Vulnerable Groups in Latin America: Towards a Communal Model of Development in a Neoliberal World*, 30 STAN. J. INT'L L. 221, 223 (1994). This policy came to be known as the "import-substitution" (ISI) model of development. *Id.* An element of great importance in the ISI model was the strong influence of the state in the economy through parastatals, or government enterprises. See Amy L. Chua, *The Privatization-Nationalization Cycle: The Link Between Markets and Ethnicity in Developing Countries*, 95 COLUM. L. REV. 223, 233 (1995). The state typically claimed the domestic monopoly in the products manufactured by its enterprises and through aggressive protectionist measures often limited imports of competing products. See Carrasco, *supra*, at 229-30, 233-34. These policies resulted in highly concentrated industries, often state-run or state-sanctioned monopolies, which, in turn, resulted in substantial inefficiencies. *Id.* at 238-40. See, e.g., DIANA HUNT, *ECONOMIC THEORIES OF DEVELOPMENT: AN ANALYSIS OF COMPETING PARADIGMS* 292-332 (1989) (describing the analysis of neoclassical critics and citing market imperfections and governmental interven-

change around twenty years ago when Chile implemented an antitrust law during reforms in the 1970s,⁶⁰ fine-tuning the regulation in 1980.⁶¹ Brazil, Peru, Mexico, and Venezuela passed or reformed their antitrust laws in the early 1990s.⁶² More recently, in early 1995, Argentina's proposed antitrust law passed the lower chamber of parliament.⁶³

Recent regulations include prohibitions against a wide range of business practices. While all the newest laws generally ban price fixing (consistent with an efficiency-based standard),⁶⁴ the regulations differ as to the treatment of other activities. Brazil, Mexico, Peru, and Venezuela restrict various activities of dominant firms,⁶⁵ with some countries⁶⁶ focusing on vertical restraints and/or price discrimination. These regulations could have adverse effects on competition. On the other hand, Chile attempts to limit anticompetitive uses of vertical restraints with a rule-of-reason.⁶⁷ In general, all the countries mentioned above are attempting to impose antitrust policies that can be characterized as "active."

2. Eastern Europe

Not far behind the Latin American nations, a number of Eastern European countries have recently adopted (or will soon adopt) antitrust legislation and policy. Albania,⁶⁸ Bulgaria,⁶⁹

tions in resource allocation as the cause of these insufficiencies). In effect, monopolies and particularly state-sanctioned monopolies, with their resulting supracompetitive prices, could not co-exist with a pro-market efficiency based antitrust policy. *Id.*

60. See Coate et al., *Antitrust in Latin America*, *supra* note 3, at 44 n.33.

61. *See id.*

62. *See id.* at 44-45.

63. Mark Dutz, Industry and Development Division, Competition Law to Support Market-Oriented Reform: The Argentine Context (The World Bank, 1992) (manuscript on file with the authors).

64. *See* Coate et al., *Antitrust in Latin America*, *supra* note 3, at 50.

65. *Id.* Such restrictions include prohibitions of price fixing, predation, monopolization, tying arrangements, horizontal restraints, resale price maintenance, vertical restraints, and price fixing. *Id.*

66. These countries include Argentina, Brazil, Chile, Columbia, the Dominican Republic, Guatemala, Mexico, Peru, and Venezuela. *Id.*

67. *Id.* This standard is also applied to mergers, monopoly, price fixing, resale price maintenance, and predation. *Id.*

68. Law Against Restrictions on Competition Monopolies and Unfair Competition (Alb.) (unofficial draft and trans., undated) (emphasis in the original) [hereinafter Albanian Competition Law] (unpublished draft, on file with the

the Czech Republic,⁷⁰ Estonia,⁷¹ Hungary,⁷² Latvia,⁷³ Lithuania,⁷⁴ Poland,⁷⁵ Romania,⁷⁶ Russia,⁷⁷ Slovakia,⁷⁸ and Slovenia⁷⁹ have received U.S. assistance with the drafting or review of their antitrust legislation and with training of agency

authors).

69. Law on Protection of Competition, SG No. 39/1991, May 2, 1991, (Bulg.) (Commission for the Protection of Competition trans., 1991) [hereinafter Bulgarian Competition Law].

70. Act No. 63 of 30th January 1991 on the Protection of Economic Competition in the wording of Act No. 495/1992 Coll. and Act No. 286 of 11th November 1993 (Czech. & Slovak Rep.), *reprinted in* ECON. BULL. (Ministry of Economic Competition trans., 1994) [hereinafter Czech Competition Law]. See Mastalir, *supra* note 1, at 79-83 & n.162 (citing publication of the Czech Competition law, in 13 BULL. CZECHOSLOVAKIAN L. 73-83 (Dr. Ivo Dvorak trans.) (Fall 1991)).

71. Law on Competition of June 16, 1993 (Estonia), *reprinted in* 1 LEGAL ACTS OF ESTONIA 3-10 (1994), *available in* WESTLAW, INT-EEUROPE Database, 1992 WL 562749 (N.T.I.S.).

72. Act of the Prohibition of Unfair Market Practices (Hung.) (Competition Agency trans., 1991) [hereinafter Hungarian Competition Law] (draft on file with the authors). See *generally* Ben Slay, Industrial Demonopolization and Competition Policy in Poland and Hungary (April 1994) (unpublished manuscript, on file with the authors) (paper presented at the panel on "Industrial Development in Transitional Economies," at the twentieth annual meeting of the Eastern Economics Association, held March 18-20, 1994, in Boston); Mastalir, *supra* note 1, at 79-83.

73. Law of the Republic of Latvia on Competition and Restriction of Monopoly (unofficial trans. by Biruta Ozola, 1991) [hereinafter Latvian Competition Law] (draft on file with the authors).

74. Law on Competition, No. 1-2879, September 15, 1992 (Lith.) [hereinafter Lithuanian Competition Law] (unofficial draft on file with the authors).

75. Act of February 24, 1990, on Counteracting Monopolistic Practices (Pol.), *as amended* by the Act of June 28, 1991, *available in* WESTLAW, INT-EEUROPE Database, 1992 WL 563320 (N.T.I.S.) [hereinafter Polish Antimonopoly Law]. See Mastalir, *supra* note 1, at 69-70.

76. Competition Law (Rom.) (unofficial draft of June 24, 1994) [hereinafter Romanian Competition Law] (draft on file with the authors).

77. Law of the Russian Soviet Federative Socialist Republic on Competition and the Restriction of Monopolist Activity in Commodity Markets (unofficial draft of April 16, 1991) [hereinafter RSFSR Competition Law] (draft on file with the authors).

78. The Act No. 188 of the National Council of the Slovak Republic of July 8, 1994 on Protection of the Economic Competition, *reprinted in* THE NEW SLOVAK COMPETITION LAW (Milan Banas trans., 1994) [hereinafter Slovakian Competition Law]. The Act replaced Act Number 63/1991 Coll. of Laws of Economic Competition, as amended by the Act Number 495/1992 Coll. of Laws. *Id.* art. 24.

79. The Law on the Protection of Competition (Slovenia), *reprinted in* SLOVENIAN BUS. REP. (undated) at 12 [hereinafter Slovenian Competition Law].

staff.⁸⁰ One unifying characteristic of antitrust policy in these countries appears to be a desire to support a promarket model of privatization.⁸¹ The Polish antitrust law, for example, is part of the government's campaign to strengthen its power to actively pursue industrial deconcentration and to take action against practices that effectively restrict competition.⁸² There also appears to be an underlying attempt to design legislation and enforcement practices to resemble those of the EU as much as possible in a process known as harmonization.⁸³

While differing in their specific content, the same core set of legal guidelines for unacceptable types of horizontal and vertical mergers,⁸⁴ agreements between firms,⁸⁵ enforcement procedures,⁸⁶ and definitions of dominant firm behavior⁸⁷ ap-

80. Information provided by Staff Attorney Julie Gearty, Technical Assistance Coordinator for Central Europe, Office of the Executive Director, U.S. Federal Trade Commission. The FTC and the Antitrust Division of the Department of Justice have sent advisory missions to Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, and Slovakia.

81. See generally *supra* notes 68–79 (citing various countries' competition laws). This does not suggest that all of the policies are necessary for a market economy.

82. Mastalir, *supra* note 1, at 69.

83. See, e.g., Kurt Stockmann, *Merger Control and State Aids Panel: Antitrust Merger Control—A German Perspective*, 9 CONN. J. INT'L L. 565, 566–67 & n.6 (1994). "Harmonization with EU law is one of the main purposes . . . [of amending] existing competition laws in Poland, Hungary, the Czech and Slovak Republics, as well as in Bulgaria." *Id.* at 566 n.6.

84. See, e.g., Bulgarian Competition Law, *supra* note 69, arts. 5–6; Czech Competition Law, *supra* note 70, §§ 8–8a; Slovakian Competition Law, *supra* note 78, art. 8; Estonian Competition Law, *supra* note 71, art. 5. These merger control guidelines establish the rules for recognizing a merger, i.e. the transfer of shares, or the acquisition of control of a competitor, and establish when the merger has resulted in a threshold market share level owned by the merged parties, thereby creating the presumption of an anticompetitive act. The presumption can be overcome by showing that the detriment of the merger was outweighed by the advantages. See, e.g., Czech Competition Law, *supra* note 70, § 8a(2).

85. See, e.g., Bulgarian Competition Law, *supra* note 69, arts. 8–9 (listing banned or regulated agreements); Czech Competition Law, *supra* note 70, §§ 3–6a (regulating cartel agreements and establishing Competition Office guidelines for the types of business agreements that can be reviewed); Estonian Competition Law, *supra* note 71, art. 18 (providing regulations for "Contracts and Coordinate Activities Impairing Competition"); see also Carolyn Brzezinski, *Competition and Antitrust Law in Central Europe: Poland, the Czech Republic, Slovakia, and Hungary*, 15 MICH. J. INT'L L. 1129, 1132–37 (1994).

86. See, e.g., Bulgarian Competition Law, *supra* note 69, arts. 16, 21–25; Czech Competition Law, *supra* note 70, §§ 12, 14; Estonian Competition Law,

pear in each nation's antitrust laws. Legislative measures directed towards cartels and other restrictive agreements attack anticompetitive conduct.⁸⁸ Actions of individual firms may also be covered by the laws.⁸⁹ As in the EU, the instrument of choice for challenging anticompetitive conduct—the concept of *abuse of dominant position*⁹⁰—plays a key role in the various laws.⁹¹ All of the above nations have codified legal provisions which enable challenges to perceived abuses of dominant position.⁹² To be challenged, a firm's market share must generally exceed thirty to forty percent of the market, a standard which certainly begs the question of market definition.⁹³

supra note 71, arts. 24–26; Slovakian Competition Law, *supra* note 78, arts. 12–14. These enforcement mechanisms are provided by the establishment of some sort of administrative office which acts through various enforcement mechanisms to monitor the behavior of market participants. *See, e.g.*, Czech Competition Law, *supra* note 70, § 11 (giving jurisdiction to the Ministry of Economic Competition).

87. *See, e.g.*, Bulgarian Competition Law, *supra* note 69, art. 7; Czech Competition Law, *supra* note 70, § 9; Estonian Competition Law, *supra* note 71, art. 17.

88. Mastalir, *supra* note 1, at 66 (discussing differing philosophies of anti-trust law between the U.S., with a structuralist system preferring “dismemberment of monopolies,” and the EU, which prefers regulation of anticompetitive behavior rather than “dismemberment of offenders”).

89. *See generally* Brzezinski, *supra* note 85, at 1134 (discussing differences between Polish and Czech law, which provides a list of monopolistic practices by single firms that may result in the restriction of competition).

90. *See id.* at 1137–38; *see also* Mastalir, *supra* note 1, at 67–68.

91. *Id.* at 1137 (comparing “market dominance” abuse provisions in Polish, Hungarian, Czech, and Slovakian competition laws).

92. Albanian Competition Law, *supra* note 68, art. 45; Bulgarian Competition Law, *supra* note 69, arts. 7, 21; Czech Competition Law, *supra* note 70, §§ 9, 11; Estonian Competition Law, *supra* note 71, arts. 15, 17, 24; Latvian Competition Law, *supra* note 73, arts. 5, 12 (referring to monopoly action, rather than dominant position); Lithuanian Competition Law, *supra* note 74, arts. 3, 12; Polish Antimonopoly Law, *supra* note 75, art. 5; Slovakian Competition Law, *supra* note 78, art. 7; Slovenian Competition Law, *supra* note 79, arts. 10, 24.

93. Albanian Competition Law, *supra* note 68, art. 3(5) (specifying this threshold at 30%); Bulgarian Competition Law, *supra* note 69, art. 3(2) (specifying this threshold at 35%); Czech Competition Law, *supra* note 70, art. 9(2) (specifying this threshold at 30%); Estonian Competition Law, *supra* note 71, art. 15(1) (specifying this threshold at 40%); Latvian Competition Law, *supra* note 73, ch. 2 (containing no thresholds); Lithuanian Competition Law, *supra* note 74, art. 2 (specifying this threshold at 40%); Polish Antimonopoly Law, *supra* note 75, art. 2(7) (specifying this threshold at 30%); Slovakian Competition Law, *supra* note 78, art. 7(2) (specifying this threshold at 40%); Slovenian Competition Law, *supra* note 79, art. 10 (specifying this threshold at 40%). Antitrust con-

Additionally, several nations target enforcement towards market structure.⁹⁴ Structural policies are of two general types. The first attempts to eliminate consolidations of monopoly power by breaking them up,⁹⁵ and the second tries to prevent incipient consolidations which would lessen competition through merger oversight.⁹⁶ Forced divestiture policies often affect large state enterprises and interact with the goal of privatization.⁹⁷ The goal of merger control is to deter attempts to re-create large state enterprises through acquisition.⁹⁸

Vertical agreements⁹⁹ such as vertical foreclosure¹⁰⁰ and dealer restrictions¹⁰¹ are also covered in the legislation.¹⁰² However, in contrast to the relative uniformity of the treatment of market dominance, vertical legislation differs across nations.¹⁰³ Nonetheless, all the vertical laws include some type

sequences vary depending on the market power of the firm or firms engaged in the transaction. See The 1992 Merger Guidelines, 4 Trade Reg. Rep. (CCH) ¶13,104 (1992). The measure of market power, however, turns on the definition of the "relevant market." *Id.* A relevant antitrust market consists of the goods among which a firm or group of firms acting in concert can raise prices significantly without losing so much business to substitutes so as to make the price rise unprofitable. *Id.* For a complete discussion of the 1992 Merger Guidelines, see generally *Symposium on New 1992 Merger Guidelines*, 38 ANTITRUST BULL. 473 (1993).

94. See Mastalir, *supra* note 1, at 66-67.

95. *Id.* at 66. See Pittman, *Critical Provisions*, *supra* note 4, at 487.

96. See Pittman, *Merger Law*, *supra* note 57 (discussing the importance of merger oversight regulations as a vital mechanism in the creation and maintenance of demonopolized economies in developing Eastern European economies).

97. See Brzezinski, *supra* note 85, at 1132 (discussing the issues involved in converting large state-owned industrial enterprises to a market economy).

98. *Id.* at 1137 (describing the role of the competition laws in post-communist countries as "provid[ing] a means of controlling the legacy of state monopolies left behind by central planning . . . they alleviate the fear that privatization of state monopolies will result in the creation of new private monopolies.").

99. Agreements between firms and their customers or suppliers are termed "vertical" because they involve firms at different levels in the production chain. Pittman, *Critical Provisions*, *supra* note 4, at 488.

100. "Vertical foreclosure" results from anticompetitive practices by dominant firms through market agreements that restrict access of certain buyers and sellers from certain markets. SCHERER, *supra* note 4, at 70.

101. Dealer restrictions involve vertical agreements which give "exclusive dealing" rights to a dealer or distributor in a given market. *Id.* at 70.

102. See, e.g., Bulgarian Competition Law, *supra* note 69, art. 10; Estonian Competition Law, *supra* note 71, art. 17(3)-(4); Pittman, *Critical Provisions*, *supra* note 4, at 487-90 (comparing and contrasting the vertical dealing provisions in the laws of Poland, Hungary, Russia, and the Czech Republic).

103. See Pittman, *Critical Provisions*, *supra* note 4, at 487-90. The Czech and

of proscription against refusals on the part of firms to buy from particular upstream suppliers or sell to particular downstream suppliers,¹⁰⁴ resale price maintenance (where suppliers mandate consumer prices),¹⁰⁵ exclusive dealing (agreements limiting a retailer to the purchase of products of a single manufacturer),¹⁰⁶ and certain forms of nonprice vertical contracts (i.e., limitations on a retailer's geographic scope).¹⁰⁷

While the intent of the antitrust laws is reasonably easy to understand, it is more difficult to address the issue of enforcement in the various countries. In civil code countries, the implementation of laws often requires further clarification via "rules" or "regulations" issued by the relevant enforcement agency.¹⁰⁸ These regulations can, among other things, either expand the reach of the law or restrict the applicability of its enforcement.¹⁰⁹ Once given the regulations, each antitrust agency typically adds an element of discretion to its enforcement initiatives.¹¹⁰ Thus, a full understanding of antitrust

Slovak Federated Republic (CSFR) law makes no distinction between horizontal agreements and vertical agreements but instead bans all agreements among market participants, both vertical and horizontal, that restrict competition. *Id.* at 488. The Polish law distinguishes slightly between the two, for example, banning pricing restrictions among competitors (horizontal) and agreements limiting market access (vertical). *Id.* at 489. The Russian law and Hungarian law provide clearer distinctions between horizontal and vertical regulation and are "in this respect more encouraging to foreign investment than the CSFR and Polish laws, since they provide greater clarity concerning the treatment of vertical restraints." *Id.* at 490.

104. *Id.* at 488, 490; Mastalir, *supra* note 1, at 81.

105. See Pittman, *Critical Provisions*, *supra* note 4, at 501-02 (discussing how Poland, Hungary, the CSFR and Russia all have provisions which attempt to control the pricing, production and distribution by dominant firms).

106. See, e.g., Bulgarian Competition Law, *supra* note 69, art. 10; Polish Antimonopoly Law, *supra* note 75, art. 5(3); RSFSR Competition Law, *supra* note 77, art. 6(2).

107. See Pittman, *Critical Provisions*, *supra* note 4, at 488-93.

108. Mastalir, *supra* note 1, at 66-67 ("The rules regulating competition are usually drafted in terms of per se illegality, although their application is currently much tempered by a 'rule of reason' or case-by-case assessment of the economic benefits or detriments of alleged anticompetitive activity.").

109. See Brzezinski, *supra* note 85, at 1143-44 (discussing the "far reaching" enforcement powers of competition offices who must balance economic interests as they facilitate the switch from a centrally planned to a market economy). "[T]he authorities must balance full and aggressive enforcement against the practical limitations that stem from . . . recession, . . . inflation, . . . [and] political instability . . ." *Id.*

110. If a market participant reaches a certain dominant position, as deter-

issues in developing countries requires a detailed case-study approach.

D. Demand and Supply for Antitrust Legislation

What determines the demand for antitrust in reforming economies? As noted earlier, the FTC, the Antitrust Division of the U.S. Department of Justice, the American Bar Association (ABA), the EU, the OECD, the German Cartel Office, and the World Bank have vigorously advocated and supported the idea of antitrust in emerging market economies.¹¹¹ Bureaucratic extension of power and influence¹¹² and the potential to cultivate a new and growing client base¹¹³ may explain a portion of this international demand. Establishment of antitrust policy may also be seen as a necessary antecedent for international agreements. The recently adopted NAFTA between Mexico, the United States, and Canada explicitly requires each party to "adopt or maintain measures to proscribe anticompetitive business conduct."¹¹⁴ As a result of this requirement, prior to the finalization of the NAFTA, Mexico formulated and adopted an antitrust law.¹¹⁵ Similarly, the expectation of joining the EU is a strong incentive to Eastern European countries to adopt EU antimonopoly legislation in a process known as "harmonization."¹¹⁶

mined by a floor level of market share, there is a presumption of an anticompetitive practice, but it may be determined that the market benefit of the dominant firm outweighs the detriment of the potential for abuse of the dominant market position. *See generally id.* at 1139.

111. *See supra* note 4 and accompanying text.

112. "Western nations [have been] prompt[ed] to offer their assistance as midwives to the birth of new market economies." Mastalir, *supra* note 1, at 61.

113. A \$7.2 million grant from the Agency for International Development was used by the Antitrust Division of the United States Justice Department and the FTC to establish consulting teams to assist Poland and the former Czechoslovakia. *Id.* at 63.

114. NAFTA, *supra* note 19, art. 1501(1); *see* Mark R. Joelson, *Antitrust Aspects of NAFTA: Is There a Three Party Commitment to the Effective Enforcement of National Antitrust Laws?*, 40 FED. B. NEWS & J. 573, 573 (1993).

115. *See* Joelson, *supra* note 114, at 573.

116. *See* Brzezinski, *supra* note 85, at 1131 n.14 (stating that Poland, the Czech Republic, Slovakia, Hungary, Romania, and Bulgaria have all executed agreements which will make them associated countries with the EU). However, these demonopolizing countries have experienced difficulties harmonizing antitrust policies. *See* Stockmann, *supra* note 83, at 567-69.

However, even with external pressure, it is unlikely that antitrust policy could be easily imposed on numerous Latin American and Eastern European countries without some internal support. Although the common justification for implementing antitrust policy appears to be the alleged inadequacy of the marketplace to effectively handle particular structural problems,¹¹⁷ political forces should not be overlooked. Antitrust policy imposed for political reasons¹¹⁸ is unlikely to be appropriately implemented and thus is unlikely to generate the expected benefits.

The standard benefit of antitrust enforcement is the deterrence of monopolistic practices.¹¹⁹ Monopolistic practices and other restraints of trade challenge the conventional belief that "a workably [sic] competitive marketplace will achieve a more efficient allocation of resources, greater efficiency in production, and increased innovation."¹²⁰ Moreover, the adoption of antitrust initiatives may enable the governments of developing economies to signal potential investors about the relative attractiveness of investing in their countries.¹²¹

117. Brzezinski, *supra* note 85, at 1132-49. The author states:

Each of these . . . [Eastern European] antimonopoly laws was designed to accommodate the special characteristics of the post-socialist economies, such as the high degree of monopolization and severe problems of market measurement. The vague language of the laws and the discretion of the competition authorities freely to shift their enforcement efforts comprise means of introducing and protecting competition in these highly transitional economies.

Id. at 1149.

118. For an example of antitrust policy imposed for political, rather than commercial reasons, see *EC Official Faults U.S. for Bilateralism; Commission Criticizes U.S.-Japan Accord*, BNA INT'L TRADE DAILY, Jan. 28, 1992, available in LEXIS, News Library, US File, at *1.

119. See generally KENNETH G. ELZINGA & WILLIAM BREIT, *THE ANTITRUST PENALTIES: A STUDY IN LAW AND ECONOMICS* (1976) (discussing costs and benefits of antitrust enforcement). The active enforcement of antitrust laws is believed to act as a deterrent to monopolistic behavior by increasing the cost of such behavior. See Robert M. Feinberg, *Strategic and Deterrent Pricing Responses to Antitrust Investigations*, 2 INT'L J. INDUS. ORG. 75, 76-77 (1984).

120. Rodriguez & Williams, *supra* note 30, at 216 (citing PHILLIP AREEDA, *ANTITRUST ANALYSIS* 6-34 (1974)).

121. See generally Mastalir, *supra* note 1 (discussing the economic objectives of Eastern European nations in adopting antitrust laws). Some have argued that the adoption of antitrust legislation familiar to potential investors could reduce some of the uncertainty associated with operating in foreign legal environments. *E.g.*, FTC Commissioner Roscoe Starek III, What are the Limits of Antitrust

A recent statement by a Department of Justice official appears to reflect this particular motivation. Charles Stark, Chief of the Foreign Commerce Section, in referring to recently passed antitrust legislation in Eastern Europe, noted that Eastern European countries "recognize the importance of maintaining a competitive marketplace to attract trade and foreign investment, and to promote the vigor of their domestic economies."¹²² However, this focus on achieving an optimal solution to a welfare problem assumes a benign and welfare-maximizing state.¹²³ This "naive" premise has come under intense scrutiny from supporters of the "New Political Economy"¹²⁴ who view the state as an endogenous participant in the reform pro-

Cooperation? Remarks Before the Fourth Annual Symposium on EU Mergers and Joint Ventures: New Commission/New Merger Policy? 25 (Mar. 17, 1995) (unpublished transcript, on file with the authors) ("[W]orldwide convergence among national competition policies holds the long-run promise of making the law easier for multinational firms to understand and obey . . ."). It should be clear, however, that Commissioner Starek did conclude by favoring gradualism in harmonization efforts. *Id.* But see generally George Bittlingmayer, *Stock Returns, Real Activity, and the Trust Question*, 47 J. FIN. 1701 (1992) [hereinafter Bittlingmayer, *Stock Returns*] (claiming that antitrust fosters investor uncertainty). We also provide a competing interpretation of the likely effects of activist antitrust enforcement on investment, but the substantially less bullish view of the benefits of antitrust we present does not, at least in principle, necessarily exclude the procompetitive effect discussed here. See *infra* part III. A more likely use of the antitrust laws to foster investment entails governments privatizing assets while simultaneously granting tacit or explicit antitrust exemptions. See generally William Glade, *Privatization in Rent-Seeking Societies*, 17 WORLD DEV. 673 (1989) (noting that this is not an uncommon practice among recent reforming economies). Unfortunately, if investors believe that governments cannot credibly commit to such a policy, then they would be unwilling to pay capitalized monopoly rents for government assets.

122. Charles S. Stark, International Antitrust: Looking Ahead, Address Before the Antitrust and International Sections of the American Bar Association (Aug. 9, 1993) (unpublished transcript, on file with the authors).

123. MERILEE S. GRINDLE, *THE NEW POLITICAL ECONOMY: POSITIVE ECONOMICS AND NEGATIVE POLITICS* 5-7 (World Bank Working Paper WPS 304, 1989). "The harsh realities of the 1980s made it increasingly difficult to sustain assumptions about welfare maximizing states." *Id.* at 6. "Politicians and bureaucrats ceased to be seen as value neutral public servants and became . . . narrowly motivated to stay in power or to maximize their individual gains . . ." *Id.* at 7. But see Brzezinski, *supra* note 85, at 1130-31 (discussing the organization of competition authorities in post-communist countries at the sub-ministerial level which allows them to operate "as apolitical institutions capable of ensuring continuity in economic reform during turbulent periods of political and social transition").

124. Rodriguez & Williams, *supra* note 30, at 216 n.34.

cess.¹²⁵ Antitrust policy will serve to protect competition and attract investment only if appropriately applied.¹²⁶

125. *Id.* at 216. Even though there is a wealth of material on the New Political Economy, it is not easy to provide a "representative" reference due to the proliferation of labels describing work by authors, not only in different disciplines (e.g. Economics and Political Science), but also within disciplines (e.g. International Trade and Industrial Organization). Nonetheless, labels and descriptives such as endogenous tariff theory, rent-seeking, and others share a methodological similarity which consists of viewing the state as an endogenous participant with competing claims on scarce resources. See generally GRINDLE, *supra* note 123 (discussing the application of the New Political Economy to conditions in developing countries); Anne O. Krueger, *Virtuous and Vicious in Economic Development*, 83 AM. ECON. REV. 351 (1993) (discussing the interactions between politics and economics in various contexts); ANNE O. KRUEGER, *THE POLITICAL ECONOMY OF POLICY REFORM IN DEVELOPING COUNTRIES* 129-34 (1993) (discussing the nature of reforms and factors affecting their success).

126. Apart from anecdotal vignettes, we have found no clear evidence that the objectives of antitrust have been misinterpreted or incorrectly applied. This is a reflection not so much of any inherent inability to practice antitrust enforcement but rather a reflection, most likely, of what has been called "demography's hidden curse." Arnold C. Harberger, *Policymaking and Economic Policy in Small Developing Countries*, in *THE OPEN ECONOMY: TOOLS FOR POLICYMAKERS IN DEVELOPING COUNTRIES* 249-51 (Rudiger Dornbusch & F. Leslie C.H. Helmers eds., 1988) (arguing that basic demographic factors suggest that small countries, defined as those with a population of less than 20 million, contain small endowments of trained, educated professionals who are able to make and enforce government policies). Harberger concludes that there is an urgent need for "keeping the process of government—the laws, the regulations, and the procedures and indeed the very scope of the public sector—as simple as possible." *Id.* at 250. He continues by noting:

Small, developing countries should especially avoid the all too common trap of endowing regulators, administrators, and other government officials with wide discretionary powers. Such powers are dangerous even in economies well supplied with trained talent, and with an informed and vigilant public. They can be utterly noxious in countries with a fragile bureaucracy of relatively low administrative competence and a public that does not and probably cannot subject public decision to public scrutiny.

Id. at 251. See Joan Nelson, *The Political Economy of Stabilization: Commitment, Capacity, and Public Response*, in *TOWARD A POLITICAL ECONOMY OF DEVELOPMENT* 80, 91-92 (Robert H. Bates ed., 1988) ("In some cases, ministers and political leaders simply have very limited economic background and understanding. This can be true in any country . . . , but it is more likely in countries with a short history of independence and comparatively few highly educated people."). Lacking the common law roots of antitrust, a number of civil code countries never developed jurisprudence that could easily accommodate antitrust legislation. See Coate et al., *Antitrust in Latin America*, *supra* note 3, at 48-52 (discussing the various means of antitrust enforcement used in civil law countries, and their possible drawbacks, inherent due to developing countries lack of well-functioning institutions). As a result, the newly inaugurated antitrust agencies have found it necessary to educate bar and bench in addition to the general public on the mechanisms and scope of antitrust law. The

An alternative proposition is that support for antitrust measures varies according to the likely effect such measures will have on the political agendas of the diverse domestic and international groups competing for influence and control in reforming economies.¹²⁷ Numerous possible political uses for antitrust policy exist if we assume that nontariff barriers are a fairly close substitute for tariff barriers. An interest group that controls government policy might allow tariff liberalization, thus enabling the government to claim it has satisfied international lender conditionality agreements.¹²⁸ In turn, the government could swiftly erect nontariff barriers to placate internal opposition while ignoring the recommendations of its own antitrust agency.¹²⁹ In this scenario, antitrust policy would only be window-dressing.

Under yet a third scenario, we can see situations where an interest group could support an activist antitrust policy to discipline new competitors who are too aggressive in the marketplace. Predation and dominance regulations make it relatively easy to use the governmental process to attack successful businesses. Antitrust laws and practices could also be used to protect the current distribution of rents in society. New distribution techniques could be blocked by vertical antitrust enforce-

particular case of the Eastern European countries evokes similar comments. Martin C. Spechler, *Competition and Structural Change in Eastern Europe*, 6 REV. INDUS. ORG. 189, 195 (1991) ("With markets still rudimentary in most places and needed structural changes so many, it can be plausibly thought that economic managers are still needed, if for nothing else than dealing with international aid agencies. Talent, it is said, is scarce, and entrepreneurship and risk-taking not habitual in these place[s] . . ."). Lack of a basic familiarity with market process could result in the inappropriate execution of antitrust policy.

127. This certainly has appeared to be the case in the U.S. See Comanor, *supra* note 22, at 734. For an alternative perspective, see Fred S. McChesney & William F. Shughart II, *Introduction and Overview*, in *THE CAUSES AND CONSEQUENCES OF ANTITRUST* (Fred S. McChesney & William F. Shughart II eds., 1995).

128. See generally Michael P. Leidy & Bernard M. Hoekman, *Spurious Injury as Indirect Rent Seeking: Free Trade Under the Prospect of Protection*, 3 ECON. & POL. 111 (1991) (discussing direct and indirect influences that labor and industry lobbies can have on government policies related to free trade, especially in the context of protection from foreign competition).

129. "The political task [of liberalization proponents] has always been somehow to assuage the interest groups opposed to liberalization. One important way in which importcompeting industry and labor groups have been accommodated is by offering them the *prospect of protection* should liberalization prove injurious." *Id.* at 111.

ment against new and more efficient forms of business organization. Finally, antitrust may provide political cover for unpopular decisions. By referring a political problem—such as the rise of gasoline prices (due to exogenous reasons)—to the “independent” antitrust authority, the government may defuse potentially troublesome demands for action by affected groups. However, unless the report of the antitrust agency represents solid economic analysis, policymakers may find themselves forced into an inappropriate decision.

As we take stock of recent developments, it seems that the strengthening or inauguration of antitrust regimes appears to have proceeded unabated. Small economies such as Guatemala and Albania appear to have joined numerous other reforming economies in uncritically adopting antitrust policy as a component of its reform policy. The significant number of antitrust laws and policies in place puts us in the difficult and unfavorable position of having to establish a negative: That the antitrust laws will do little or nothing to foster competitive behavior or to aid the transition to a market economy. Still, recent interest in revising of some of the earlier attempts at antitrust legislation suggests that there may be a window of opportunity for addressing the issues raised here and elsewhere.¹³⁰

III. EFFECTS OF ANTITRUST ON INVESTMENT INCENTIVES

From the beginning of the structural adjustment programs during the late 1970s, reforming economies have opened their markets to international competition as a method of promoting economic growth and facilitating a rapid recovery from decades of statist policies.¹³¹ By opening domestic markets to foreign

130. See generally Ana J. Jatar, Competition Policy in Liberalizing Economies (Jan. 1991) (unpublished manuscript, on file with the authors) (paper presented at the January 1995 American Economic Association Conference) (discussing problems with Venezuelan antitrust legislation and policy and recommending changes); see, e.g., Khemani, *supra*, note 4 at 2, 10–11 (claiming that Russia's antimonopoly law has not been vigorously applied, incorrectly applied, or both, and recommending corrections); Ricardo M. Paredes, Jurisprudence of the Antitrust Commissions in Chile (Feb. 1995) (unpublished manuscript, on file with the authors) (paper presented at the First Congress of the Latin American and Caribbean Association of Law and Economics in Mexico City) (recommending revisions to Chilean antitrust legislation and practice).

131. See Brzezinski, *supra* note 85, at 1129 (describing the rapid transformation of Eastern European economies from noncompetitive socialist systems to

competition, producers of tradeable goods and services are forced to become more efficient in order to protect their market shares.¹³² Enhanced efficiency, in turn, makes domestic producers more competitive in export markets, to which they increasingly look to make up for domestic market share lost to imports.¹³³ Yet, despite the promise of increased productivity, growth will not be sustainable unless assisted by an increase in investment.¹³⁴ To fully capture the benefits of market reforms, policymakers realized that it was crucial to increase both domestic and foreign investment.¹³⁵

competitive market-based systems). Although these "statist policies" varied significantly across national borders, the consistent element was the strong influence of the state in the economy through "parastatals," or government enterprises. *Id.* at 1130; see Glade, *supra* note 121, at 674 (discussing different cases which can illustrate the roles parastatals played in transitioning Latin American economies). The state typically claimed a domestic monopoly in products manufactured by its enterprises and often limited imports of competing products. This resulted in highly concentrated industries, often state-run or state-sanctioned monopolies, which, in turn, resulted in substantial inefficiencies. Brzenzinski, *supra* note 85, at 1130. Prices of intermediate and final goods were frequently regulated and often explicitly set by the government. The existence of monopolies and particularly state-sanctioned monopolies not only resulted in supracompetitive prices but also in a misallocation of scarce resources, and costly production due to reliance on inefficient technology—all because of the absence of competition. The Latin American countries followed a version of these policies known as import-substitution industrialization. See HUNT, *supra* note 59, at 321 (describing how Brazil and Mexico have made a successful transition to export-led growth); see also Carrasco, *supra* note 59, at 223. For a general discussion, see ANNE O. KRUEGER, SAN FRANCISCO INSTITUTE FOR CONTEMPORARY STUDIES, *DEVELOPMENT WITH TRADE* (1988); ANNE O. KRUEGER, *POLITICAL ECONOMY OF POLICY REFORM IN DEVELOPING COUNTRIES* (1993).

132. James Levinsohn, *Testing the Imports-as-Markets-Discipline Hypothesis*, 35 J. INT'L ECON. 1, 2 (1993). "That international competition might act to curtail domestic market power is an old, theoretically robust, and very simple insight." *Id.* at 20. See Robert M. Feinberg & Mieke Meurs, *Privatization and Antitrust in Eastern Europe: the Importance of Entry*, 39 ANTITRUST BULL. 797, 799–802 (1994) (noting the special importance that entry enjoys in antitrust analysis).

133. See MICHAEL R. CZINKOTA, *INTERNATIONAL BUSINESS* 309–10 (1989) (stating that domestic producers often engage in international activities, which include exportation, to combat declining market share and increased foreign competition).

134. See Robert Pindyck, *Irreversibility, Uncertainty and Investment* 2–3, 44–46 (National Bureau of Economic Research Working Paper No. 3307, Mar. 1990) (unpublished manuscript, on file with the authors).

135. See BRADLEY R. SCHILLER, *THE MACRO ECONOMY TODAY* 500–02 (4th ed. 1989).

Investment, in almost any form or magnitude, necessitates the commitment of capital,¹³⁶ along with the possibility of losing the committed assets. As a general principle, private investors will hesitate to invest in an environment of public policy uncertainty.¹³⁷ To the extent that capital investment is irreversible, any likelihood of a policy change that may result in capital losses can reduce the incentive to commit capital.¹³⁸ Firms may prefer to wait for greater policy stability than to commit resources to sectors which, although presently profitable, may face substantial risk.¹³⁹ An increase in investment, it follows, requires a sustainable policy environment.¹⁴⁰ Enhancing the sustainability of the policy environment, therefore, must be a primary objective of reforming economies.

It is well known that in a world of risk-averse investors, an increase in uncertainty usually decreases the equilibrium level of investment.¹⁴¹ Entry is a business decision with the profits subject to significant uncertainties in reforming economies.¹⁴² Thus, abstracting from the normal return to business risk, firms may choose to commit capital in reforming economies only if they are compensated for the added risk of policy reversal.¹⁴³ Accordingly, entry into reforming economies is likely to occur only if firms, *ex ante*, expect higher returns than those expected for an economy with less policy uncertainty. Overall, market performance will most likely be characterized by high returns for successful entrants.¹⁴⁴ Moreover, returns are likely to be

136. See CAMPBELL R. MCCONNELL & STANLEY L. BRUE, *ECONOMICS: PRINCIPLES, PROBLEMS, AND POLICIES* 219 (11th ed. 1990).

137. See Dani Rodrik, *Policy Uncertainty and Private Investment in Developing Countries 2* (National Bureau of Economic Research Working Paper No. 2999, June 1989) (unpublished manuscript, on file with the authors) (presenting a model linking policy uncertainty to private investment response and shows that even moderate amounts of policy uncertainty can act as a hefty tax on investment).

138. See Pindyck, *supra* note 134, at 46-47.

139. See *id.* at 46-47; Rodrik, *supra* note 137, at 2.

140. See Rodrik, *supra* note 137, at 1-2.

141. Refinements within this literature have shown that when new information has the potential of making the future value of an investment less uncertain, even a risk-neutral firm has an incentive to postpone irreversible investments and gather more information. See generally Pindyck, *supra* note 134 (reviewing various models of irreversible investment and their application to investment decisions).

142. See Rodrik, *supra* note 137, at 1-2.

143. See *id.* at 7-8.

144. The actual performance of the investment may make the returns look

correlated over time, with successful firms continuing to earn premium returns until their techniques can be fully copied in the marketplace. As a result of these forces, systematic high returns may reflect risks undertaken by investors rather than the exercise of market power.¹⁴⁵ These dual interpretations are not often adequately parsed and an incorrect conclusion may be drawn by antitrust regulators.¹⁴⁶

An active antitrust enforcement policy runs the risk of a myopic focus on the static market model, instead of broadly considering the institutional realities of a reforming economy. For example, predation enforcement agendas are likely to use evidence of high returns as suggestive of monopoly power.¹⁴⁷ Likewise, merger deconcentration policies may use evidence of "supranormal" profits to justify attacking mergers in affected industries.¹⁴⁸ Any activist antitrust policy may be considered

even higher for certain periods of time. Calculations have shown that with setup costs, the equilibrium intertemporal price path requires charging a price for an initial transaction below marginal cost and then increasing the price so that the supplier earns quasi-rents on subsequent transacting. See generally Joseph Farrell & Carl Shapiro, *Optimal Contracts with Lock-Ins*, 79 AM. ECON. REV. 51 (1989) (discussing observable and unobservable set-up costs in the context of long-term and short-term contracts in the context of efficiency).

145. Cf. L. Wayne Dobson, *Usury Ceilings Fail to Meet Intended Objectives*, AM. BANKER, Mar. 17, 1980, available in LEXIS, News Library, US File, at *5 (explaining that studies indicate, in the case of interregional interest rates, that differences exist partly due to degrees of risk, rather than market power).

146. There may be other contributing factors that corrupt information usually obtained from conventional price signals. Episodes of high inflation, for example, distort the normal functions of relative prices. See Dennis W. Carlton, *The Disruptive Effect of Inflation on the Organization of Markets*, in INFLATION CAUSES AND EFFECTS 139 (Robert Hall ed., 1982). High inflation severely complicates, among others, the most fundamental step of an antitrust investigation: the determination of the antitrust product market. *Id.* at 142. In specifying an antitrust product market, antitrust analysts rely heavily on a price test, which consists of discerning clear differences between anticompetitive and cost-based price increases. To examine this methodology, see DEPT. OF JUSTICE AND FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES 48 (1992). There are still other reasons that weaken the usefulness of prices and other traditional signals for antitrust purposes. See Feinberg & Meurs, *supra* note 132, at 801 ("Rapid changes in the structure of prices, forms of ownership, and sources of demand have made it difficult for profits rates to convey signals for entry in the way they do in the established market economies.").

147. See John C. Hike & Philip B. Nelson, *Strategic Behavior and Attempted Monopolization: The Coffee (General Foods) Case*, in THE ANTITRUST REVOLUTION 208, 220 (John E. Kwoka & Lawrence J. White eds., 1989) (studying the FTC's decision against General Foods).

148. Cf. Sam Peltzman, *The Gains and Losses from Industrial Concentration*,

by investors as an adverse shift in the policy environment. Thus, a naive focus on short-run allocative efficiency may adversely affect the long-run investment potential of a reforming economy.

Although examined empirically only by George Bittlingmayer, the charge that aggressive antitrust prosecution hurts business confidence is plausible even in developed economies.¹⁴⁹ Three channels of influence seem possible under general conditions. In addition, there appear to be two additional channels which are of special importance to economies in transition. We briefly discuss these factors.

First, a legal challenge may lower the value of the defendant's equity. Peggy Wier, for example, estimated the enforcement costs imposed on shareholders whose mergers were challenged by antitrust enforcement agencies.¹⁵⁰ Only by demanding a higher return for committing capital will investors be compensated for the possible costs associated with a legal challenge.¹⁵¹ Second, increased enforcement activity may constrain innovative business behavior.¹⁵² This, in turn, lowers the *ex ante* value of any potential investment and may preclude affected efficient activities.¹⁵³ Finally, even firms that expect

20 J.L. & ECON. 229, 229 (1977) (stating that "with few exceptions, market concentration and industry profitability are positively correlated").

149. See George Bittlingmayer, *Output and Stock Prices When Antitrust Is Suspended: The Effects of the NIRA*, in THE CAUSES AND CONSEQUENCES OF ANTITRUST 287, 318 (Fred S. McChesney & William F. Shughart eds., 1995) (noting that "lax merger policies coincided with the stock booms . . . at the turn of the century, in the 1920s, and in the 1980s"). See generally Bittlingmayer, *Stock Returns*, *supra* note 121, at 1701 (discussing the history of antitrust enforcement in the United States and its effect on American business confidence).

150. Peggy Wier, *The Costs of Antimerger Lawsuits: Evidence from the Stock Market*, 11 J. FIN. ECON. 207, 216-23 (1983) (concluding that "the evidence presented . . . indicates that the prevention of allegedly illegal acquisitions is particularly costly for [the] firm's shareholders . . .").

151. See Bittlingmayer, *Stock Returns*, *supra* note 121, at 1727 (stating that antitrust filings decrease the value of a defendant's stock); CONRAD W. THOMAS, RISK AND OPPORTUNITY: A NEW APPROACH TO STOCK MARKET PROFITS 169 (1974) (concluding that stock investors demand a higher level of return with increased variability).

152. See Bittlingmayer, *Stock Returns*, *supra* note 121, at 1727.

153. George J. Stigler, *The Economic Effects of the Antitrust Laws*, in THE ORGANIZATION OF INDUSTRY 255, 266 (1968) (examining data on merger tendencies over the 1950s and 1960s and concluding that the "1950 anti-merger statute [amendment to the Clayton Act] has been a powerful discouragement to

no direct challenge may find the value of their investment lowered if a major antitrust initiative lowers business confidence.¹⁵⁴ Supreme Court antitrust decisions have ripple effects that extend beyond the direct effect on the challenged merger.¹⁵⁵

The two channels of influence particular to economies in transition are (a) the socio-political importance of early and prompt investment; and (b) the signalling benefits of successful investment returns on the part of the initial investors.¹⁵⁶ Most countries undergoing reforms have designated, as highest priority, policies to attract and sustain capital investments.¹⁵⁷ The urgency of attracting capital quickly is driven by potentially disruptive social strife that is associated with large numbers of displaced workers, deteriorating living standards, reduced growth, and other post-reform economic maladies.¹⁵⁸ Social disruptions threaten the business environment and may directly diminish forthcoming investments.¹⁵⁹ Clearly, an antitrust

horizontal mergers.”); Andre Shleifer & Robert W. Vishny, *The Takeover Wave of the 1980s*, 249 SCI. 745, 748 (1990) (arguing that “a return to the antitrust stringency of the 1950s and 1960s, where an acquisition that raised a firm’s market share from 5 to 7% could be disallowed, would be a mistake” because it could lead to an inefficient allocation of resources).

154. See McWilliams et al., *supra* note 26, at 519.

155. *Id.* at 518.

156. See generally Randi S. Cohen, *OPIC Insures Investment in Central and Eastern Europe and the Baltic States*, 1 NEW EUR. L. REV. 95 (discussing the substantial risks which dissuade investment in transitional economies and the efforts the U.S. government has made to facilitate investment).

157. See Jonathan C. Carlson, *A Missing Link in the International Debt Strategy: Trade Policy Reform in Industrial Nations*, 32 HOW. L.J. 771, 777 (1993) (describing the desires for “new infusions of international funding and market-oriented economic policies [to] spur economic growth and attract new investment to the indebted nations”).

158. See William K. Jones, *A Theory of Social Norms*, 1994 U. ILL. L. REV. 545, 561–63, 594–95 (1994) (discussing the importance of trying to achieve optimal levels of capital investments in order to reduce the implications of low standards of living).

159. According to the Chairman of the OECD Committee on Competition Law and Policy,

If a substantial part of the population does not regard government policies (for instance reforms in connection with privatization and deregulation) as socially equitable, this part will feel insecure and unfairly treated. There may be social unrest and that social unrest in turn may become an important factor in the economy. Recent developments in some Latin American countries indicate that neglect of the social side of a country’s development may easily endanger the success of economic reforms.

agency must be willing to incorporate these long-term economic considerations. However, because investment is so sorely needed, antitrust, with its strict focus on short-term anticompetitive effects, may not be the most adequate instrument to encourage capital investments in recently liberalized economies.¹⁶⁰

As for the second point, given the high degree of uncertainty prevalent in a number of transition economies, investors will only commit capital if they feel confident that a policy reversal, which would wipe out or reduce the expected value of their investment, is unlikely.¹⁶¹ The experience of other investors may serve to reduce this imputed likelihood of a policy reversal.¹⁶² Only if and when potential investors are assured that their original capital investments are not at serious risk, will more capital be forthcoming.¹⁶³ Thus, there is clearly a significant benefit from the initial capital that is attracted.¹⁶⁴ Accordingly, antitrust enforcement against initial investors must consider any adverse effects on future investment.

It would be foolhardy, especially in reforming economies, to claim that antitrust activity by itself, can have a determining effect on investment activity. Realistically, any detrimental

Kurt Stockmann, *Competition Policy in Transition: The Issues*, in COMPETITION AND COMPETITION POLICY: A COMPARATIVE ANALYSIS OF CENTRAL AND EASTERN EUROPE 83 (Saul Eastern & Martin Cave eds., 1993).

160. As noted in the main body, the current implementation of antitrust policy largely reflects conventional prescriptions based on short-run allocative efficiency. Yet, it is precisely this short-run theoretical foundation that renders antitrust at odds with the long-run capital needs of developing countries. The potential for conflict between short- and long-term objectives of competition policy has, of course, long been debated in antitrust. For a recent discussion similar to that found here, see Janusz A. Ordover, *Economic Foundations of Competition Policy*, in W. COMANOR ET AL., COMPETITION POLICY IN EUROPE AND NORTH AMERICA: ECONOMIC ISSUES AND INSTITUTIONS 7 (1991).

161. See Christopher T. Curtis, *The Legal Security of Economic Development Agreements*, 29 HARV. INT'L L.J. 317, 365 (1988) (arguing that economic development agreements reduce the political risks that discourage international investment).

162. Roger H. Gordon, *Fiscal Policy During the Transition in Eastern Europe*, in 2 THE TRANSITION IN EASTERN EUROPE 37, 47 (Olivier J. Blanchard et al. eds., 1993) (noting that capital flows from abroad have been limited possibly because of little confidence in the legal system).

163. Rodrik, *supra* note 137, at 20 (stating that reform packages which emphasize policy stability and sustainability are more likely to bring greater payoffs in terms of investment).

164. See SCHILLER, *supra* note 135, at 204-05 (explaining Keynes' view that a shift to a lower rate of investment follows from worsened expectations).

influence antitrust may have on investment is likely to be small in comparison to macroeconomic policies.¹⁶⁵ However, as often in microeconomics,¹⁶⁶ antitrust is likely to have an effect at the margin and the magnitude of the real effects will ultimately have to be established empirically.

In sum, we have argued that antitrust enforcement policy could have a detrimental influence on business investment. This effect could be small, especially when contrasted with more pervasive macroeconomic policies.¹⁶⁷ However, a careful examination of the microeconomic mechanisms that a reforming economy must develop reveals a stronger avenue for the potentially disruptive influence of antitrust. In particular, in the next section we note that to achieve full competitive parity with world competitors, a reforming economy must strive to develop institutions that facilitate the entry of specialized capital. Unaware of such needs, antitrust enforcers may act in a manner that increases the transaction costs of such investments.

IV. EFFECTS OF ANTITRUST ON COMPLEX CONTRACTS

Whereas the ease and reliability of contracting generally plays an important role in the competitive performance of a market economy, the ability to contract attains a special significance when parties are unable to legally enforce agreements. Under circumstances in which parties considering a mutually advantageous trading situation are unable to write a legally binding agreement, nonlegal market devices often emerge in the

165. Rodriguez & Williams, *supra* note 30, at 222-23.

166. See *id.* at 223 n.70 (citing George J. Stigler, *The Economic Effects of the Antitrust Laws*, in *THE ORGANIZATION OF INDUSTRY* 259 (1968) for the proposition that antitrust analysts' use of diverse and inefficient procedures limits the ability to judge the full effects of antitrust policies).

167. This is consistent with the results obtained. Andrew Stone et al., *Public Institutions and Private Transactions: The Legal and Regulatory Environment for Business Transactions in Brazil and Chile* 2 (World Bank Working Paper WPS 891, 1992) (unpublished manuscript, on file with the authors) ("The relative ranking of obstacles to growth perceived by Brazilian entrepreneurs makes clear that problems relating to legal and regulatory institutions take a distinct back seat to macroeconomic instability, and that Federal government economic policy imposes greater insecurity on property rights than any regulatory or judicial institutional weakness."). Similarly, others recommend that the highest priority should be assigned to macroeconomic stabilization and deconcentration policies in Eastern European countries. Spechler, *supra* note 126, at 195.

normal course of business to allow self-enforcement of contractual arrangements that enable the transaction.¹⁶⁸ We claim that these decentralized, self-enforcing contractual devices are: (a) the norm in reforming economies, and (b) especially susceptible to vigorous antitrust activity. In this section, we also observe that by reducing the ability of firms to commit to investment contracts, active antitrust activity may result in reduced growth rates for reforming economies.

A. *The Commitment Problem*

A detailed analysis of the commitment problem¹⁶⁹ is important for several reasons. Understanding how particular economies deal with the commitment problem helps explain the incentives to either contract or internally expand. Thus, the commitment issue has important implications for the organization of firms, their optimal size, the structure of markets, and ultimately, the performance of the economy.¹⁷⁰

Commitment problems also sharply limit the scope of contract.¹⁷¹ Since all contractual exchanges are not simultaneous, the absence of mechanisms to enforce commitments will bias investments toward economic activities which are either completed in a short period of time or completely under the control of one firm.¹⁷² One commentator, addressing the applicability

168. See Robert Sugden, *Spontaneous Order*, 3 J. ECON. PERSPECTIVES 85, 86 (1989). Often these devices are already present as cultural or ethnic norms, nonlegal historical institutions, or other forms of conduct present in business habits and lore. *Id.* "Although markets may work more smoothly when property rights are defined by formal laws and enforced by the state, they can come into existence and persist without any such external support." *Id.* This is especially true in illegal transactions in "markets in foreign currency, gambling, prostitution, alcohol and narcotics . . . [which] can continue despite the attempts of governments to suppress them . . . only because the participants recognize *de facto* property rights that the state does not." *Id.*

169. The commitment problem deals with the adverse effects on the economy which will occur if firms are not able to commit to future actions.

170. Steven N. Wiggins, *The Economics of the Firm and Contracts: A Selective Survey*, 147 J. INSTITUTIONAL & THEORETICAL ECON. 603, 604 (1991).

171. *Id.*

172. See David M. Becker, Comment, *Seaman's Direct Buying Service, Inc. v. Standard Oil Co.: Tortious Breach of the Covenant of Good Faith and Fair Dealing in a Noninsurance Commercial Contract Case*, 71 IOWA L. REV. 893, 908 (1986) (pointing out that a business may choose "not to enter a long-term agreement for lack of reasonable predictability of the enforceability of its' contracts."); see also Gillian K. Hadfield, *Problematic Relations: Franchising and the*

of New Institutional Economic Theory to development economics, has explained the point as follows:

Absent confidence in the governance supports for such [market] transactions, what could otherwise be viable middle-range transactions will flee to one of the poles—by moving to the spot market (attended by the sacrifice of asset specificity and resulting loss of productive value) or by moving to hierarchy (with the added bureaucratic cost load). A high-performance economy will support transactions of all three kinds rather than force polar choices. Widespread reliance on subcontracting will thus be observed in a high-performance economy.¹⁷³

Overall, the ability of a firm to commit to future actions allows a more efficient structure to evolve throughout a market economy. Thus, the inability of firms to commit is likely to have significant adverse effects on the productivity of the economy “[b]y attenuating contractual hazards that would otherwise preclude investments in transaction specific assets, more productive investments and organization will thereby result.”¹⁷⁴

The conclusion drawn from Williamson’s quote—that contract disincentives force transactions to occur in spot markets (or mandate vertical integration)¹⁷⁵—can best be understood by parting from the traditional neoclassical assumption of a world with no uncertainty. Such an approach to the analysis of commitment assumes that firms would not be concerned with commitment for future activity, presumably because every circumstance can be described through a complete contingent claims contract in which the parties specify the required perfor-

Law of Incomplete Contracts, 42 STAN. L. REV. 927, 955 (1990) (presenting the hypothesis that “neither franchisee nor franchisor would choose voluntarily to form a franchise relationship in the absence of legally enforceable commitments.”).

173. Oliver Williamson, *Institutions and Economic Organization: The Governance Perspective* 18 (Apr. 1994) (unpublished manuscript, on file with the authors) (paper presented at the Annual Conference on Development Economics, The World Bank, Washington D.C., Apr. 28–29, 1994).

174. *Id.* at 9.

175. See generally Kirk Monteverde & David J. Teece, *Appropriable Rents and Quasi-Vertical Integration*, 25 J.L. & ECON. 321 (1982) (standing for the proposition that quasi-vertical integration lessens the opportunity for one contracting party to appropriate the other’s quasi-rents).

mance in every state of the world. As a step towards more realism, an elementary model would incorporate a degree of uncertainty in contracting and the accompanying likelihood of strategic behavior. However, it would add the state as an institution to enforce agreements. The ready willingness of the state to sanction any breach limits the incentive of parties to act strategically and discourages nonperformance. With no additional particulars this model may work reasonably well for a set of simple contracts (i.e. simultaneous transactions with no asymmetry of information, etc). However, for a complex transaction, involving specific capital and spanning time, firms may choose self-enforcing agreements to consummate the business transaction, because relying on the state may not be the least costly means of enforcing contracts. Stuart Macauley, for example, in his study of contractual relations in American business,¹⁷⁶ noted that legal sanctions are seldom used to settle disputes in market systems.¹⁷⁷ The concept that arrangements will emerge to enhance the security of agreements where legal remedies are inadequate is relatively well known.¹⁷⁸ What is less well known is the particular contractual-efficiency hazards found in less developed economies.

Because of this analysis, one would expect informal mechanisms to be much more prevalent in reforming economies than they are in economies not in transition. In particular, privatizing ownership of industry leaves many more decisions to private bargaining, and thereby places a greater burden on the proper functioning of a legal system.¹⁷⁹ Unfortunately, the judiciary, typically the forum which is sought out in order to resolve contractual conflicts, often lags behind, rather than accompanying the modernization of the economy.¹⁸⁰

176. Stuart Macauley, *Non-Contractual Relations in Business: A Preliminary Study*, 28 AM. SOCIOLOGICAL REV. 55 (1963).

177. See *id.* at 61-62. Macauley attributed the infrequent use of legal sanctions in American business largely to competition and to the pressure to protect one's business reputation, which render such sanctions unnecessary. *Id.* at 63.

178. See Oliver E. Williamson, *Credible Commitments: Using Hostages to Support Exchange*, 73 AM. ECON. REV. 519, 520-21 (1983); Benjamin Klein & Keith B. Leffler, *The Role of Market Forces in Assuring Contractual Performance*, 89 J. POL. ECON. 615, 616 (1981).

179. See *Economy Overhaul 'Must for Diversification Success'*, MONEY CLIPS, Aug. 27, 1995, available in LEXIS, News Library, NON-US File, at *1.

180. Although not directly addressing antitrust issues, one group of commentators shares our basic premise:

A large body of literature has explored the roles which bilateral reciprocity plays in enforcing contracting behavior.¹⁸¹ Reputation is probably the best known factor that can create commitment.¹⁸² In fact, situations in which potential trading partners meet repeatedly in the marketplace, reputation has been shown to suffice to insure against breach of contract.¹⁸³ If reliance on reputation for the decentralized enforcement of contracts is a lower cost alternative to other types of enforcement,¹⁸⁴ then it should be observed in the marketplace as a guarantee that contractual commitments will be honored. Resource cost savings, which can be substantial, would be retained by the parties.¹⁸⁵ Unfortunately, a number of business relationships do not offer the potential for repeated interactions. Instead, the relationships may represent one-time business opportunities, which create a long-lived set of assets. In addition, our argument offers a much broader applicability by

Countries differ, of course, but there is clearly a cost to poor enforcement which is particularly high for an economy when an open market policy is introduced. This cost is both a deadweight loss and a systematic obstacle to transacting, and hence an obstacle to furthering the division of labor.

To a greater or lesser extent this cost is offset by private mechanisms that encourage enforcement. Yet, even where these substitute mechanisms function relatively well, the effect of poor enforcement is to place a heavy obstacle in the way of new entrants.

Robert M. Sherwood et al., *Judicial Systems and Economic Performance*, 34 Q. REV. ECON. & FIN. 101, 112-13 (1994). In concluding, the authors recommend that judicial systems be strengthened. *Id.* at 113 ("We are led to speculate that once it is demonstrated that effective judicial systems create, sustain and limit positive market behavior, then judicial effectiveness would be more easily seen as a priority for countries striving to open their markets."). Although we do not generally disagree, our recommendation suggests that better results will be achieved if private enforcement mechanisms are facilitated.

181. See generally Anthony T. Kronman, *Contract Law and the State of Nature*, 1 J.L. ECON. & ORGANIZATION 5 (1985); OLIVER WILLIAMSON, *THE ECONOMIC INSTITUTIONS OF CAPITALISM* chs. 1-3 (1985).

182. See Wiggins, *supra* note 170, at 640 (describing reputation as one of the three primary mechanisms for private contract enforcement); see also David Charny, *Nonlegal Sanctions in Commercial Relationships*, 104 HARV. L. REV. 375, 375; see Richard Morrison, *Efficient Breach of International Agreements*, 23 DENV. J. INT'L L. & POL'Y 183, 188 (1994) (stating that damaging a contractor's reputation is an extra-legal sanction which is sometimes more important than the possible legal sanctions).

183. Wiggins, *supra* note 170, at 640.

184. See Morrison, *supra* note 182, at 188.

185. See David W. Barnes, *Federal and State Philosophies in the Antitrust Law of Mergers*, 56 GEO. WASH. L. REV. 263, 267 (1988).

recognizing that repeated transactions may have to overcome first-mover problems.¹⁸⁶ It is this particular type of business relationship which we will next analyze.

Many real-world business transactions are sequential, one-time investment opportunities.¹⁸⁷ In these transactions, there typically exists some amount of time between the first party's commitment to the investment scheme and the second party's completion of the joint investment program.¹⁸⁸ These opportunities often require an investment in transaction-specific capital, which creates a set of assets that increase in value when used to produce output pursuant to a specific agreement with a given firm.¹⁸⁹ This need to sink capital before the business partner actually completes the transaction allows for various forms of opportunism to affect the returns to the investment or the value of the specific capital.¹⁹⁰ This is known as the "hold-up" problem, because strategic behavior by the second party may affect the profitability of the transaction, even foreclosing the transaction opportunity.¹⁹¹ In particular, unless it has committed to completing the transaction before the first firm invests, the second party may renege on the contract. Commitment is secured if the contract is self-enforcing; that is, if compliance with the contract is more profitable than opportunism. Given a number of other contractual parameters, the maximum allowable time for completion becomes an endogenous variable that can be compared to exogenous, technologically-driven contract-specific timing parameters. Our argument then emerges by examining the sensitivity of this time-to-completion variable to antitrust's influence. As the maximum allowable time for completion decreases due to active antitrust enforcement, many potential contracts become no longer viable. The loss of these investment contracts, will, in turn, lower the growth rate in a reforming economy.

186. See Wiggins, *supra* note 170, at 604 (stating when two parties in "a long term trading relationship" have to perform at different times, "the second party can only make limited commitments to follow through").

187. See *id.*

188. See *id.*

189. *Id.*

190. See Wiggins, *supra* note 170, at 640.

191. *Id.* at 608.

B. *The Model*¹⁹²

When an exchange is simultaneous, neither party need worry about enforcing the other's performance. But whenever the full performance of an exchange requires time (on one side or both), a situation may arise in which one party receives what they have bargained for before the other does. In such a situation, the second party can only rely on the promise of their trading partner to complete the still-unfinished job. Thus, in an arrangement to jointly complete a *single* sequential transaction, both parties recognize that the party finishing the transaction has an incentive to renege on promises to perform.

One mechanism which may overcome this incentive to renege involves designing the timing of the revenues from the project in a way which overcomes the potential for opportunism. In particular, the revenues may be divided into two earnings streams. The first would be relatively independent of the actions of the second firm, while the second would be dependent on the actions of the second firm. By strategically offering the second firm a significant share of the second payment stream, it may be possible to prevent opportunism. In particular, the contract is self-enforcing if the second firm is offered an ex-post payment that exceeds the value of the party's incentive to behave strategically (λ). Mathematically, if the value of completing the joint sequential transaction is V , then the payment to the party completing the sequential transaction can take the form of a fixed share (s) of the value V . Intuitively, the firm's promise to perform on the contract will be credible if its share of future returns once the project is completed is greater than its immediate return to cheating the first firm : $sV \geq \lambda$. A more general model would allow for a technologically based time parameter to account for the number of periods between the first firm's initial investment and the completion of the project. Thus, the equation becomes $sV/r \geq t\lambda$, where s remains the share of the return, V becomes the annualized return, r is the discount rate, and t is the number of periods required to complete the invest-

192. For the basic model discussed in this section, see generally Wiggins, *supra* note 170. The application and subsequent extension of the model into the context of antitrust in developing countries is, of course, the authors'.

ment.¹⁹³ Within this formulation, the contractual horizon, t , takes on the implicit representation of contractual complexity.

A fundamental objective of a party entering into a contractual agreement should be to minimize the potential for opportunism. In effect, all the terms of the contract can be adjusted to maximize the chance for successful completion of the transaction. For example, the terms of the contract can mandate certain actions which reduce the potential gain from opportunism (the parameter λ), or shift revenues for the second firm from an initial period to the final period to increase the share of the marginal returns going to the second party (increase parameter s). Also, it may be possible to increase the value of the business, given successful completion of the investment, by sacrificing initial revenues to create more future revenues for the firms to share.

Adjustments in the contractual terms can give rise to antitrust issues linked to either vertical or horizontal agreements. Thus, in terms of functional notation, the coefficients of the model $\lambda(a)$, $s(a)$ and even $V(a)$ become functions of antitrust enforcement activity, " a ."

1. Vertical Agreements

Vertical restraints, which limit the independence of two firms involved in a long-term customer-supplier relationship so as to reduce the incentive for opportunism, are regular targets of antitrust enforcement. In numerous vertical agreements, a manufacturer invests first (often building a brand name) to create a product and then expects numerous retailers to invest in customer services.¹⁹⁴ Rather than investing in service, retailers may opportunistically reduce price and attempt to sell the product to price-sensitive customers who have already obtained services from other retailers. In effect, this opportunism drives the service-providing retailers out of business and destroys the manufacturer's distribution scheme. To minimize the potential for opportunism, manufacturers frequently use restrictions on resale price (RPM) to reduce the scope of opportunism available to the downstream retailer.¹⁹⁵ While the retailer

193. The potential for opportunism is implicitly discounted in the model.

194. This represents a slight generalization of the standard service model in which services are provided directly to the consumer.

195. Manufacturers can also use restrictions on sales territories to reduce the

may still be able to opportunistically evade performing on the marketing agreement, cheating is likely to be less profitable. Moreover, it is easier to observe cheating and terminate the business relationship with the offending firm before the manufacturer's distribution system is totally lost. By reducing the profitability of opportunism, RPM makes the vertical contracts easier to enforce. In terms of the model, RPM reduces λ and hence makes it more likely that the contract will be self-enforcing.

Naive enforcement of the standard antitrust prohibitions against vertical price agreements makes these sophisticated contracts less likely to be implemented. In terms of our model, $\partial\lambda/\partial a < 0$. For example, the use of per se prohibitions against RPM agreements will force manufacturers to use less efficient nonprice contractual clauses to deter opportunism. As costs rise, some potentially longer contracts will not be supported by the economy and thus opportunities for development will be lost. Additional antitrust attacks against various nonprice mechanisms will further reduce the ability of firms to enter into long-term vertical contracts.

Exclusive dealing agreements may also reduce the profitability of opportunism by linking more tightly the prospects of the two businesses. The second-moving downstream firm commits itself to only deal with one upstream firm, so that the failure of the venture adversely affects the second firm's business prospects. Thus, the second firm is more motivated to successfully complete the investment program. Note that the upstream firm is able to deal with more than one downstream firm, so it may survive any particular downstream firm's opportunism. Given that the upstream firm invests in the project first, the downstream firms do not need to fear incidents of opportunism.

Active antitrust enforcement may prevent these vertical contracts. By precluding downstream firms from signing exclusive contracts, regulators may make various business relationships untenable. Unless other schemes can be devised, certain contracts will not occur. While an upstream firm could attempt to simulate exclusive dealing systems by only contracting with downstream firms that will unilaterally limit themselves to one

upstream supplier, the downstream firms could cheat and contract with other suppliers once the initial investment is sunk. Alternatively, the antitrust regulators could attack the upstream firms for refusal to deal with various other downstream firms. Under this doctrine, one firm (usually large) has some type of duty to deal with trading partners. Such an antitrust policy creates a number of problems for a market economy. In addition to making it more difficult for an upstream firm to be selective in its business relationships to create incentives for self-enforcing contracts, an active refusal-to-deal policy could force firms to deal with others that they expect to be opportunistic. Given the expected opportunism, the initial firm will try to avoid committing to investments, further dooming the project to failure. Alternatively, a firm may just avoid a type of business relationship so as not to be forced into unprofitable investments. Finally, one could observe that the entire policy is doomed to failure, because the upstream firm could set a high price instead of refuse to deal. Thus, an active refusal-to-deal policy could degenerate into price setting by the government regulators.

Another type of vertical contract may enable manufacturers to offer different shares of the profit stream to different retailers. It is possible that some retailers will require higher payments to refrain from opportunism than others, especially if the retailers sell in different markets. Thus, the manufacturer may need to devise schemes with high α for the retailers in order to make the contract self-enforcing. The manufacturer could recoup the higher final payment by accepting a hostage or collateral from the retailer in the initial period. Thus, this would result in a distribution system in which "favored" retailers appear to earn high profits.

Naive enforcement of antitrust regulations against price discrimination may preclude this type of sophisticated contract by mandating a single price for each type of business relationship. Although manufacturers could claim an efficiency justification for its pricing behavior, the firm is likely to have problems proving its policy is efficient, because enforcers usually take a narrow view of efficiencies. As such, the pricing formulas described above would be illegal and the firm would have to use a less efficient technique to control opportunism. For example, contracting may prove impossible in some local markets, so the firm would have to vertically integrate into these areas to sell

its product. Thus, efficient contracting solutions are lost under active antitrust enforcement.

It may even be possible to adjust the timing of payments to enhance the future attractiveness of the investment. For example, tying schemes often offer customers a low price for the purchase of a product in exchange for a commitment to buy related products from the firm at higher prices.¹⁹⁶ While this type of tying is generally considered to be a price discrimination scheme in which intense users of the system are charged more than casual users, it could also serve to shift the flow of revenue to the business partners. As long-term profits are dependent on a successful product introduction, each business partner would have more of an incentive to perform on the contract. Thus, tying may make certain contracts self-enforcing.

However, under an active antitrust policy, these contracts could be viewed as a type of illegal tie. Tying is often considered illegal per se, so no efficiency defense could be mounted. If enforcement activity prevents the partners from using tying, other less efficient contractual terms would have to be devised to make the contract self-enforcing. In some situations, no terms may exist, so the contract would not be viable.

2. *Horizontal Agreements*

Horizontal contracts among direct competitors could also include terms which seek to control opportunism. In fact, horizontal agreements are probably subject to the highest risk of opportunism, because the two firms which are parties to the contract are direct competitors. Joint venture agreements include restrictions that are designed to prevent either firm from gaining an inappropriate advantage. Although the exact nature of the restrictions may depend on the type of agreement (i.e. technology, marketing, or manufacturing) it is possible that restrictions on price and output may be necessary. In effect, these joint ventures may include sufficient restraints to effectively merge the two firms' operations in a particular area.

196. An example of a classic tie would be the sale of copy machines at low prices in order to induce firms to pay high prices for service contracts. This type of contract may also allow a manufacturer to share the risk of business failure. If the technology fails in the marketplace, the manufacturer captures little in the way of premium-priced service business. On the other hand, if the product is successful, the manufacturer earns high profits on the service business.

While a firm may still be able to cheat on the joint venture contract, the potential profitability of the opportunism is significantly reduced because the business partner could quickly detect the independent behavior and undertake actions to reduce its profitability. As long as the contractual terms reduce λ , more complex contracts are likely to be viable.

Many joint venture restrictions are likely to be considered illegal under an active antitrust policy. Although the merger analogy could be appropriate, standard Western antitrust procedure gives only limited consideration to efficiencies. Thus, a standard merger policy would find joint ventures illegal in many concentrated industries, unless those agreements related to joint pricing and output are dropped. However, it is these very agreements that reduce the potential for opportunism. If the venture partners must use more costly mechanisms, some complex contracts will not be practical.

Overall, these examples show how numerous standard Western antitrust policies limit the ability of the market to devise sophisticated self-enforcing contracts. While one could argue that the same effects are felt in developed economies, the weaker legal system in reforming economies is likely to force firms in these markets to rely almost entirely on their ability to write self-enforcing contracts. Given that the economic basis of all of these antitrust activities is generally considered to be weak,¹⁹⁷ these activist antitrust policies are, at best, not likely to benefit reforming economies.

This conclusion stands in stark contrast to the strong theoretical observation that monopolies are able to adversely effect markets. However, monopolies are generally not necessary for complex contracts. The only questionable situation involves horizontal joint ventures in which all of the firms in a market participate. While such a venture is unlikely to be necessary to produce an existing good, it may be necessary for an innovation. If monopoly is the only way the innovation will be introduced to the economy, the joint venture would be justified.¹⁹⁸ The risk of policy errors is minimized by the world-market structure of most innovation markets, so entry tends to limit the market

197. See BORK *supra* note 7, at 4, 7.

198. Another concern is the joint venture would lead to monopolization in other markets that the partners compete in. Such a monopoly could be attacked independent of the joint venture.

power of any domestic joint venture. Overall, policies designed to attack naked monopoly do not appear to have an adverse effect on the ability to contract and thus would be appropriate.

V. CONCLUDING COMMENTS

Widespread perceptions of the virtues of antitrust policies diverge significantly from actual problems with the operational aspects of these policies. Challenging allocative distortions due to market power is an unassailable theoretical position. This premise constitutes the basis of our confidence in recommending an antimonopoly component to a liberalization program. However, in the developed world, antitrust has grown far beyond a simple attack on monopoly. While there may be some narrative linking each aspect of antitrust enforcement to the monopoly problem, the underlying assumptions of the typical enforcement program are so extreme as to render the constituent concept almost useless. Taken as a whole, antitrust as practiced in the developed world may have adverse effects on a reform policy in the developing world, and may stunt growth.

The arguments advanced here have implications for a competition policy intended to serve the goals of economic efficiency and consumer welfare. To be sure, any policy prescription must remain fairly general. Yet, the arguments do create a critical framework for policy analysis by rebutting presumptions and evaluating particular factual matters. Some particular observations and recommendations follow.

First, a necessary condition for effectively and *simultaneously* accommodating the two policy goals of antitrust law—allocative efficiency and increased investment—is the government's ability to restrain the injudicious application of antitrust laws. It is necessary to keep antitrust initiatives focused directly on the problem of monopoly pricing. Any attempts to prosecute agreements because of their purported monopolistic effects runs the risk of attacking competitive conduct and reduces incentives to invest in the economy. If a focused approach to antitrust is not possible, it may be wise to relegate the adoption of antitrust policies to a period of long-run equilibrium.

If limited in the type and conditions of contracts into which they can enter by excessive antitrust scrutiny, transition economies may never obtain the contractual sophistication required to compete adequately in an international market economy.

Clearly, as it greatly facilitates foreign and domestic investment, reforming economies must foster the development of mechanisms which encourage self-enforcing agreements.

Our hypothesis that institutions affect economic performance is, as Douglas North has noted,¹⁹⁹ hardly controversial. North observes that the institutional requirements essential to create efficient markets entail a set of political and economic institutions that provide for low transaction costs and credible commitment, thus making possible the efficient factor and product markets which underlie economic growth. Because they will influence the post-transition equilibrium, a careful understanding of the *emergence* of new institutions in liberalizing economies adds another dimension to the research agenda. Antitrust, despite its theoretical underpinnings, may not be a salutary institution for emerging market economies.

199. Douglas C. North, *Institutions, Ideology, and Economic Performance*, 11 CATO J. 477, 477 (1992) (stating that "[i]nstitutions affect economic performance by determining (along with the technology used) the cost of transacting and producing").