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Competition Policy Convergence: Where Next?

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Abstract

As the 20th Century dawned, there were radical divergences in the policies individual nations pursued toward restraints of competition by cartels and monopolies. Since World War II there has been considerable convergence as an increasing large number of nations have adopted explicit pro-competition policies. This paper traces the reasons for the divergence and then convergence and asks what important steps remain to be taken, especially where the concerns of international trade policy and competition policy intersect. A proposed augmentation of the World Trade Organization's functions to deal with competition policy issues is examined.

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1 Introduction

During the last half century, there has been a remarkable convergence in competition policies among the nation state members of the world community. Scores of nations have moved from having no pro-competition laws, or even laws that favored monopoly, to presumptions against collusive agreements and the exploitation of dominant market positions. The world economy has also become much more open. Increasing fractions of nations' gross domestic product originate through international trade, and multinational enterprises have greatly increased their overseas presence through foreign direct investment.

With international trade and investment flows determining to an increasing extent the character of competition within nations, it becomes increasingly important to review how the rules governing cross-border competition will be determined. Does the enforcement of competition law within one's own boundaries suffice? Or should national policies be extended extraterritorially to reach foreign business enterprises' conduct? Or should there be steps to harmonize the competition policies of individual nations, and perhaps even to create supra-national institutions, coordinating and facilitating the exercise of competition policies across multiple national jurisdictions?

These are the broad issues addressed in this paper.[1] I begin with an historical overview of the competition policy convergence process, examining inter alia the reasons why convergence occurred. I then identify the trans-national problems left unsolved by the evolution of national institutions and consider, without resolving the most thorny disputed issues, the main alternatives for further development.

2 Divergence and Convergence

To study convergence, one must begin with the extremes from which convergence took place. The policies toward competition that emerged during the second Industrial Revolution, i.e., from about 1870 to 1915, provide a fascinating subject in the intellectual history of both economics and economic policy.

The closing decades of the 19th Century brought dramatic changes in the character of industrial competition. Improvements in transportation, notably, railroads and iron-hulled ships propelled by increasingly efficient steam engines, reduced the costs of geographic market interpenetration, both within and across national borders. In the manufacturing and extractive industries, there were also many dramatic technological changes -- e.g., in steel-making, petroleum extraction and refining, chemistry, and the electrification of illumination and mechanical power. Improvements in communication -- first the telegraph and then the telephone -- facilitated the development of new managerial

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[1] For a much more detailed exploration of these issues, see my monograph, Competition Policies for an Integrated World Economy (Washington: Brookings Institution: 1994).

structures able to control organizations of greatly increased scale and complexity. Advances in technology and management in turn permitted industrial organizations to grow to unprecedented size. As entrepreneurs sought the advantages, real or imagined, of large scale, the quest for increased volume and geographic scope precipitated ferocious price wars, prompting the formation of preventive cartels and (later, often through mergers) market-dominating enterprises. Well before these developments became unmistakable, Karl Marx prophesied "a centralization of capital" under the "immanent laws of capitalist production"[2] "One capitalist always kills many," wrote Marx, leading to "the constantly diminishing number of the magnates of capital, who usurp and monopolize all advantages of this process of transformation."

The unfolding changes in the structure and conduct of modern industry were perceived by economists in widely varying ways.[3] Richard Ely, who chaired the 1886 organizational meeting of the American Economic Association, and Alfred Marshall, England's leading economist, believed that newly-emerging economies of scale required monopolistic market structures only in rare cases. A quite different view was taken by Robert Liefmann, the leading German thinker on industrial economics at the close of the 19th century:[4]

> But since as a rule, a single seller is the cheapest... competition has the tendency, when pushed to its limit, to destroy itself and to be turned into monopoly. Since the cheapest seller can often lower costs by producing the whole supply, it follows that the maximum satisfaction of wants is obtained when there is only one seller, competition remaining latent in the background, effective only when the seller does not employ the most efficient methods of production, or when as a monopolist he appropriates a profit much above the economic marginal return.

Liefmann believed that bitter price wars weeded out inefficient producers, leaving a monopolist, who often then raised prices, triggering a flood of entry and renewed price wars. This, Liefmann concluded, was inefficient and macroeconomically destabilizing,

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[2] Karl Marx, Capital, vol. 1 (translated from the 3rd German edition by Samuel More and Edward Aveling) (New York: International Publishers, 1967), p. 763.

[3] This summary is abstracted from my edited collection, Monopoly and Competition Policy, vol. I (Hants, UK: Edward Elgar, 1993), which pulls together representative analyses by leading economists of the late 19th and early 20th centuries.

[4] "Monopoly or Competition as the Basis of a Government Trust Policy," (translated by H. R. Tosdal) Quarterly Journal of Economics, vol. 29 (1915), pp. 314-315; reprinted in Scherer, Monopoly and Competition Policy, pp. 119-120. Liefmann's views appear to have had a formative influence on the later writings of Joseph A. Schumpeter. See Erich W. Streissler, "The Influence of German and Austrian Economics on Joseph A. Schumpeter," in Yuichi Shionoya and Mark Perlman, eds., Schumpeter in the History of Ideas (Ann Arbor: University of Michigan Press, 1994), pp. 26-29.

and so he argued for monopolization or cartelization, with prices regulated by a government authority to prevent entry-encouraging excesses. In the United States too, many economists, and especially Arthur Hadley, later the president of Yale University, saw competitive processes as naturally "cut-throat" and "ruinous." Others such as Cornell University's Jeremiah Jenks, the most careful empirical analyst of industrial structure and conduct at the turn of the century and the principal advisor on competition policy matters to Theodore Roosevelt, disagreed.

It is debatable whether Liefmann's views merely reflected the prevailing intellectual sentiment in German-speaking Europe, or whether they actually shaped the policy climate. The former is more likely true than the latter. Whatever the intellectual roots were, Germany adopted, through judicial decisions and the inability of the Reichstag to reach a consensus on alternatives, an expressly pro-cartel policy.[5] Under the freedom of association accorded workers and businesses by German law, cartel agreements were lawful and binding upon their participants except in cases of "actual monopoly" or extreme exploitation of consumers -- cases that never seemed to come to the authorities' attention. Beginning with the Coalition Law of 1870, Austria pursued an essentially similar policy, although without express judicial mechanisms to enforce cartel agreements against recalcitrant participants.[6]

In the United States, a quite different tack was chosen. Economists held divergent views concerning the benefits and costs of the newly emerging industrial practices and forms. But there was widespread popular concern over predatory practices and (when monopoly power was consolidated) price-raising by "trusts" such as Standard Oil, the American Sugar Refining Company, the American Tobacco Company, and National Cash Register. In response to the popular outcry, Congress in 1890 passed the Sherman Antitrust Act, declaring illegal "every contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade." Also subjected to fines and injunction were monopolization and attempts to monopolize. Scholars disagree over whether Congress truly intended the Sherman Act to be a mandate for a tough anti-monopoly policy, or merely a placebo to pacify public opinion. At first, the law was enforced only lackadaisically. But tough, literal interpretations by the Supreme Court during the late 1890s made it clear that virtually all types of horizontal price-fixing agreements would be condemned, whether or not they successfully or unreasonably raised prices. And with the accession of Theodore Roosevelt to the U.S. presidency in 1901, government agencies with an explicit competition-enhancement mission were created, and vigorous

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[5] Scherer, Competition Policies, pp. 23-26.

[6] Peter Pöch, "Austrian Law/Commentary," in D. J. Gijlstra, ed., Competition Law in Western Europe and the USA, Supplement 66 (January 1986).

enforcement began against market-dominating mergers and consolidations, leading to the fragmentation inter alia of Standard Oil, American Tobacco, and DuPont.[7]

Positions between the German and American extremes -- cartel-enforcing on one hand and cartel-breaking on the other -- were chosen elsewhere in the world. In England, the leading industrialized nation of the 19th century, the Court of Appeals ruled in an important 1889 decision that cartel agreements would not be enjoined except in cases of manifold abuse, but that the courts would also not intervene, as German authorities did, to enforce such agreements. As other European nations evolved their own solutions to the problem, the predominant approach was to tolerate or even encourage the operation of cartels except in rare cases of abuse. Thus, at a conference of the Inter-Parliamentary Union in 1930, the European participants unanimously adopted a resolution stating:[8]

> Cartels, trusts and other analogous combines are natural phenomena of economic life towards which it is impossible to adopt an entirely negative attitude. Seeing, however, that those combines may have a harmful effect both as regards public interests and those of the State, it is necessary that they should be controlled. This Control should not take the form of an interference in economic life likely to affect its normal development. It should simply seek to establish a supervision over possible abuses and to prevent those abuses.

3 Convergence and Spread

The first significant step toward international convergence of competition policies occurred in the wake of World War II. In both Japan and Germany, the occupying powers, led by the United States, compelled the adoption of new competition ordinances patterned to some extent after the American model. Prominent in those policies was the structural divestiture of powerful industrial groupings -- in Japan, the divestiture of cross-holdings linking members of the Zaibatsu groups; in Germany, the breakup of the I.G. Farben chemical giant into three main units (Bayer, BASF, and Hoechst) and dissolution of the leading steel and coal syndicates. The 1947 German occupation authority law authorizing these actions stated as its purpose "to destroy Germany's economic potential to wage war" and to prevent Germany from "endangering the safety of her neighbors."[9]

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[7] The German Reichstag struggled inconclusively during the late 1890s with the question of what to do about Standard Oil, which also dominated German illuminating oil markets. Fritz Blaich, "'Der Standard-Oil-Fall' vor dem Reichstag," Zeitschrift für die gesamte Staatswissenschaft, vol. 126 (October 1970), pp. 662-682.

[8] Reproduced in William Boserup and Uffe Schlichtkrull, "Alternative Approaches to the Control of Competition," in John Perry Miller, ed., Competition Cartels and Their Regulation (Amsterdam: North-Holland, 1962), p. 59.

[9] Law No. 56, "Prohibition of Excessive Concentration of German Economic Power," by order of the Military Government, December 2, 1947.

In this there was a paradox: If one fragments giant business firms and cartels to undermine economic power, what does one do to enhance economic power? The paradox was deepened when Allied authorities relaxed their structural reorganization efforts in the hope of strengthening Germany and Japan as bulwarks against the Soviet Union and Red China in the newly emerging cold war.

The paradox was recognized. In Japan, the Anti-Monopoly Law was viewed as a foreign implant imposed "to suppress the economy of Japan so that it could not recover and grow."[10] After the occupation ended, enforcement of the law was characteristically weak, although beginning in the late 1960s, in response to an emerging consumer movement, enforcement gradually became more vigorous. The German Federal Republic passed its Law Against Restraints of Competition only in 1957, after seven years of deliberation. The 1957 law contained at first no provisions to bar mergers or break up concentrations of economic power -- key elements of postwar occupation authority competition policies. However, it did authorize relatively strong anti-cartel measures, and after a slow start due in part to locating the Federal Cartel Office in Berlin but severely limiting its travel budget, it was diligently enforced. A tough law was possible despite the bad taste left by occupation authority mandates because the German government was strongly influenced by Freiburg School liberals, who believed passionately in competitive free market processes as the best alternative to dictatorship, and who saw cartels and monopolies as impediments to the attainment of competitive market order (*Marktordnung*). Among the most prominent members of the Freiburg school was Ludwig Erhard, economics minister at the time the 1957 law was passed and later prime minister of the Federal Republic.

The United Kingdom began moving away from its laissez faire competition policy with the establishment in 1948 of a Monopolies and Restrictive Practices Commission, which at first had only information-gathering and advisory powers. An asserted (but disputed) rationale for the change was fear that attaining postwar full employment objectives might be jeopardized by the price-fixing practices of cartels and monopolies.[11] A more decisive step occurred in 1956 when, spurred by a June 1955 Monopolies Commission report, Parliament created a new Restrictive Practices Court with power to prohibit cartel agreements that failed to navigate a set of exemption "gateways." That a hard new line would be taken was demonstrated in the first litigated price-fixing case.[12] The Court accepted as a defense the contention of the British Cotton Yarn Spinners Association that

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[10] Hiroshi Iyori and Uesugi Akinori, The Antimonopoly Laws of Japan (1983), p. vii.

[11] See John Jewkes, "British Monopoly Policy 1944-56," Journal of Law & Economics, vol. I (October 1958), p. 2, who attributes the post-war disposition to place greater reliance upon competition to "those mysterious and unpredictable switches in broad economic thinking, so numerous in history, in which irrationality has played at least as great a part as rationality." Jewkes views the macroeconomic employment argument as "always dubious."

[12] In re Yarn Spinners' Agreement, L.R., 1 R.P. 118 (1959).

theirs was a declining industry and that painful pockets of localized unemployment would result if their collusive activities were prohibited. But the Court held that whatever employment benefits the Yarn Spinners' agreement might yield were outweighed by the harm from preserving inefficient and unnecessary spinning capacity.

A more decisive step toward convergence between the policies of Europe and the United States came with the creation of the European Common Market in 1957. The main initial purpose of the Treaty of Rome was to eliminate tariff barriers to trade among Common Market member nations. As a true common market emerged, it was believed, anti-dumping and similar trade regulation mechanisms could be phased out -- a step begun in 1970. But to ensure that trading relationships among member nations were not distorted, an active competition policy was seen as a necessary substitute. As an EC official stated at an early date in the Common Market's evolution:[13]

> It is ... beyond dispute -- and the authors of the Treaty were fully aware of this -- that it would be useless to bring down the trade barriers between the member states if the governments or private industry were to remain free through economic or fiscal legislation, through subsidies or cartel-like restrictions on competition, virtually to undo the opening of the markets and to prevent, or at least unduly to delay, the action needed to adapt them to the Common Market.

Enforcement of Treaty of Rome Article 85, deeming inconsistent with the common market "all agreements between firms ... and all concerted practices likely to affect trade between Member States," proceeded slowly at first. The first tough enforcement actions, against quinine and synthetic dye cartels, came only in 1969. But after that, an increasingly stringent enforcement program was sustained.

Extensions of Common Market law, especially the division of merger review responsibilities between national and Community authorities, increased the compulsion for each Common Market member to have its own national competition law. Collaboration between European Economic Community and European Free Trade Association nations engendered incentives for EFTA members to pass, or strengthen, their own competition laws. Austria's less tolerant Cartel Act of 1972 is said, for example, to have resulted mainly from the agreement under which Austria joined the EEC in an extended free trade area.[14] The 1992 treaty creating a broader European Economic Space stipulated inter alia that newcomers to the agreement would adopt competition policies as strict as those within the European Community. As a result of this process, which extended some semblance of free trade to much of Western Europe, nearly every

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[13] Statement of Hans von der Groeben in 1961, reproduced in U.S. Senate, Committee on the Judiciary, Subcommittee on Antitrust and Monopoly, Hearings, Antitrust Developments in the European Common Market (USGPO: 1963), p. 96.

[14] Pöch, "Austrian Law/Commentary," p. 2.

nation involved has come to enact competition laws with presumptions of varying severity against cartels, market-dominating mergers, and abuses of dominant market positions.

Nor has the convergence process been confined to western Europe. Australia (which passed but enforced only sporadically a competition law in 1906), New Zealand, the Asian "Tiger" nations, many South and Central American nations, South Africa, and most recently, fragments of the former Soviet bloc and Russia itself have seen fit to enact or strengthen their own competition law variants.[15] It would hardly be inaccurate to say that no self-respecting nation can consider itself a full-fledged member of the world community without laws proscribing to some extent cartels and abuses of monopoly power.

4 Convergence: Fashion or True Religion?

On these developments a certain amount of skepticism seems warranted. It is far from clear that all of the nations enacting new competition laws in recent years have been converted to a religious belief in unrestrained competition as the favored recipe for consumer welfare and economic growth. Some of what has happened appears to be window dressing -- an attempt to keep up with the Joneses without really effecting significant changes in national economic policies. My own visits to two recently created national competition policy offices (which to protect the innocent will not be identified) revealed staffs uncertain as to what they should do, unable to obtain the information needed to identify serious anti-competitive practices, and fearful that aggressive action against powerful business interests could elicit prestige-eroding recriminations. In economies still bearing substantial legacies from central planning, competition policy office staffs have often exercised what power they possess not to foster unfettered market processes, but to fetter them by imposing price controls.[16] To be sure, new staff members unsure of how to do their job have not been deprived of well-intentioned advice. There is a plenitude of visiting advisers (including myself) from nations with long-established competition policy traditions, ready and willing to expound at length on the tricks of their trade. It is difficult, however, to have a positive impact when one can't speak the

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[15] On Russia, see Paul L. Joskow, Richard Schmalensee, and Natalia Tsukanova, "Competition Policy in Russia during and after Privatization," Brookings Papers on Economic Activity: Microeconomics (1994), pp. 301-381.

[16] See Joskow et al. and, on similar earlier experience in West Germany, Erich Kaufer, "The Control of Abuse of Market Power by Market-Dominating Companies under the German Law against Restraints of Competition," Zeitschrift für die gesamte Staats-wissenschaft, vol. 136 (September 1980), pp. 510-532; and Ingo Schmidt, "Different Approaches and Problems in Dealing with Control of Market Power: A Comparison on German, European, and U.S. Policy towards Market-Dominating Enterprises," Antitrust Bulletin, vol. 28 (Summer 1983), pp. 417-460.

language of the natives and has no understanding of national traditions, institutions, and industrial structures.

It seems unlikely that pro-competition policies would be adopted so widely by nations that have debated the alternatives seriously for decades if they did not offer solid, compelling advantages. What established truths underlie the conversion implied by convergence?

Perhaps the least important truth is the well-accepted proposition that resources are allocated more efficiently to satisfy human wants under competition than under monopoly. Proving this is economists' stock in trade. I assign it low importance because most empirical analyses have found deviations from competition to impose quite small allocative efficiency losses.[17] Ignoring second-best perplexities and the offsetting benefits of product differentiation when high endogenously implied price elasticities are plugged into welfare loss formulas, the estimates seldom reach five or ten percent of gross domestic product, and typically they are much lower.

Much more important is the role vigorous competition plays in forcing business organizations to run a tight ship, seek efficient scales of operation, adopt best-practice technology, and innovate. Although we have known about potential X-inefficiency since Adam Smith warned 220 years ago that "Monopoly is a great enemy to good management,"[18] we have only recently begun to accumulate systematic evidence on its magnitude. James MacDonald has shown that significant productivity gains emerged in U.S. industries subjected to new competitive shocks from imports, but only in industries with relatively high domestic concentration ratios -- presumably, those in which competition was blunted before imports forced behavioral changes.[19] From an unusually ambitious program of comparative national case studies, Michael Porter and associates found that strong enterprises able to hold their own in the rough-and-tumble of international competition emerge through a kind of natural selection process under which the contenders are repeatedly challenged by vigorous rivals.[20] Similar conclusions

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[17] For a critical survey of the large literature, see F. M. Scherer and David Ross, Industrial Market Structure and Economic Performance, 3rd ed. (Boston: Houghton-Mifflin, 1980), pp. 661-667.

[18] An Inquiry into the Nature and Causes of the Wealth of Nations (New York: Modern Library edition, 1937), p. 147.

[19] James M. MacDonald, "Does Import Competition Force Efficient Competition?" Review of Economics and Statistics, vol. 76 (November 1994), pp. 721-727. In a similar effort, I failed to find significant import shock effects because I did not analyze the interaction between imports and concentration. "Lagging Product-ivity Growth: Measurement, Technology, and Shock Effects," Empirica, vol. 20, no. (1993), pp. 5-24.

[20] Michael Porter, The Competitive Advantage of Nations (New York: Free Press, 1990), pp. 117-124, 594-598, and 662-673.

emerged from a detailed comparative analysis of productivity levels in Germany, Japan, and the United States.[21] The "Costs of Non-Europe" studies that provided intellectual underpinning for the Europe 1992 initiatives similarly assigned much greater weight to the role of competitive trade in undermining X-inefficiency than to allocative efficiency considerations.[22]

One of the most frequent exceptions to pro-competitive presumptions in national laws has been based upon a belief that cartels could cushion the shock of cyclical recessions.[23] Theoretical guidance on this point is in fact ambiguous. On one hand, microeconomic analysis teaches that if prices are held up by a cartel during a recession, the quantity of output demanded will be less than under downward-flexible competitive pricing, all else equal, and profit-maximizing firms will therefore employ less labor, aggravating the slump. Macroeconomic theory suggests that adverse Pigou effects from price rigidity will also impair recovery. On the other hand, if firms holding prices high through the exercise of monopoly power fail to maximize profits, but instead utilize their managerial slack to retain surplus labor, employment declines might be smaller during the slump, and therefore the slump could be mitigated. I tested these conflicting hypotheses with respect to the U.S. recessions of 1954 and 1958 and found, as did other analysts, no support for the "concentration leads to employment stability" version.[24] Recognition by national legislators that conventional wisdom concerning the stabilizing effects of cartels is of doubtful validity may underlie in part the rejection of traditional pro-cartel policies.[25]

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[21] Martin Baily and Hans Gersbach, "Efficiency in Manufacturing and the Nature of Competition," Brookings Papers on Economic Activity: Microoeconomics (1995), pp. 307-358. Baily and Gersbach do not analyze the construction industry, whose extremely low productivity in Japan has been attributed to "the lack of competition [which] has spilled over from bureaucrats who discourage productivity increases by fixing cost formulas for public works. This lack of competition also allows firms to buy expensive domestic materials." Mark Tilton, Restrained Trade: Cartels in Japan's Basic Materials Industries (Ithaca: Cornell University Press, 1996), p, 85.

[22] Research on the "Costs of Non-Europe" Basic Findings, two vols. (Luxembourg: Publications Office of the European Communities, 1988).

[23] See e.g. Pöch, "Austrian Law/Commentary," p. 2, who observes that the Austrian Cartel Act of 1951 embodied the idea that "cartels could compensate for the economic cycles and stabilize the markets. Therefore they could be economically useful if not indispensable."

[24] F. M. Scherer, Industrial Market Structure and Economic Performance, 2nd ed. (Chicago: Rand-McNally, 1980), pp. 365-367. See also my discussion on p. 364 of the effects of cartelization under the U.S. National Recovery Act during the 1930s.

[25] On the destabilizing effects of German cartels during the early decades of the 20th Century, see Kurt Bloch, "On German Cartels," Journal of Business of the University of Chicago, vol. 5 (July 1932), pp. 213-222.

Paralleling the view that cartels ease the pains of recession is the hypothesis that chronically excess capacity can be shed more effectively through cartel agreements than through competition. Although "down-sizing" is probably less painful, at least for stockholders, under cartel auspices, there is now a considerable amount of evidence that competition tends to squeeze out first the least efficient producers, whereas internal cartel politics require each company, efficient and inefficient, to shed proportionate amounts of capacity.[26] Thus, the capacity left in operation tends to be less efficient on average under cartelization than under competition.

Perhaps the most powerful impediment to the adoption of pro-competitive policies, at least in Europe, has been the belief that only large, monopolistic firms can compete effectively with overseas rivals, especially in high-technology fields. France's Jean-Jacques Servan-Schreiber expressed this view most eloquently:[27]

> The first problem of an industrial policy for Europe consists in choosing 50 to 100 firms which, once they are large enough, would be the most likely to become world leaders of modern technology in their fields. At the moment we are simply letting European industry be gradually destroyed by the superior power of American corporations. Counterattack requires a strategy based on the systematic reinforcement of those firms best able to strike back. *Only a deliberate policy of reinforcing our strong points* -- what demagogues condemn under the vague term of "monopolies" -- *will allow us to escape relative underdevelopment.*

France and other major European nations pursued such policies for nearly a quarter of a century with little discernible success. The toughening and spread of pro-competition policies in part reflects recognition that national champions insulated from competition seldom, if ever, become world-class competitors.

Finally, many of the world's citizens have hungered for freedoms long denied them by dictatorial governments. If Germany's Freiburg school is correct, governments are more likely to refrain from intervening in market processes when there is assurance that the markets are functioning reasonably competitively. The ease of entry that is a crucial contributor to workable competition also implies more freedom of economic opportunity for individual citizens. Here too, however, there are paradoxes. Competition policies can be oriented toward preserving competitive market processes or toward protecting

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[26] See e.g. R. W. Shaw and S. A. Shaw, "Excess Capacity and Rationalisation in the West European Synthetic Fibers Industry," Journal of Industrial Economics, vol. 32 (December 1983), pp. 149-166; M. J. Peck, Richard C. Levin, and Akira Goto, "Picking Losers: Public Policy Toward Declining Industries in Japan," in John B. Shoven, ed., Government Policy Toward Industry in the United States and Japan (New York: Cambridge University Press, 1988), pp. 195-239; and Tilton, Restrained Trade, pp. 46-47, 65, 94, and 200.

[27] The American Challenge (translated by Ronald Steel from the 1967 original, Le Defi Americain) (New York: Athenaeum, 1968), p. 159.

individual competitors from the not-so-tender mercies of aggressive rivals. The United States has experienced repeated conflicts -- e.g., in merger, predatory pricing, and other price discrimination cases -- over which of the two quite different objectives should be dominant in its antitrust enforcement activities.

5 International Challenges and Opportunities

For whatever mixture of reasons, pro-competitive policies have spread to most of the world's economically developed nations and to some of the less-developed nations. This phenomenon coupled with the increase in world trade and foreign direct investment poses new challenges. In particular, now that competition policies have taken root within national borders and, within the EU, across boundaries, is there a need for harmonization and/or coordination of policies among nations?

Several loose ends have been left hanging in the wake of recent competition policy developments.[28] For one, most nations (or in the case of the EU, trade blocs) discourage cartels and monopoly abuses within their boundaries, but exempt export cartels from those prohibitions or even actively encourage the cartelization of export activities. Second, for similar reasons, mergers to achieve monopoly power in export markets are also encouraged. But third, because many mergers involve multi-national enterprises operating throughout the world, the proliferation of laws requiring evaluation of a merger's domestic consequences means that some mergers are subjected to duplicative national reviews -- in the extreme case of Gillette's acquisition of Wilkinson Sword, to fourteen such costly reviews. There is reason to believe also that national merger decisions are biased against foreign enterprise attempts to take over domestic companies. Fourth, when domestic monopolies and cartels are tolerated, e.g., because they have justified their existence by sustaining impressive export campaigns,[29] the ability to hold prices high at home may facilitate and encourage dumping abroad. Dumping can distort international trade flows and, if GATT-compatible retaliatory tariffs are imposed or voluntary restraint agreements are negotiated, engender new trade distortions. Finally, there is much disagreement among economists and national economic policy-makers over the desirability of vertical market restraints such as exclusive dealing agreements between manufacturers and their retailers, exclusive territorial agreements, and resale price maintenance agreements. To the extent that such vertical restraints are permitted under

[28] This is an excessively brief and superficial summary. My book, Competition Policies for an Integrated World Economy, devotes a 45-page chapter to the subject.

[29] As a majority of the U.S. Supreme Court observed in 1920 when it absolved the United States Steel Corporation from monopolization charges: "And what of the foreign trade that has been developed and exists? ... We do not see how the Steel Corporation can be such a beneficial instrumentality in the trade of the world, and its beneficence be preserved, and yet be such an evil instrumentality in the trade of the United States that it must be destroyed.... [W]e do see in [dissolution of the company] a material disturbance of, and it may be serious detriment to, the foreign trade." United States v. United States Steel Corporation, 251 U.S. 417, 457 (1920).

national competition laws, they may serve to perpetuate distribution channels that inhibit imported products' access to consumers, and hence distort international trade.[30]

There are several possible solutions to this set of border-spanning problems. One is for nations (or the EU) to apply their national competition laws extraterritorially, reaching out and levying penalties against restrictive practices abroad that have adverse effects in the complaining nation's home market. This is most successfully done when the offending foreign business enterprises have resident branch offices or subsidiaries whose documents can be subpoenaed and assets that can be seized if fines are imposed. Such exercises of extraterritorial jurisdiction often anger the home governments of the offending enterprises, but they have achieved a substantial measure of acceptance, having been pursued by the United States, the European Union,[31] and Canada. The United States has also engaged in "aggressive unilateralism" under Section 301 of its international trade law, viewing as actionable distortions of trade import cartels and vertical restraints that inhibit the access of U.S. goods to foreign markets. Claims that U.S. automobile and auto parts exports were held back by exclusive dealing arrangements between Japanese car manufacturers, their dealers, and repair shops, and that Fujifilm's powerful exclusive wholesaler network retarded Kodak color film sales in the Japanese market, are the most recent examples of competition policy actions under Section 301.[32]

A second possibility is the negotiation of bilateral cooperation agreements, under which national competition policy authorities collaborate in the collection of evidence and perhaps also in enforcement actions against alleged restraints of competition that span their home boundaries. The United States, for example, has entered into such agreements with Germany, Australia, Canada, and the European Community Commission. Needless to say, the home country authorities of enterprises accused of restrictive practices are likely to cooperate in such endeavors only when they find it in their national interest to do so.[33]

A third way of attempting to contain the loose ends is to create a supra-national authority with jurisdiction over defined restraints of trade that span national borders. The first step in this direction was taken at the United Nations Conference on Trade and Employment

[30] See F. M. Scherer, "Retail Distribution Channel Barriers to International Trade," forthcoming in the proceedings of a Columbia University School of Law conference on the Multilateral Trade Regime in the 21st Century, held in November 1995.

[31] E.g., in A. Åhlström Osakeyhtiö et al. v. Commission of the European Communities, 1988 E.C.R. 5193 (1988).

[32] See Scherer, "Retail Distribution Channel Barriers."

[33] For examples of non-cooperation, see my paper, "International Trade and Competition Policy," presented at the international conference on Competition Policies for an Integrated World Economy, Oslo, June 1996.

in Havana, Cuba, in 1947 and 1948. Under the so-called Havana Charter, a new International Trade Organization (ITO) would be created. Article 46 of the Charter stated that:[34]

> Each Member shall take appropriate measures and shall cooperate with the [ITO] to prevent, on the part of private or public commercial enterprises, business practices affecting international trade which restrain competition, limit access to markets, or foster monopolistic control, whenever such practices have harmful effects on the expansion of production or trade ...

The ITO was given a mandate to consult with member nations over alleged violations (including price fixing, production quota agreements, spheres of influence agreements, and the collusive suppression of technology), to urge corrective action, and to publish compliance reports. Although U.S. officials had played a leading role in drafting the Havana Charter, the United States Senate refused to ratify it because many senators believed its provisions would infringe too much on U.S. sovereignty. As a result, only the sections of the Charter that gave rise to the GATT organization were actually implemented.

Subsequent attempts to reach international agreement on substantive codes for business firms' competitive behavior in the world trading arena also came to naught when nation states jealous of their sovereignty withheld their support. Meanwhile, however, international trade grew by leaps and bounds. And in 1995, the Treaty of Marrakech (culminating the Uruguay Round of trade negotiations) substantially broadened the rules governing international trade and investment and created a World Trade Organization to oversee their enforcement.

With these important steps taken, there has been renewed interest in moving forward toward harmonization of competition policy rules among trading nations and the designation of a supra-national organization (such as the WTO) to sustain coordination and conflict resolution functions. Several proposals, including my own,[35] have surfaced. Since I understand best the rationale and pitfalls of my own proposal, I focus here on it.

If progress is to occur, I believe, certain desiderata must be clearly acknowledged. These are embodied in my proposal.

For one, despite convergence, there remain enormous differences across nations in the substance of national competition policies. If an agreement is to be reached, it will have to be on some modest subset of core principles governing only transactions with

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[34] U.S. Department of State, <u>Havana Charter for an International Trade Organization</u> (March 24, 1948), p. 86.

[35] In <u>Competition Policies for an Integrated World Economy</u>, Chapter 5.

significant implications for international trade and/or investment. The most likely candidates are export and import cartels, serious abuses of dominant positions in the world market, and merger approvals, or at least, the paperwork processes underlying merger reviews.

Second, even in these core areas, many nations will be unwilling to go all the way to a flat prohibition. Brazil is unlikely to surrender its (usually unsuccessful) right to orchestrate an international coffee cartel, Saudi Arabia and other oil-producing nations their participation (however dispirited of late) in OPEC, Canada its right to control exports of potash (in which it holds a position analogous to that of OPEC) and uranium yellowcake, Russia its cooperation with the de Beers diamond syndicate, and the United States the dominance of Boeing in large turbojet airliner markets. Thus, exceptions will be necessary. Under my proposal, each nation would be allowed three four-digit SITC industry exceptions from a general ban on export cartels. As experience is gained, the number of exemptions might be progressively reduced to two and then one per nation.

Third, it must be recognized that historically, a consid-erable time interval passed before national competition policy enforcement agencies learned how to do their work effectively. Seven years elapsed between passage of the U.S. Sherman Act and the first Supreme Court prohibition of a price-fixing ring; twelve years between the Treaty of Rome and the first imposition of fines against European Community cartels; eleven years between the creation of the U.K. Monopolies and Restrictive Practices Commission and the first prohibition of a cartel by the Restrictive Practices Court; and 20 years between the post-occupation amendment of Japan's Anti-Monopoly Law and a Fair Trade Commission attack on illegal cartels, including the Commission's first criminal price-fixing indictment.[36] Before really serious enforcement can proceed, much learning and the perhaps also the building of political support must occur. Therefore, I would have any international body charged with competition policy responsibilities begin by confining its activities to investigation and the publication of reports on alleged border-spanning restrictive practices. Only in the seventh year (perhaps too few) of its existence would I have the agency undertake enforcement activities.

Finally, even after a considerable shakedown period, an international competition policy agency would have to tread warily, according considerable respect to national sovereignty. It would use the good offices of national competition authorities to support its investigations, and it would entrust national authorities with implementing recommended corrective actions. Only in cases of national intransigence would conventional WTO enforcement mechanisms be set in motion.

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[36] Tilton, Restrained Trade, pp. 33-35.

Despite the timidity of my proposals, it is questionable whether the community of nations would accept my proposed expansions of the WTO's mission.[37] My home nation, the United States, is likely to be at best a reluctant partner. Jealous of their own predominance in competition policy matters, the U.S. antitrust enforcement agencies have opposed internationalization proposals, preferring negotiated bilateral arrangements in which they play a leading role. Ratification of the Uruguay Round treaty by the United States Senate was a close call, achieved in part by the Administration's acceptance of provisions requiring a panel of U.S. judges to review WTO decisions contrary to U.S. positions and determine whether they were correctly decided. If within the first five years of the WTO's operation three of the decisions reviewed in this way are deemed unjustified, a mechanism will be set in motion under which Congress reassesses whether the United States should remain a WTO member. In other words, the United States has left a Sword of Damocles hanging over its participation in an already ratified institution.

When a would-be legislative draftsman cannot deliver the votes from his home constituency, he has little claim to leadership in the game of statesmanship. Perhaps therefore I should yield the forum to others with more solid mandates. Perhaps too one must accept a conclusion that the world is not yet ready for steps harmonizing competition policies across borders. What seems clear, however, is that the problems, and hence the pressures for new solutions, will not go away.

[37] When I presented these proposals at a Washington conference in March 1995, Judge Diane Wood commented that the world would adopt Esperanto as a universal language before it accepted a competition policy innovation like mine. Three days later I found myself in a Munich hotel watching a German television interview with the Common Market's chief translator. He observed that with the accession of ever more nations (and bilateral language combinations) to the Union, his task was becoming impossibly difficult, perhaps solvable only by the adoption of Esperanto.