

COMPETITION AND TRADE POLICIES

Coherence or conflict?

*Edited by
Einar Hope and Per Maeleng*



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PREFACE

This book documents the proceedings of the conference 'Competition Policies for an Integrated World Economy', held in Oslo on 13-14 June 1996, and organized by the Norwegian Competition Authority.

The conference was intended as a meeting place for practitioners of competition policy in competition authorities and representatives for the academic and research communities and the business community. The proceedings include invited contributions from leading experts within each field. The contributions consist partly of plenary session papers and partly of background documentation for panel discussions. Some panellists have prepared full-length papers for their panel presentations while others have written shorter statements. This implies that the level and style of presentation of the articles in the book may vary somewhat more than one normally finds in proceedings from purely scientific conferences. Hopefully, this variety of approaches makes the book the more interesting and accessible to a broader readership than would otherwise have been the case with a more narrow approach.

The Norwegian Competition Authority is grateful to the Norwegian Ministries of Government Administration and Foreign Affairs, respectively, for financial support to the conference. A number of my colleagues at the Authority rendered invaluable assistance in connection with the arrangement; I would like especially to mention Unni Bache, Øyvind Christensen, Anne Sofie Gjestrum, Per Mæleng, Laila Rundtom, Knut Wettermark and Ellen Aas. Per Mæleng's skills and patience have also been invaluable in the editorial process.

The subject of the book – interlinkages between competition and trade policies and the development of an effective competition policy for an integrated world economy – is one of the most important and challenging questions competition policy-makers presently face. It is also a fertile research area. I hope that the book will contribute to this policy debate with new knowledge and insights, and that it will stimulate further analytical and policy-oriented work.

Einar Hope
Director General
Oslo, December 1996

COMPETITION AND TRADE POLICIES

Is there an inherent conflict between competition and trade policies, or are the two policy areas complementing each other? The relationship between competition and trade policies, and the development of an effective competition policy for an integrated world economy, is one of the most important and challenging issues policy-makers presently face. This book examines current debates around competition and trade policy interactions, and discusses the need for new policy initiatives in an international context.

The papers in this collection are presented in five parts. Part I contains a discussion of some general principles and issues, while Part II is more specifically related to network industries and telecommunications. Part III examines some development policy aspects. Part IV presents European Economic Area policies and proposals, notably the initiative taken by Commissioner for Competition, Karel van Miert, for developing an EU competition policy for the new trade order. Parts V and VI contain background papers for panel discussions on vertical restraints and business perspectives, respectively, in an international trade and competition policy context.

Einar Hope is Director General of Competition for the Norwegian Competition Authority, and Professor of Economics at the Norwegian School of Economics and Business Administration, Bergen, Norway. His fields of research include industrial organization, energy economics and financial economics. He has founded three research institutions for applied economic research, and has been actively involved in work on regulatory reforms in Norway, especially in the electricity industry.

Per Maeleng has been Head of Division for Information in the Norwegian Competition Authority, and is now editor of a new journal on competition policy, for publication by the Norwegian Competition Authority in 1998. He is preparing a doctorate thesis in comparative literature and has been publishing articles on literature in various publications in Norway and abroad.

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Coherence or conflict?
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CONTENTS

<i>List of illustrations</i>	viii
<i>List of contributors</i>	ix
<i>Preface</i>	xi
1 Introduction	1
EINAR HOPE	
PART I	
Competition and trade	11
2 International trade and competition policy	13
FREDERIC M. SCHERER	
3 Competition and/or trade policy?	31
LEONARD WAVERMAN	
4 Basic principles for an international antitrust code	46
ULRICH IMMENGA	
5 A small open economy perspective on international competition policy	57
VICTOR D. NORMAN	
6 Unilateral refusals to license intellectual property and international competition policy	65
RICHARD J. GILBERT AND CARL SHAPIRO	

CONTENTS

PART II	
Network industries	79
7 Access and interconnection in network industries	81
HENRY ERGAS	
8 Regulation, competition policy and market access negotiations: lessons from the telecommunications sector	115
BERNARD HOEKMAN, PATRICK LOW AND PETROS C. MAVROIDIS	
 PART III	
Development aspects	141
9 A brief note on the role of competition policy in economic development	143
R. SHYAM KHEMANI	
10 Competition at the crossroads	152
PHILIPPE BRUSICK	
 PART IV	
European Economic Area policies	181
11 EU competition policy in the new trade order	183
KAREL VAN MIERT	
12 The competition policy in the European Economic Area: a unique system of international cooperation	192
KNUT ALMESTAD	
 PART V	
Vertical restraints	199
13 Reflections on vertical restraints of trade and national competition laws in an integrated world economy	201
STEPHEN CALKINS	
14 Vertical restraints: a United Kingdom perspective	220
MARTIN HOWE	

CONTENTS

15	EU competition policy on vertical restraints CHRISTOPHER JONES	233
16	Competition policy regarding vertical trade restraints: a Japanese view HIDEAKI KOBAYASHI	262
17	Vertical restraints of trade and national competition laws in an integrated world economy DIETER WOLF	269
PART VI Business perspectives		275
18	International competition law in the 1990s: a Canadian perspective CALVIN S. GOLDMAN AND MILOS BARUTCISKI	277
19	International competition policies: a business perspective – Furthering effective procedures within Europe P. M. A. L. PLOMPEN	297
20	Merger control in the EU and the treatment of strategic alliances MICHAEL J. REYNOLDS	304
	<i>Index</i>	337

ILLUSTRATIONS

Figures

2.1	Movement of Saskatchewan potash prices, 1986-93	22
2.2	Cement price differences among six EC nations, 1983-91	24
5.1	Single-industry demand and marginal cost curves	59

Tables

3.1	Adoption of competition law in selected developing and emerging market economies	43
7.1	A comparison of access pricing approaches	105-6

INTRODUCTION

Einar Hope

A number of developments have taken place in recent years in the international economy which have changed fundamentally the conditions for competition. This imposes new requirements and demands on policy-makers developing an effective competition policy for the efficient use of resources in an international context. The globalization of economic activity and relations, rapid technological developments, and the progressive elimination of trade restraints are some of the most important factors to be mentioned. As a consequence, markets have become more open and interconnected, and competition is increasingly transcending national boundaries and penetrating deeply into national markets. The process of trade liberalization has to some extent shifted the emphasis from trade restraints to competition restraints as obstacles to international investment and trade flows. This has led to an increased awareness of inter-linkages between trade and competition policies and their consequences for the international trade system.

Attention is being increasingly devoted to these issues around the world; at the political level as well as from an institutional and analytical perspective. The World Trade Organization (WTO) decided at its First Ministerial Conference in Singapore in December 1996 to 'establish a working group to study issues raised by Members relating to the interaction between trade and competition policy, including anti-competitive practices, in order to identify any areas that may merit further consideration in the WTO framework'.¹ The Organization for Economic Cooperation and Development (OECD) has done a considerable amount of analytical and policy-oriented work in this area, both separately in the Trade Committee and the Competition Law and Policy Committee, and jointly between the two committees. A decision has recently been taken by the OECD to create a Joint Group on Trade and Competition.² The UNCTAD has recently reviewed and revised its set of 'Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices'.³ Within the EU, Commissioner for Competition, Karel van Miert, took the initiative in 1994 to produce the van Miert Report,⁴ and this has been followed up with further work.

INTRODUCTION

In addition, interested parties have taken the initiative to form private, politically independent bodies, like, e.g., the Global Forum for Competition and Trade Policy⁵ and the International Antitrust Code Working Group.⁶ Influential individuals have also come up with suggestions or proposals for solutions on policy issues.⁷

The work and the initiatives referred to above are represented, directly or indirectly, in this volume. The issues are primarily approached from a competition and competition policy perspective, while at the same time emphasizing the need for developing a coherent policy framework for a consistent treatment of competition enforcement principles and trade remedies in an international context.

Coherence or conflict?

In the ideal world one would expect to find a high degree of coherence or complementarity between trade and competition policies, rather than conflict. Both policy areas have the same basic objectives for policy decisions: the attainment of economic efficiency in resource utilization and the advancement of overall economic welfare. They also have a common theoretical foundation – the theory of free trade and the theory of perfectly competitive markets – as reference point for realizing these objectives. The analysis typically starts from there by identifying possible sources of market failures or imperfections and their consequences for achieving the economic welfare and resource utilization goals. The nature of such distortions is different, though. In the trade policy area they typically consist of trade restraints created by policy decisions by governments of nations in the form of tariffs, quotas, export subsidies on traded goods and services, anti-dumping duties, voluntary export restraint agreements, etc., while in the competition policy area they typically consist of market imperfections in the form of monopolization, collusion, various forms of restrictive business practices etc., instigated by acts of private market agents.

Methodologically, there is also 'coherence', in the sense that the same analytical tools or models are being applied in both policy fields. This is at least the case for the modern strategic trade policy analysis⁸ and the analysis of strategic interactions in oligopoly markets. Thus, an integrated treatment of policy options and effects should, in principle, be possible.

There is, however, still a considerable gap or divergence of focus with regard to analytical approaches under the present state of the art of policy research. The literature on strategic trade policy is almost void of explicit treatment of competition policy issues, basing the analysis to a large extent on the 'third country model', although there have been some recent attempts to extend the analysis to include effects on consumers in the home country of trade strategic measures. Similarly, competition policy analysis has been almost void of explicit treatment of strategic trade policy issues,

INTRODUCTION

concentrating the analysis on welfare effects for domestic consumers of market strategic behaviour of, e.g., a national oligopoly.⁹

Further theoretical work to bridge this gap is needed in order to develop a coherent framework for an integrated analysis of (strategic) trade and competition policy issues.

Even though trade and competition policies have similar basic objectives, the instruments to achieve those objectives are radically different. Trade policy enforcers try to obtain collective, cooperative solutions through international negotiations to reduce the adverse effects on international trade of unilaterally imposed trade restraints by individual countries or groups of countries, while competition policy enforcers try to prevent firms under their jurisdictions from behaving collectively or collusively, if such behaviour is likely to jeopardize the economic efficiency goal.¹⁰ Competition policy enforcers have quite powerful policy instruments at their disposal, in the form of *per se* prohibitions or interventions on a rule of reason basis against market behaviour and practices which can be considered detrimental to the stated goal. The trade policy enforcers find themselves in a quite different situation in this respect, with much weaker policy instruments and typically based on some form of international consensus in order to be applied.

The performance criteria for evaluating the outcome of the use of policy instruments are also somewhat different. In competition policy, performance is measured directly as an increase in economic efficiency of improved competition following a policy intervention. Under trade policy an increase in international trade flows often seems to be considered as a performance criterion in itself, or at least as a proxy for the efficiency enhancing effect on the international division of labour of a given trade policy instrument.¹¹

The welfare function for the assessment of welfare improvements of policy measures may also be weighted somewhat differently across interest groups under the two policy regimes. Generally speaking, competition policy emphasizes consumer interests over producer interests, to the effect that efficiency gains should be passed on to consumers in the form of lower prices, better quality, improved accessibility to products and services etc., and not accrue as increased profits with the producers. A protectionistic trade policy measure would therefore be met with general scepticism by competition authorities, because this would normally harm consumers and favour domestic producers. In fact, in many countries competition policy and consumer policy are integrated under the same legal and institutional umbrella. There is, on the other hand, at least a presumption, based on empirical observations, that producer interests tend to be weighted more favourably under trade policy than competition policy in most countries.

This brief exposé indicates that there are close similarities and interlinkages between trade policy and competition policy, but also differences.¹² It is a demanding task to design an optimal policy mix of targets and instruments for the two policy areas under such conditions, even for an 'ideal' world

INTRODUCTION

situation. The difficulties multiply as we move to the real world with all the complexities added, because of, for example, quite different legal and institutional systems across countries, for the enforcement of such an optimal policy mix in an international setting.

Anti-competitive practices and trade

The efforts to liberalize trade through successive rounds of trade negotiations have limited the scope for governmental trade policy measures that distort the conditions of international competition. This development has, as already mentioned, gradually shifted the attention of policy-makers and analysts from trade policy remedies to private anti-competitive practices as potential barriers to trade, and thus to the efficacy of competition policy as a possible remedy. Since the focus in this book is on competition policy, let us consider briefly and in a summary fashion some such private anti-competitive practices and trade distortive effects that may result from them. For this purpose we use a simple classification scheme:

- 1 Anti-competitive practices of private parties in one country affecting the markets of other countries.
- 2 Anti-competitive practices of private parties in one country affecting the domestic market of the same country.
- 3 International anti-competitive practices of private parties in several countries affecting the markets of one or more countries.

The prime candidate for a private regulation of the first category is cooperation among exporters in one country in the form of an export cartel. This may distort competition in foreign markets, provided the cartel has a strong enough market position in those markets to influence prices or other parameters. The likely outcome is increased prices in the foreign markets, a negative effect on consumers' welfare in those countries and reduced traded volumes in international trade of the commodities encompassed by the cartel agreement.

A merger between two or more firms in the home country may have similar effects in foreign markets, again provided the merger gives scope for exercising market power in those markets. The effects of a merger compared with an export cartel may be different in the home markets of the country, though, depending on the specific competitive conditions of those markets in relation to the said practices.¹³

Export cartels and similar private practice, anti-competitive arrangements which have their intended effects solely outside the jurisdiction of the country in question, are usually exempted legislatively from competition law enforcement in most countries. An increased awareness of the possible distortive effects of such arrangements on international trade and competition

INTRODUCTION

should make this 'effect doctrine' an obvious candidate for review and revision by competition authorities in a joint effort to reduce distortions of this kind.

The second category above encompasses a number of national regulations and practices by domestic firms which may create barriers to market access for foreign competitors to the domestic market. The prime candidates here are vertical restraints and relationships effectuated by a dominant firm, or group of firms, seeking to obtain vertical control of, for example, a distribution system. Vertical restraints come in many forms: exclusive dealing contracts for products or geographical territories, resale price maintenance agreements, franchise arrangements, and vertical control through full vertical integration.

The trade distortive effects of vertical restraints materialize to the extent that domestic firms succeed in preventing foreign competitors from entering the domestic market, e.g. by foreclosing access to distribution channels for goods and services locally. Measures like refusals to deal, boycotts, loyalty discounts, price discrimination, predatory pricing, strategic adjustment of production capacities, control of access to essential facilities such as the domestic electricity network system, and import cartel agreements may also be used as measures to deter entry by foreign competitors to the domestic market.

Private regulations and practices in this category fall normally within the domain and jurisdiction of the national competition authority and can be enforced under its competition law. Whether they will be intervened against or not depends upon how aggressively the competition authority combats such practices.¹⁴ This may vary from country to country, but in view of the increased importance being given in recent years in competition policy analysis to entry conditions in general, and to potential import competition in particular, as a disciplining factor for the market behaviour of incumbent firms – derived from the theory of contestable markets – one would expect to find a more 'interventionistic' approach to those practices in most competition authorities than before. This may particularly be the case for small countries, where potential import competition normally means relatively more for competition and trade than for large countries.

The third category consists first and foremost of anti-competitive practices that are associated with international cartel agreements: price or quota cartels, market sharing arrangements, bid-rigging, etc. Such practices are normally prohibited *per se* in the competition laws of most countries. The competition and trade distortive effects are obvious, as several national markets are normally affected. Enforcement is difficult, partly because of information problems and partly because of the multinational nature of the agreements, and therefore requires some form of international agreement among the competition authorities of the countries where the parties to the cartel agreement are localized.

INTRODUCTION

Policy options

Competition and trade policy officials seem to agree generally about the need to develop a more coherent framework for the analysis of competition and trade policy issues, and a more consistent approach to an effective application of policy instruments. There is, however, much less consensus about the specific structure of the framework and the policy options. Several schools of thought or divergences of opinion can be distinguished.

Some question the very position or hypothesis that private anti-competitive practices necessarily have substantive distortive effects on trade and competition that require corrective measures in an international context, and emphasize the need for empirical documentation before policy solutions are set forth. Others seem to be more inclined to go directly to solution concepts.

Another dividing line is between those who favour voluntary agreements of cooperation among countries or authorities to find policy solutions. Others advocate more binding commitments to an organized international policy enforcement cooperation, with dispute settlement procedures or other mechanisms for the imposition of common enforcement rules and principles for the participating countries.

A third divergence of opinion exists between those who maintain that policy interventions to correct for trade and competition distortions are best pursued by a policy area by policy area approach, attacking trade restraints with trade policy remedies and competition restraints with competition policy instruments. Others argue for an integrated approach within a common framework for policy decisions, where trade and competition policy measures can support and reinforce each other.

In spite of some differences of opinion on policy issues, a number of policy options have been proposed for a more effective application of competition policy measures in an international context, and work is in progress of implementing some of them. One can distinguish between three main approaches:¹⁵

- 1 harmonizing national competition law and practices (convergence), and extending the scope and coverage of competition laws;
- 2 improving cooperation among national competition authorities; and
- 3 creating a multilateral framework for competition law enforcement and dispute settlement.

The work on convergence of competition laws has been pursued most actively by the Committee on Competition Law and Policy of the OECD. It has been going on for several years, a number of publications have been produced which have had some influence on policy development,¹⁶ and interim reports have been submitted to the OECD ministerial meetings.¹⁷ The intention is not necessarily to obtain strict uniformity in law and institutions across