

Convergence

On the art of slaying dragons: the case against the International Competition Network

By *A E Rodriguez**

In one of his books, Rene Thom recounted the story of a Chinese warrior who spent years learning the art of slaying dragons. The warrior's quest took him to all corners of China, much practice and complete devotion to learning. At the end of ten years, the warrior, finally satisfied, decided he was done. Knowing absolutely all there was to know about the art of slaying dragons he set forth into the world only to realise, to his dismay, that there were no dragons. Pondering his future, he came to a masterly solution: he decided to teach how to slay dragons.

Despite the recent downturn, there has been an enormous growth in the proportion of trade to domestic output - a measure of the openness of an economy - reflecting the way in which the world's economies are growing more integrated and global.

Worldwide, the merchandise export share of production has more than doubled over the last 45 years. The manufactured export share of production has almost quadrupled over the same period. Developed and developing economies alike have experienced increases in their export share of GDP.

This explosion in trade is largely due to the remarkable success of the pro-market reforms of the last decade. The elimination or reduction of tariffs, combined with other micro- and macroeconomic liberalisation, has been adopted by many developing countries to facilitate international trade and commerce.

However, trade-driven gains and growth are facing an insidious challenge by competition regulation advocates.

The rise of competition policy

In addition to the traditional liberalisation programmes, pro-market reforms in many countries also contained legislation calling for regulatory oversight of the

private sector, known generally as "competition policy."

Practically all countries either have active enforcement agencies already or are committed to setting them up. While these antitrust agencies and their mission may be familiar to most western nations, they are an entirely novel undertaking for most of the rest of the world.

Understandably, treading uncharted territories has led to poor policy, hidden protectionism, unwarranted enforcement activity, and a general increase in the costs of doing business.

The ensuing regulatory mess increases the cost of transnational mergers, reduces the frequency of mergers and, of course, adds to the associated attorney billings.

Not surprisingly, operational problems and the inherently contradictory objectives of these regulatory programmes have led to calls for some form of coordination of antitrust review and enforcement policies between countries. The new fix for these problems is the International Competition Network (ICN).

The ICN tells us that its objective is to "help bring international antitrust enforcement into the 21st century. By enhancing convergence and cooperation, ICN will promote more efficient, effective antitrust enforcement worldwide. Consistency in enforcement policy and elimination of unnecessary or duplicative procedural burdens stands to benefit consumers and businesses around the globe."

As it is structured today, the ICN appears to be one more taxpayer-funded boondoggle that makes senior government officials' mouths water. Aside from spending money, how harmful can it be? And is it addressing a real problem?

To find the answer, one must first question the need for vigorous antitrust authorities in developing countries.

Second, if the ICN becomes more than a good excuse for a field trip abroad, it is doubtful that it will achieve its goal of promoting effective antitrust.

The ICN and its progenitors

International competition policy coordination is not a new concept. Over the past half-century there have been several unsuccessful proposals.

The first, by UNCTAD in 1948 and known as the "Havana Charter," provided for the creation of the International Trade Organisation (ITO) as a specialised agency of the United Nations.

Due to historical circumstances, the ITO did not become a reality at the time. Amended and transformed, it became the General Agreement on Tariffs and Trade (GATT) - now the World Trade Organization (WTO) - the only multilateral institution governing international trade, but one still without jurisdiction over international antitrust matters.

The concept for the ICN came directly out of recommendations of the International Competition Advisory Committee (ICPAC). The membership of ICPAC, established in November of 1997 by Attorney General Janet Reno and Assistant Attorney General for Antitrust, Joel Klein, is a select gathering of leading competition policy scholars and practitioners.

Arguments in support of the export of competition policy

Perhaps the most perplexing argument in support of international regulation of competition, stated sometimes implicitly, sometimes explicitly, is that increased trade increases the likelihood of anticompetitive activity.

For example, chapter 4 of the ICPAC report points to the upswing in prosecutorial activity by US antitrust

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authorities against multinational cartels as evidence of more cartel activity.

Sensibly, the ICPAC report is very careful to acknowledge the obvious question of whether this statistic implies an increase in cartel activity or whether it is simply an increase in detection capabilities, or an increase in prosecutorial zeal. The report concludes: "the scope and incidence of international cartels are important matters for further examination and recommends further consideration of this issue by governments and other experts."

As a conclusion, this cannot be faulted. However, ICPAC proceeds untroubled by the possibility that the answer may be that there is no increase in the incidence of cartel activity.

This "trade begets cartels" argument turns on two key premises. The first is the belief that a number of multinationals' actions (particularly in vertical arrangements) are designed to gain or enhance anticompetitive market power rather than to increase the efficiency of their operations. Some commentators claim that tacit cooperation to avoid price wars through price leadership and other coordination is common in industries with large multinational firms.

Another keystone argument is that international competitors, often in coordination with their home countries' governments, collectively seek non-tariff barriers and other protectionist devices in their home markets when entering foreign markets.

A common example of this is the

argument that the elimination of trade barriers in the European Union has the effect of creating "fortress Europe." A protected Europe will reduce economic or social dislocations posed by international competition.

One has to question the ability of antitrust agencies to address government-approved protectionism.

Trade reduces the desirability of exporting antitrust

Contrary to the view of ICN proponents, we believe that trade, and the concurrent expansion of geographical markets, is likely to reduce the likelihood of cartelisation. All else being equal, import competition is a countervailing force against market power in the hands of domestic firms.

Clearly, successful cartelisation yields private gains. Domestic firms may respond to trade liberalisation and a prospective reduction in profits due to increased import competition by threatening to collude.

However, the effectiveness of a domestic cartel facing new import competition is doubtful. Presumably, if more collusion were profitable and enforceable before trade was liberalised, one would expect that collusion would already be occurring.

Furthermore, increased trade lowers the residual demand facing domestic firms, making collusion less profitable and therefore less likely. While the domestic firms may invite the new foreign competitor into the cartel, it is unclear why a foreign rival, especially one with a cost advantage, would willingly choose to participate in such a cartel because of the

different incentives a foreign firm would have relative to the incumbent firms.

The empty promise of competition advocacy

While vigorous antitrust enforcement may not be desirable for developing countries, many have argued that the new agencies can speak collectively in what is known as competition advocacy to protect us from protectionist forces. In fact, the ICN has recently published a report vigorously advancing competition advocacy.

The competition advocacy role is nonsensical, often merely stating the obvious and usurping a role that private sector think-tanks would be only too happy to provide.

The seeking of preferential treatment, prevalent in all societies, is especially vibrant in transition economies. For example, the recent roll-backs of market gains and short-lived liberalisations in various democratic countries are the perfect example of the power of domestic pressure groups. When the workers, small business owners, environmentalists and often large business owners march on the streets demanding protection from imports, governments listen.

But the competition advocates' conceit is that the competition agency will be able to quantify the seeming economic losses, and *ipso facto* persuade decision makers that the roll-backs are economically inefficient and counterproductive. How many agencies will willingly challenge the protectionist plans of a populist agriculture minister and live to tell the tale?

A competition agency's effectiveness in confronting legitimate, popular and

Competition Law Forum

A forum for research, discussion and policy formulation has been founded by the British Institute of International and Comparative Law. It will meet four times a year in London and Brussels to consider the most pressing issues in current competition law and policy.

Its first meeting, on 17 March 2003, will cover merger review in Europe and its second, on 19 June, the "modernisation" of EU competition policy enforcement through Regulation 1/2003. The work of the International

Competition Network will undoubtedly be high on the Forum's agenda.

Like its parent body, the CLF will be rigorously independent. On a topic chosen for in-depth treatment, the aim is to establish a collective voice for use in dialogue with governments, policy-makers and regulators.

Membership will ensure that this is not just another lobby group. It is open only to named individuals, who are likely to be practitioners, business executives, academics, regulators or other public officials, policy advisers or representatives of interest groups,

such as trade unions or consumer bodies. However, the fee of £3,500 a year is likely to mean that the lawyers and economists who join are closely associated with an organisation of some sort.

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democratic protestations is limited. With nothing to challenge legally, and with little - if any - political or popular support, the competition agency's contribution is largely relegated to pointing out the inefficiency-enhancing consequences of populist demands.

In fact, over the past ten years, agencies' effectiveness has been remarkably unimpressive. Even if governmental competition advocates were effective, developing countries do not need a government-supported research agency to tell them that eliminating the subsidies on gasoline prices is inefficient.

The Cato Institutes of the world do it better and more effectively, with someone else paying for the lecture.

Harmonisation of antitrust

There is considerable debate as to what will be the future scope of the ICN. The various paths of antitrust harmonisation advocated by its proponents range in their scope from standardising merger filing forms, to modest bilateral cooperation in enforcement actions, all the way to the more ambitious goal of establishing binding global competition codes.

The countries that are to be parties to these proposed agreements also vary. Some harmonisation proposals are limited to countries in regional trading blocks or to parties to existing free trade agreements, while others propose global membership.

Would collaboration minimise self-serving economic policies by individual countries? Yes. However, that job is already filled by the WTO.

One would like harmonisation of competition matters to allow countries to commit to restricting other countries' discretion to unilaterally grant preferential treatment to foreign and domestic interest groups. This role seems unsuited to antitrust agencies.

If the problem is governmental actions, agencies regulating the private sector are not up to the task. The enforcement of antitrust law is not the same as agreeing to rescind preferential trade practices. Competition advocacy by antitrust agencies is likely to be ineffective.

In principle, eroding asymmetries in the regulation and enforcement of competition policy can prevent governmental favouritism designed to benefit domestic economic actors. The

removal of distortions can improve overall economic performance in international markets.

The WTO was formed to establish a framework to reconcile conflicts between domestic policies and foreign interests. Further, the WTO was established in a way that could impose genuine costs on countries granting favourable preference to interest groups.

A global antitrust agency would not have this power. Harmonisation of competition policy would be less adept at achieving a limitation of group subsidies than the WTO. Substantive and practical differences between legal and political traditions and the widely divergent goals of industrial and other economic policies between countries may be unbridgeable.

Let them pay the merger tax

One potential goal of the ICN is to establish standardised reporting procedures that would reduce multinational firms' costs of transacting with the domestic antitrust enforcement agencies of the various host countries. A common agreement would surely entail similar or identical document compliance and reporting requirements from parties to transactions that encompass various political jurisdictions.

There is something pernicious about this reasoning. Antitrust advocates have vigorously supported and encouraged developing countries in adopting antitrust programmes without considering whether they were necessary.

In turn, these same advocates point to the numerous incipient agencies as a potential source of increased transaction costs. Harmonisation is then offered as a means of overcoming this problem.

However, the lion's share of the costs of antitrust compliance comes from further requests for documents after the initial filings. This further information is largely related to the domestic characteristics of the transactions and cannot be standardised. Standardising reporting requirements can offer only a very modest opportunity to reduce the costs of compliance.

Professor Andrew Kleit, calling the burdensome and costly Federal Trade Commission document requests a "merger tax," has proposed that the government be required to pay firms under investigation for its document acquisition in much the same way that the

government is required to pay compensation for property "takings."

The "Kleit solution" should perhaps be extended to all antitrust agencies worldwide, and amended to include the costs of translations and travel.

Standardisation of filing requirements has the potential to add costs to mergers. A standard form could encourage some countries to increase the number of reportable mergers. With a standardised requirement, writing such a law would not be costly. Firms wishing to merge would only have to make another copy - and, of course, pay the appropriate filing fee. The country could raise revenues without even examining the submitted forms.

The sharing of useless information

International regulation commentators have suggested that, rather than a formal code, international harmonisation of antitrust should be accomplished through the exchange of information between enforcement agencies.

The localised nature of much antitrust enforcement suggests that information exchange is likely to be largely ineffective. For instance, antitrust methodology, such as defining product markets, is almost always satisfied with information available domestically.

Most current antitrust enforcement activities focus on practices that are deemed likely to reduce domestic, but not foreign, consumer welfare. In these matters, it is unclear how information gathered by another country would be useful in determining the scope and breadth of product and geographical markets, or other factors relating to the likelihood of anticompetitive behaviour limited to one country.

The exchange of information, if useful, could change an agency's effort in its investigations. When multiple agencies investigate a matter, there is always the incentive for some agencies to free ride off the information collection and efforts of other agencies.

For any individual country, the direction of the externality derived from antitrust enforcement - whether favourable or onerous - is unclear.

On the one hand, vigorous antitrust enforcement by one country may decrease the likelihood of anticompetitive behavior for a neighbouring one. On the other,



vigorous antitrust activity in one country may foster protectionist activities by a third country, which may actually increase the likelihood of (government-inspired) anticompetitive behaviour.

Another global bureaucracy?

Some particularly enthusiastic ICN proponents may envision the harmonisation of antitrust between countries as establishing a global agency enforcing an international competition code. This seems an unlikely outcome due to philosophical and other differences between countries with different competition policy histories.

Nations currently define and administer competition policies very differently. In the United States, antitrust law is constructed to protect consumers from anticompetitive private practices, but not from government-supported activity. In Japan, competition policy historically has subordinated consumer interests to policies intended to strengthen and favour domestic producers. In the European Union, competition policy is designed to promote economic and political integration and enhance economic competitiveness *vis-à-vis* non-EU firms.

A more symmetric global competition policy might reduce the distortions brought about by individual countries setting competition policies separately. This may be neither possible nor desirable.

Professor Spencer Waller has noted that neither the transfer of existing national laws nor the international harmonisation of competition law offers any realistic prospect for the desired outcomes.

United States antitrust law represents a unique social and historical construct of events and themes that may not be easily grafted into a foreign legal setting. Thus, antitrust enforcement may be significantly more difficult for reforming economies.

This reflects the danger of what has been called the "transferability problem". It neglects the cultural, institutional, economic and political obstacles to the implementation of an antitrust policy.

Former FTC Chairman Pitofsky noted the following: "My sense is that a [world antitrust code] is not going to happen in the future. You can't expect countries at such different levels of economic development to have all the same answers

to competition policy issues."

There are a number of idiosyncratic elements that may preclude American antitrust learning from functioning as effectively in different settings as it has in the United States. A deep historical distrust of corporate or business power, or at times of bigness itself, is historically reflected in US antitrust laws.

Professor William Comanor argues that, to a large extent, two sets of interests – the fear of corporate power and the search for corporate legitimacy – provide the critical support for the American antitrust laws.

Professor Robert Pitofsky observes that the decentralisation of decision-making, the dispersion of power, and a higher standard of business ethics, as legitimate social objectives, may lay equal claim to guiding policy.

Let us hope that a closer inspection of foreign legal traditions, goals and objectives may temper the zeal of regulation advocates.

It's their burden of proof

The globalisation of the world economy has resulted in a dramatic reduction in the economic distances between nations. This process has also emphasised differences in national economic policies, practices and traditions and these differences can cause substantial transaction costs.

Policy coordination and collaboration should be encouraged if they can reduce these transaction costs. However, competition policy does not fall naturally into this category of cost-reducing collaboration.

In fact, coordination of competition policy may actually reduce legitimate antitrust enforcement efforts and thereby reduce consumer welfare.

Harmonisation advocates should address the issues in more depth, offer less theoretical rationales and more empirical proof. In particular, to fully evaluate harmonisation proposals, they need to

- (a) assess the magnitude of costs caused by international cartel activity
- (b) measure the increase in deterrence of anticompetitive activity associated with harmonisation efforts

For the former, little international cartel activity could be expected because, in general, increased trade leads to more competition and international cartels are

more likely to be unstable due to differing incentives among their members. Moreover, with increasing international competition and correspondingly larger geographical markets, one expects collusion to be the exception.

For the latter, the benefits of harmonisation can be expected to be slight because little valuable information remains unavailable to the competition authorities during the course of a normal investigation. Furthermore, it may be difficult to persuade countries to renounce important elements of sovereignty in return for information-sharing mechanisms that convey few tangible benefits.

- (c) if they manage to show (a) and (b) above, the ICN should demonstrate why the current toolkits are insufficient for the task, and
- (d) the ICN should demonstrate why curtailing the power or shuttering the myriad competition agencies outright in most countries would not be a better solution than the troubling vision of the ICN

Put simply, the burden is on harmonisation supporters to establish the empirical predicate before we adopt more of their solutions.

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