COMPETITION LAW IN ACTION

Experiences from Developing Countries

Taimoon Stewart, Julian Clarke, and Susan Joekes

Canada’s International Development Research Centre (IDRC) is one of the world’s leading institutions in the generation and application of new knowledge to meet the challenges facing developing countries. IDRC funds applied research by researchers from developing countries on the problems they identify as crucial to their communities. IDRC builds local capacity in developing countries to undertake research and create innovations, believing that people from developing countries must take the lead in producing and applying knowledge for the benefit of their own communities. IDRC also fosters alliances and knowledge sharing between scientific, academic, and development communities in Canada and developing countries. IDRC’s headquarters are in Ottawa, Canada, with regional offices in Cairo, Dakar, Nairobi, New Delhi, Montevideo, and Singapore. For more information, write to IDRC at info@idrc.ca or visit our website, www.idrc.ca.
PRELIMINARIES & EXECUTIVE SUMMARY

FOREWORD

This book is a contribution by the IDRC to the understanding of competition policy and law for all stakeholders focusing in a special way on emerging and developing economies. It provides a valuable historical perspective, which traces the role played by various international organizations in shaping the course of Competition Policy as it is implemented, not only in developed economies but in developing ones as well. Indeed, it is a widely held view that the impetus for competition is externally driven; and this accounts for the limited political commitment which it enjoys in some developing countries.

For the competition tenderfoot the book successfully explains the relationship between competition policy and competition law. The authors note the wide range of policy matters that comprise competition; and this is very useful, especially for policy makers. Often individual issues are pigeonholed without due regard for other issues.

In this context, the specific experiences of selected countries provide a practical guide to governments and government officials struggling with designing an appropriate policy and/or drafting a complementary Law. The South African and the Uzbekistan experiences are rich examples of the kinds of issues that might be considered. In both cases, improving consumer welfare was a core consideration in determining the scope of the law. In highlighting these examples, the authors are also providing the business sector as well as consumers with an insight into what goes into the making of the law.

There is no equivocation: the strongest law can be rendered useless by weak and/or mindless enforcement. All competition authorities that enforce merger control provisions are faced with the challenge of determining which consolidations are likely to have anticompetitive effects; and which will produce those outcomes which will enhance competition. Inexperienced authorities will find in the South African Commission’s treatment of concentration in the steel industry a real lesson in applying merger law. Private sector firms and their lawyers, particularly in jurisdictions which are averse to merger control, ought to gain a great deal of assurance from the authors’ careful outline of what amounts to a proper application of merger law.

In a timely word to the political directorate, the book makes the critical point that effective competition enforcement requires adequate human and financial resources; a sound statutory instrument with appropriate and meaningful sanctions. It stresses too the need for the authority to be independent from routine control by politicians and holds a mirror up to governments and government officials, in highlighting the dangers of “cronyism” and weak political will to protect the competitive process.

The book targets all persons who are likely to have an interest in Competition Policy and Law at some level; and succeeds in adding significantly to the knowledge base of all target groups. The authors’ deep insight is reflected in their recommendation that each country establish a standing consultative committee for the purpose of undertaking periodic reviews of the efficiency of the law.

I recommend this book as a major resource not only for young competition authorities, but also for agencies and government officials of developed countries, given the value of periodic review in competition law enforcement.

Barbara Lee
Executive Director
Jamaican Fair Trading Commission
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ABBREVIATIONS

ANC: African National Congress
APEC: Asia-Pacific Economic Cooperation
ATA: (Competition) Agency-to- (Competition) Agency Agreement
BEE: Black Economic Empowerment
CARICOM: Caribbean Community (and Common Market)
COMESA: Common Market for Eastern & Southern Africa
CUTS: Consumer Unity and Trust Society (of India)
EU: European Union
FTA: Free Trade Agreement
FTC: (United States’) Federal Trade Commission
GATT: General Agreement on Tariffs and Trade
IDRC: (Canada’s) International Development Research Centre
INDECOPI: Peruvian Competition Authority
KFTC: Korean Fair Trade Commission
MCR: Merger Control Regulation
MERCOSUR: Mercado Comun del Cono Sur (Southern Cone Common Market)
MNE: Multinational Enterprise (in this book used interchangeably with UNCTAD’s Transnational Corporation (TNC))
NGO: Non-Government Organization
OECD: Organization for Economic Cooperation and Development
RTA: Regional Trade Agreement (in this book, RTAs encompass bilateral and multilateral FTAs and Customs Unions irrespective of geography)
SME: Small and Mid-sized Enterprise
SOE: State Owned Enterprise
UNCTAD: United Nations Conference on Trade and Development
USAID: United States Agency for International Development
USDOJ: United States Department of Justice
USVI: United States Virgin Islands
WTO WGTCP: WTO Working Group on the Interaction between Trade and Competition Policy
WTO: World Trade Organization
Since the early 1990s, the number of competition authorities has increased markedly around the world, and most of these have been established in transition and developing economies. These young institutions have faced many challenges, and experienced successes and failures. The knowledge of these experiences could prove invaluable to those countries that are establishing competition regimes, and particularly to young competition authorities that can learn from each other’s experiences. Canada’s International Development Research Centre (IDRC) has supported research on competition issues in developing and transition countries over the last five years to assist officials from these countries to understand the issues related to competition law, both at the domestic level and as they relate to trade. This information has helped formulate policy and negotiate trade provisions. This report draws upon the research findings from the IDRC sponsored projects in particular, but also other research findings where appropriate, to provide information, analysis and recommendations to assist young competition authorities.

IDRC’s approach to research in this field is outlined in Part 1, while Part 2 provides insights into the issues. The discussion indicates that competition policy has become significant to international trade and economic relations. The lowering of governmental barriers to trade and cross-border investment can be undermined by domestic companies through collusion or abuse of dominance, which can act as barriers to market entry. Furthermore, increased trade may expose countries to the anticompetitive behaviour of international cartels, whose activities may be more pervasive than common wisdom would suggest. Finally, countries are increasingly becoming aware of the advantages of having a competition law as means of enhancing consumer protection and maximising welfare. Part 2 distinguishes between competition law and competition policy, and provides brief explanations of the principal components of the law: prohibition of anticompetitive agreements; abuse of a dominant market position; and merger control regulation.

The challenges faced by young competition authorities are outlined, as a precursor to the substantive information provided in Part 3. These include the drafting of appropriate legislation, educating stakeholders, dealing with resource capacity constraints, and dealing with cross border anticompetitive conduct.

Section 3.1 examines the assertions of economic theory in favour of competition based on the experiences from developing countries. The evidence gathered here confirms that protecting and promoting competition is the most effective – perhaps in many circumstances, the only – means of attaining certain fundamental economic objectives. A strong argument is made for the benefits of competition law and policy in developing countries, using case examples to illustrate such benefits. However, there can be serious market failures in developing economies and in international trade, which require consideration when adopting competition law and policy. These considerations are necessary to advance development goals and maintain socio-economic stability. Examples are drawn from the studies to illustrate these caveats.

Section 3.2 addresses how competition law may be tailored to meet the specific needs of an economy. Analysts of competition law acknowledge that there will be winners and losers from competition law enforcement and that it may be appropriate for governments to intervene to buffer losing factors of production, such as labour, supporting them while they re-tool. However, this may not be easy in many resource-poor developing countries. Furthermore, there are market structures in some developing countries that are skewed in favour of entrenched elites with inequitable distributions of wealth with social stratification drawn along racial or ethnic lines. Competition law should be used cautiously in those circumstances if such inequity is potentially exacerbated by its enactment.

Policy makers are provided with many illustrations of the options available for defining the scope of the law. Examples are provided of laws that have
been tailored to address public interest considerations, such as South Africa's Competition Act, which specifically address the historically disadvantaged economic position of the native Africans and ensures that policies for entrepreneurial development are protected. Examples from Mexico and Costa Rica are also provided to show that access to basic needs by the poor can be protected. Disadvantages faced by very small firms, particularly in small economies are also highlighted, and the provisions in the competition law of the US Virgin Islands are quoted as examples of how these can be addressed. These laws are clearly aimed at protecting public interest and enhancing consumer welfare. The usefulness of exceptions and exemptions is illustrated by their use in the Jordanian and Moroccan examples, while the exclusion of state enterprises in Thailand illustrates the harmfulness of unnecessary protection. Finally, in developing countries a very large proportion of enterprises are informal. This obscures the analysis of real market shares and competition among firms and by the same token makes the drafting of the appropriate competition law and its enforcement more difficult.

The challenges of instituting a new competition regime are addressed in Section 3.3. New institutional arrangements – the laws and the competition authority itself – have a limited time-window within which to demonstrate their value. A society prepared ideologically for market competition is more likely to have an effective competition law. The authority’s credibility has to be earned within the family of regulatory institutions of the state. The competition law framework works best when it permits the competition authority, through its rulings, to generate strong and visible benefits to stakeholders. Several of the strategies used by developing countries to secure the legitimacy of its competition authority are described in the following pages. These include training judges, strong institutional leadership and the exercise of prosecutorial discretion. The unfortunate experience recounted in a Jamaican case study, in which the Law Association was prosecuted as its first case, demonstrates the importance of choosing the initial showpiece cases carefully to enhance credibility and wide public support.

Frequently, young competition authorities have inadequate resources. This Section emphasizes the importance of providing adequate funds for institution building and ensuring that the legislation allows large enough sanctions to deter anticompetitive practices and gives the tools to enforce those sanctions. Several young competition authorities such as Peru, Costa Rica and others are modifying their laws to provide for more robust sanctions, having recognized the weaknesses of their earlier provisions.

Involving crucial national stakeholders when introducing and implementing a competition regime is crucial for its eventual success. Successful implementation requires a culture of competition in the society whereby the two principal stakeholders – the producers and the consumers (both intermediary and final) – are made aware of the benefits of competition and act accordingly. Section 3.4 draws from the rich experiences found in the case studies and suggests means by which young competition authorities can involve and relate with the private sector, other government bodies, the media, consumer organizations and NGOs, and the research community.

In Section 3.5, the issues at the interface of trade and competition law are explored from the perspective of project findings and case examples. Cross border anticompetitive conduct can arise when foreign cartels sell their goods at cartelized prices to developing country consumers or impose conditions or prices on developing country suppliers. Competition can also be damaged by entrance of a large multinational enterprise, as for example through a merger. Specific problems, including jurisdictional issues and cross border cooperation are discussed. Cross border cooperation is shown to be a successful means of prosecuting some modes of anticompetitive cross-border transgressions. Included in this section is a discussion about international agreements, including competition law provisions in Regional Trade Agreements in addition to Agency to Agency Cooperation Agreements and less formal cooperation.
Guidelines are provided in Section 4 that draw on the arguments and conclusions formulated in the body of the book, so that the lessons and analyses of each section can be easily digested by policy makers. The Ten Key Recommendations drawn from all the case-studies in this book are contained in the list below.

Section 5 concludes with a vision of the vital role that a strong competition regime can play in boosting the authority and effectiveness of a government intent on promoting equitable growth and development.

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<td>1. Draft and enact a strong, enforceable and flexible competition law that is respectful of legal principles;</td>
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<td>2. Appoint and encourage strong leaders – energetic, non-partisan and competent – to direct the competition authority;</td>
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<td>3. Recruit diverse and expert staff and support the authority with reliable and adequate funding;</td>
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<td>4. Give specialized competition law training to judges likely to hear cases from the authority;</td>
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<td>5. Build alliances with competition law beneficiaries, counteracting opposition to competition law’s encroachment on the private sector. This will mitigate the risk of regulatory capture and engage stakeholders in the implementation process;</td>
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<td>6. Stir popular interest in competition issues – the media can be helpful here;</td>
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<td>7. Collaborate with other government departments and agencies whenever possible and oppose them when necessary;</td>
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<td>8. Tackle domestic and international cartels by providing immunity for the first defector, and levies penalties against the collaborators – a leniency programme;</td>
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<td>9. Overcome national legal boundaries by developing cross-border cooperation among competition authorities and including competition provisions in trade agreements to act against anticompetitive conduct; and,</td>
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<td>10. Stay vigilant against various forms of abuse carried out by very large foreign entrants into the domestic market.</td>
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## INDEX TABLE OF DEVELOPING COUNTRIES’ EXPERIENCES

This table lists the developing countries’ experiences in competition law synthesized in this book. Readers of an electronic version of the complete book can click on the page number to link to the applicable text.

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<td>Taxi transport as an example of municipal regulatory capture</td>
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<td>Roberts (2004)</td>
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PART 1: INTRODUCING IDRC RESEARCH INTO COMPETITION ISSUES

Canada’s International Development Research Centre (IDRC) has supported research on competition issues throughout the developing world since 2001. The IDRC is unique among developed country donor agencies because it is a publicly financed, but non-governmental, body which was founded in 1970 with a mandate to support scientific research to address development problems. Most of the research is done by developing country researchers themselves, although, in pursuit of the highest scientific standards, many international collaborative research projects have been supported involving researchers from all over the world. As the interpretation of its mandate has matured over time, IDRC’s objectives have coalesced around three pillars: generating new knowledge in different fields, supporting research capacity building in developing countries, and ensuring, not only that research is done on topics that are immediately relevant to current policy challenges, but also that the findings of IDRC-supported research are brought to the attention of developing country policymakers.

Support for research into competition has been done under the auspices of two programs that successively funded research into international economic problems: the Trade, Employment and Competitiveness program (1997-2006) and the Globalization, Growth and Poverty program (2006-). Prioritization of competition law emerged from two previously funded research themes: new elements in the agenda for international economic negotiations, at regional and multilateral level, and institutional aspects of efforts towards national economic reform and restructuring. Policy measures to protect competition are a central component in the establishment of the market system. Economists from Adam Smith and Marx onwards have recognized that markets have an inherent tendency towards polarization of outcomes in terms of incomes and producer power. As part of the disciplining of the international activities of investors and corporations, many different international regional and bilateral economic treaties and agreements had adopted competition provisions from 1957 onwards, with the signing of the Treaty of Rome. However this trend accelerated from the mid-1990s onwards.

The perceived need to review and rationalize those provisions was one of the reasons why a new, comprehensive competition framework agreement under WTO auspices was initiated as part of the Doha Development Agenda. The introduction of competition as an Agenda item was a somewhat startling challenge to the trade policy makers who were the main actors in those discussions. It provoked a need to better understand the issues driving competition law enforcement, and to inform their negotiating stance, as well as the dialogue between trade negotiators and competition experts. Moreover, there was little familiarity with the operation of competition law in developing country settings at this time. Investment in research in this field therefore seemed to IDRC to carry the promise of being able to generate much better knowledge about competition law in the development context and to feed those research findings into the policy making community.

IDRC’s research support has been directed to improve research-based evidence on a number of issues related to the design and implementation of policies to promote and protect competition in developing country markets. The research is always specifically related to the developing country context, i.e. informed by consideration of developmental goals and objectives. Emanating from an international economics research program,
IDRC support has paid special attention to cross-border competition problems, with particular reference to the exposure to anticompetitive practices from abroad that comes with the liberalization of trade and investment. But to ignore domestically generated anticompetitive practices, which anecdotal evidence suggests are endemic worldwide, would be unbalanced. Thus, the diagnostic scope of IDRC supported research has covered analysis of the problems related to anticompetitive conduct at all levels: local, domestic, regional and international. Similarly, IDRC projects have given consideration to the potential for policy development in all available arenas, ranging from local level measures to national and regional structures, and the agenda of global negotiations.

Research support has been given to many different types of institutions including universities, international organizations and non-governmental action-research and advocacy organizations. University based studies tend to be purely academic in inspiration and execution, international organizations have special skills in synthesizing and publicizing research findings for policy audiences, and NGOs receiving IDRC support are encouraged to carry out and use more research-based evidence in their advocacy work. IDRC believes that providing support for such combinations of topics and policy research actors, and feeding their findings into policy debates, is a good way of bringing rich, empirically verified material to the attention of policymakers as they manage the political process to design and implement policies for development.

This book distills the lessons arising from this body of IDRC-financed research for the effective implementation of competition law. It is structured as a guide for the staff of young, or not-so-young, competition authorities in their work of helping to construct and patrol the foundations upon which market economies in developing countries are being built. It conveys the practical findings of research to assist the day-to-day work of competition law practitioners. While written specifically for such practitioners, the book should also be useful for officials in various branches of government, such as trade and industry ministry officials, who interact with competition practitioners and need to understand the purposes of competition law enforcement. It should also interest practicing lawyers and consultant economists, researchers and policy analysts, and civil society organizations and interest group representatives.

Most of the concrete examples and illustrations are drawn from the body of work supported by IDRC in many countries over the past five years, which is systematically analyzed here for the first time. Information on these research activities is available on the IDRC website at www.idrc.ca/competition. This book sets out the findings from these studies in relation to the wider literature, partly to show how the IDRC work has added value and partly to suggest how debates around key points of controversy have been evolving over time.
Imagine an open air market in a developing country — a busy, bustling, lively place. Customers move from one vendor to another, testing the produce, haggling over prices, seeking the best value for their money. The vendors extol the virtues of their produce, offer bargains in an effort to attract more customers. It’s an age-old system that is based on open competition; vendors who offer the best value do the most business, and the customers benefit.

Now imagine a market where all the poultry vendors sell their chickens at the same price, a price that always seems to be a little higher than last week, just like the price of sugar, which has gone up — again! To make matters worse, the bank charges more and more commission to release the money that your family members send from their jobs overseas. Then there’s the bus ride back to the village. There used to be several bus companies. Now there’s only one, and the fare has doubled. But what can the consumer do if there’s no competition?

Sometimes it is difficult to distinguish anticompetitive practices from the workings of a perfectly competitive market but what might have happened here is that the poultry producers and sugar manufacturers have formed cartels so that they can force up prices and make ever larger profits. The bus companies may have merged to give the new owners a monopoly and the freedom to charge whatever fare it believes the market will bear. The bank may have reached an exclusivity agreement with the company that transfers money from one country to another, effectively shutting out competitors. And if such is the case, it is the welfare of the consumers that suffers because of the lack of competition. Tax payers too pay the price, as a result of bid rigging, if governments have been forced to pay billions of dollars over the real cost for building roads, schools, and hospitals. The problem has an extremely important international dimension as well: price fixing by international cartels seems to be a pervasive, world-wide phenomenon.

2.1. Why has Competition Policy Become an Issue?

In the last decade, competition policy has become an integral component of development policy in the South as understanding has grown of the need to put in place complex sets of market institutions to support economic growth and policy management capability.

In the last two decades or so, there has been ever increasing international economic integration. This is seen particularly in the disaggregation of production processes facilitating outsourcing and offshoring (mainly from developing countries) of components in the production chain, and in the exponential growth in the services sector, including export of services, facilitated through utilization of information and communications technologies.

Old systems of production and products have become obsolete and therefore unprofitable, and developing countries are busily restructuring their economies so as to integrate into these new global production structures and seize opportunities for new lines of production.

This restructuring involves a new approach to competition policy. It includes enhancing competition in domestic markets by dismantling the protective border barriers and restrictive investment rules that have prevailed since the middle of the last century, and creating an enabling domestic environment to facilitate foreign investment and trade. As far back as early 1980s, developing countries had started liberalizing their
economies under IMF/World Bank Structural Adjustment Programmes, a conditionality of debt rescheduling. The process of trade liberalization was accelerated by the successful negotiation of the General Agreement on Tariffs and Trade (GATT) 1994 in the Uruguay Round, by which tariffs were lowered considerably, particularly in non-agricultural goods, by industrialized countries.

The need to introduce competition legislation was increasingly seen to be closely linked to this process because anticompetitive arrangements can negate the intended positive welfare effects of lowering tariffs and removing other barriers to trade. The need to adopt competition law has accordingly rapidly been taken up into the discourse and the agendas of international trade and investment negotiations. Accordingly, consideration of the links between trade and issues related to competition law was included in the Agenda of Doha Round of WTO negotiations as one of the Singapore issues, although it was never moved into the negotiations agenda itself. Competition law provisions are prevalent in many regional trade agreements.

Notwithstanding these external factors, many developing countries have embraced the need to liberalize their economies and embarked on processes of economic policy reform anchored in market liberalization, coupled with some degree of privatization of state owned enterprises. Adoption of a competition law is vital to ensure not only that the consequent growth of the private sector serves the public interest but also that the efficiency of the state enterprise sector is improved. This is now being acknowledged by developing countries (despite continued use of industrial policy to support national champions and/or sunrise industries).

The growing interest in competition law is reflected in the increasing number of countries that have adopted competition legislation. Since 1985 the number of countries with some sort of competition law on their statute books has almost doubled. In 2006 approximately 100 countries had a competition law in effect, many with a competition authority of some kind in place to enforce it. Among these are Costa Rica, Panama, Peru, Jamaica, Barbados, Egypt, Turkey, and several countries from Eastern Europe and the former Soviet Union, Asia, and Africa. This reflects the increased understanding of the value of competition for growth and development, and the fact that its benefits are undermined by anticompetitive practices.

Competition law aims to keep markets as competitive as possible by preventing firms from engaging in strategies to limit competition. In “competitive” markets, as defined here, there are many firms operating; their ability to set prices is limited in that if they charge above the market price, they would lose their customers; information is widely available to producers and consumers; both entry and exit are relatively easy for firms in the market; externalities are limited; infrastructure is adequate; and contracts can be enforced and property rights protected (gleaned from Carleton and Perloff, 1999, p. 85). When these characteristics apply, economists infer that the market functions well as an institution and permits resources to be used efficiently and welfare (consumer and producer surplus) to be maximized. Seen in this perspective, competition law is one of the key measures needed to support the proper functioning of markets in the fullest sense. It is the primary means of addressing a major form of market failure i.e. the harmful exercise of market power. Once the purpose and application of competition law and analogous measures are better understood, and methods of implementation are refined and proven, then market expansion takes its place as a proper and valuable aim of development strategy.

However, one should note here that competition law can only be enforced in national jurisdictions, so that while there are anticompetitive conducts emanating from other countries with cross-border effects, foreign perpetrators cannot be reached by the national law. Cooperation with other competition authorities is required to deal with cross-border cases, but there are many problems associated with this, which is dealt with later in the book.

Enforcement of the law is good for growth and development for many reasons. When firms can
freely enter a market they increase the pressure on firms already in the market, forcing them to be more efficient to maintain their market share. The less efficient firms will tend to drop out of the market as the number of firms increases. The process of entry and exit from the market is beneficial for growth and development, in the following sense:

- the process induces increases in the competitiveness of firms of all sizes because it delivers improvements in efficiency, innovation and productivity;
- firms that conspire to avoid competing undermine human and social development because they re-direct consumer welfare benefits to themselves in the form of rents;
- prohibiting anticompetitive practices in the private sector has indirect effects on development. Competition in the market prevents the erosion of beneficial government policies and programs which are intended to provide, or facilitate the provision of goods (such as medicines), services (such as transportation) and infrastructure investments of all kinds;
- a competitive environment motivates firms to attain the minimum level of costs for a given level of output;
- the enforcement of competition law ensures that the intended benefits of trade reform are achieved;
- a well-structured and enforced competition law makes an economy more attractive as a location for foreign investment and maximizes the benefits that flow from such investment; and
- greater competition in the product market creates incentives for firms to innovate.

Through all these mechanisms, prohibition of anticompetitive behaviour results in consumer welfare gains by inducing lower prices and better quality of goods and services.

2.2. WHAT IS COMPETITION POLICY?

From the very beginning, economists – most famously Adam Smith, the father of them all – have noticed that business people are prone to conspire together. “People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public.” They are driven by a wish for larger profits than their efforts and aptitudes and the competences of their enterprises would normally provide, and try to manipulate the market, hamper their rivals’ operations, limit the entry of new firms and force up final product prices to achieve their goal. Some forms of business collaboration are beneficial in improving efficiency and reducing information gaps. Such cases need to be acknowledged. However, collaboration is exclusionary and exploitative when it is designed to boost the profits of the colluding firms. Such collaborations decrease productive efficiency and consumer welfare and may result in the misallocation of government expenditures. As a consequence, they hold back growth and development. The objective of competition policy is to frustrate damaging practices of this kind and ensure that competition is protected in markets.

A specific instrument of competition policy is competition law, that is, the adoption of legislation to prohibit anticompetitive conduct by the private sector that reduces competition in markets. But a competition law is only one of a range of policies adopted by governments to advance the process of liberalization and market development; others include trade, investment, and other general government policies which affect competition within an industry or market.

Another specific instrument of competition policy is regulation. Specifically for industries or markets in which market failures or particular sensitivities are expected, a framework should be in place to regulate prices and/or quality within that industry.
or market. Recent trends to privatize state owned enterprises and modernize utilities often require regulation. Regulation can be considered an extreme instrument of competition policy which shares many of the same tools (such as rent and cost-of-capital) that competition law uses. But regulation is different – there is a principal/agent relationship between the regulator and the private sector provider (Motta 2004, p. xviii).

Competition law is thus a sub-set of competition policy (see schematic). Competition laws can deter one important source of market malfunction – that created by market power 1. This book focuses narrowly on the challenges to competition law legislation and enforcement in the context of those other policies and instruments.

Competition law rests on two pillars: the behaviour of firms and the structure of markets, insofar as each may reduce competition. Pragmatists also recognize that public policy (be it industrial or social policy) plays a role in legislating and applying competition law. This book describes many concrete cases of the interaction of those pillars and that influence drawn from IDRC-supported research studies.

Competition law addresses the following three main situations:

- **Abuses of dominance.** Dominance, in an economic sense, refers to a disproportionate amount of market power in the hands of one firm. If a firm is sufficiently powerful – i.e. large enough relative to its market – that it can act without taking into account how its competitors may respond, then it may be defined as dominant. Abuses of dominance include predatory pricing (pricing below cost to drive competitors out of a market and then raising prices after their demise), tying up distribution networks (not allowing distributors to carry competitors’ products) to exclude competitors in the market, denying competitors access to essential facilities without which they are unable to provide related goods or services and tied selling (requiring the purchase of a product not linked to the primary purchase).

- **Anticompetitive agreements,** including collusion by two or more firms to fix prices, create price inflating scarcity through jointly limiting production, divide markets up geographically amongst colluders and rig bids in tendering for government contracts.

- **Merger control regulation** (MCR) generally requires that firms with joint market share above a designated percentage have to notify the competition authority of their intention to merge. The authority investigates and determines whether the merger would lead to over-concentration in the product markets in which the firms trade, or would substantially lessen competition in the markets. In most cases, mergers are allowed, with a requirement to divest products and production facilities where markets would be substantially affected by a lessening of competition.

MCR ensures that prospective mergers do not lead to over-concentration in product markets and excessive market power that would expose the economy to a firm’s possible abuse of its dominant position. MCR is more powerful than the instruments available for abuses of

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1 A short glossary of some of these terms is provided in the References & Closing Matters at the back of this book.
dominance or anticompetitive agreements. This is because MCR is pre-emptive – economists would say *ex-ante* – whereby an authority can block an event (the merger) occurring. Responses to the other two situations are reactive (*ex-poste*) whereby the events have already occurred.

However, several countries do not provide for MCR in their law. There is a heated debate on whether MCR is relevant for developing countries, particularly small economies, where concentration may be necessary to achieve economies of scale and competitiveness, both in domestic and export markets. For instance, neither Peru nor Jamaica provide for MCR in their laws. However, there is a trend towards adoption of MCR because its value is increasingly being recognized. Concrete cases are drawn later in the book to demonstrate the value of having a MCR.

### 2.3. Challenges of Introducing Competition Law

**Drafting of Appropriate Legislation**

There are obvious gains from prohibiting anticompetitive conduct, but developing countries face major challenges in legislating and implementing competition law. While in Canada, the United States and the EU, competition law provisions evolved over a long period of time and were shaped and re-shaped to suit changing local economic realities, the competition provisions in force in those jurisdictions have largely been copied by developing countries without being tailored to the precise needs of their economies. The current laws in industrialized countries address situations with complex and technologically advanced business structures and relations and an array of formal market institutions. This is not the case in most developing countries. There can therefore be a disconnection between the legal provisions being adopted by developing countries and their economic realities.

Consistent with this critique, some developing countries have been emphasizing that the “one size fits all” approach will not work. Yet, little research had been done to understand the differences in how competition functions in developing economies as opposed to industrialized countries. IDRC funded projects on competition law have been addressing some of the gaps in this knowledge. With better understanding of the differences, competition laws could be shaped to respond to the specific needs of developing economies, case by case. Specifically include developing an understanding of market structure and firm conduct in order for the legal provisions to:

- place emphasis on prohibiting the most prevalent anticompetitive actions that affect development goals;
• determine the appropriate formula for fines so as to provide a serious disincentive to market participants;
• assign a level of resources appropriate to the role of the competition authority as a key agent of reform and development;
• tailor merger control regulation to the institutional capacity and market size of the country; and
• arrive at the appropriate threshold for determining a firm’s dominance in a market.

EDUCATING STAKEHOLDERS

Competition law cannot succeed unless there is societal understanding of the law and acceptance of its value to development policy. Competition advocacy is the means by which the benefits of legislation are explained and disseminated through various levels of society, including the government and the judiciary. Difficulties go beyond determining the content of the law to the problem of introducing it to stakeholders who do not understand the intent of the law and its benefits, and overcoming the objections of those whose interests would be negatively affected by the law. Difficulty in getting the legislation through the legislative body (Parliament or Congress) is symptomatic of such problems. Once the law is passed, there are a host of problems faced by the competition authority in establishing the institution and enforcing the law. In general, there is therefore an urgent need to engage in advocacy with stakeholders, including other public institutions, in order to build a culture of competition in the society that is receptive to and supportive of a new competition regime.

RESOURCE CAPACITY CONSTRAINTS

Lack of resources and financial and institutional capacity, particularly skilled human resources, is a huge obstacle to successful implementation. Without judges and lawyers trained in competition law, skilled staff in competition authorities able to discern anticompetitive behaviour, journalists with understanding of the law and its benefits who can act as watchdogs, consumer groups and NGOs that also can be watchdogs for the society based on understanding of the law, it is very difficult to implement a competition regime and enforce the law. Institutional weakness is a pressing and chronic problem in developing countries.

DEALING WITH CROSS BORDER ANTIMCOMPETITIVE CONDUCT

The liberalization of market economies and globalization of trade has empowered market actors to initiate anticompetitive conspiracies, such as international cartels, that stretch across national borders and are seemingly invulnerable to the laws of one single country. The challenges of developing and implementing a domestic competition regime are compounded by the need for dealing with cross-border anticompetitive conduct that impact on the domestic economy. Enforcement of competition law is almost entirely confined to national jurisdictions. Therefore, if a firm or group of foreign firms engages in anticompetitive conduct that adversely affects competition or consumer welfare in another country, there is no recourse for the authorities in the affected market to discipline those firms. Yet, international cartels – which can arise either in formation and/or scope of action – exist in the global economy and are increasingly targeting countries where there are no competition regimes, or where enforcement is weak. Levenstein and Suslow (2001) have shown that,

In 1997, the latest year for which we have trade data, developing countries imported $81.1 billion of goods from industries which had seen a price-fixing conspiracy during the 1990s. These imports represented 6.7% of imports and 1.2% of GDP in developing countries. They represented an even larger fraction of trade for the poorest developing countries, . . . [where they] . . . represent 8.8% of imports.

Competition authorities in industrialized countries, particularly the United States and the EU, have been increasingly successful in uncovering international cartel activity and successfully investigating and prosecuting conspirators.
Leniency programs were largely responsible for the successes, as well as deep cooperation between the Competition Authorities of the US and EU. Leniency programs confer immunity from prosecution on a member of a cartel if he is the first to come forward and blow the whistle on other cartel members, providing evidence of the agreement and helping in the investigation. In the last decade, many cartels have been uncovered and successfully prosecuted by the US Department of Justice because of whistle-blowing by a member, as for instance, in the Vitamin Cartel and the Lysine Cartel cases (vitamins and all foods containing vitamin additives, and animal feed in the case of the Lysine cartel), both of which impacted on cost of basic foods in developing countries since there is evidence that the cartel agreement extended to these countries. The problem, though, for developing countries is that invitation to whistle-blowing is only effective if the Competition Authority is feared, necessarily meaning that it is strong and powerful, and the consequences of discovery and prosecution are dire enough to provide a serious disincentive.

Developing countries need to find a way to deal with international cartels whose activities adversely affect their economies. One major obstacle is the lack of formal and informal cooperation between authorities. Another is the fact that foreign firms may be protected by the confidentiality laws of the country in which they have their home base. Lack of knowledge and skill in investigating international cartels, combined with the extreme power asymmetries between the governments of some developing countries in relation to large multinational enterprises (MNEs), may also play a role. In the discussions of the WTO Working Group on the Interaction between Trade and Competition Policy (WTO WGTCP), which was active between 1996 and 2003 when issues related to competition law were under consideration within the framework of the WTO Doha Round, the depth of cooperation to allow developing countries to effectively deal with international cartels was the burning issue. Cooperation also features regularly in the negotiations on competition provisions in RTAs (see graph).

The limitations posed by cooperation at bilateral and regional levels raise the question of whether a multilateral (more or less worldwide) agreement on competition law and policy would benefit developing countries. In fact, two multilateral agreements already exist, but they are severely limited.

The first is the UNCTAD Set of Mutually Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices. The Set (as it is known) was negotiated during the 1970s and adopted in 1980 by the General Assembly of the United Nations. The objectives of the Set are to ensure that:

- Restrictive business practices do not impede realization of the benefits of trade liberalization;
- Competition is protected in the market and concentration of capital and economic power are controlled;
- Social welfare is protected; and,
- Disadvantages to trade and development resulting from restrictive business practices are eliminated.

The Set proscribes anticompetitive agreements that restrict competition in the market; it also prevents abuses of dominant market position and calls for merger control regulation. However, UNCTAD cannot bind governments to adopt and enforce the rules.

The OECD countries agreed upon Guidelines for Multinational Enterprises, first adopted in 1976 and
revised in 2000, as part of the OECD Declaration on International Investment and Multinational Enterprises. These guidelines include a competition section which requires MNEs to refrain from entering into or carrying out anticompetitive agreements among competitors to fix prices, make rigged bids, establish output restrictions or quotas or share or divide markets by allocating customers, supplies, territories or lines of commerce. They are also required to conduct their activities in a manner consistent with all applicable competition laws, cooperate with competition authorities in other jurisdictions providing prompt and complete responses as practicable to requests for information, and promote employee awareness of the importance of compliance with all applicable laws. All entities, including parent companies, local subsidiaries, as well as intermediary levels of organization, are expected to cooperate and assist. The Guidelines were largely ineffective until they were followed up in 1998 by the Recommendation of the OECD Council Concerning Effective Action Against Hard Core Cartels, inspired by the success of the US Department of Justice’s prosecution of international cartels and the realization that they are much more prevalent than was previously thought.

Efforts towards creating a new multilateral framework for competition in the WTO through the debates in the WTO WGTCP led to a realization that most developing countries were uninformed about competition law and policy. There was recognition that at the national level, countries were moving towards introducing competition regimes but without the necessary expertise. These national efforts have been supported by technical assistance from international organisations such as the WTO, UNCTAD and the World Bank. These technical assistance initiatives aimed at raising awareness of basic concepts of competition law and techniques of enforcement and have alerted developing countries to the dangers of cross-border anticompetitive conduct. The WTO, for example, has responded to country requests for technical assistance by providing national workshops to train the staff of competition authorities and ministry officials even while exploration of issues related to the interaction between trade and competition policy have been placed in indefinite recess. For example, in 2005, the WTO conducted national workshops for Trinidad and Tobago as well as Ethiopia, and it has held regional workshops in Latin America, Asia, the Middle East, Francophone and non-Francophone Africa, and elsewhere since 2001.

UNCTAD has been even more active, producing a regular output of literature and dissemination events, many of which have been sponsored by IDRC. The Competition and Consumer Policies Branch of UNCTAD has sponsored at least five regional dissemination events over the past twelve months, disseminating the importance of cross-border issues within the context of regionalism on the basis of a book dealing with this subject, while also supporting several competition projects in Latin America and other regions. The World Bank, for its part, regularly organises conferences to explore various issues associated with multilateralism, legislation and, more recently, regional aspects of competition law enforcement.

A vigorous debate took place as to whether a different kind of multilateral agreement is needed; one that would enable developing countries to tackle egregious practices from abroad. The WTO Doha Development Round included talks toward this end in its Agenda for a while. The differential impact of such an agreement on developed versus developing countries was one of the sticking points that led to the suspension of discussions on potential negotiations at the WTO. Developing countries felt that they were being persuaded to legislate and implement competition provisions which would indeed enable them to prosecute international cartels whose conduct impacts on their economies, but that they were being given no guarantee that the necessary evidence would be shared through cooperation and assistance with developed authorities. Yet most MNEs are headquartered in developed countries and evidence would most likely reside in their jurisdiction. Furthermore, they were concerned about the fact...
that the WTO is a sanctions-based institution, and were uncertain about the implications for industrial policies designed to shelter domestic industries from the full force of international market pressures. Further, they argued that anti-dumping measures were being used as protectionist policies by industrialized countries, and this was anticompetitive, but not being adequately addressed by WTO members.

Academic arguments have been put forward both for and against a multilateral framework on competition of a type that might have emerged in the WTO. Those opposed (most prominently Bernard Hoekman and his co-authors: Hoekman and Mavroidis (1994, 2000, 2002) and Hoekman and Kee (2003)) argue that the limited adoption of international trading system rules, along with government practices, which they allege are more damaging than private restrictive business practices, are the main cause of problems. Accordingly, they argue that full implementation of trade liberalization and restriction of the actions of governments with anticompetitive effects would be a more useful endeavour for WTO trade negotiators than formulating a competition framework. Those in favour, notably Evenett (2003, 2006), argue that a multilateral framework or framework(s) is a necessary complement to national legislation and enforcement because of the flourishing of international cartels since the liberalization of cross-border trade in the 1990s. They propose that in the light of the failures of inter-agency cooperation under other arrangements and the weak character of existing multilateral agreements, the only way to prosecute international cartels and discourage others from forming is through a multilateral agreement anchored in dispute settlement procedures such as those of the WTO.
PART 3: DEVELOPING COUNTRIES’ EXPERIENCES

The following section details the experiences of new competition authorities in developing countries – the constraints they have faced and the strategies they have used to overcome impediments. Lessons are drawn and guidelines and recommendations provided for consideration. The issues have been classified into five discrete areas, framed by the following questions:

- Has enforcement of competition law benefited developing economies?
- How can competition law be tailored to meet the specific needs of an economy?
- What are the challenges to legislating and implementing competition law?
- How and why are stakeholders involved in the implementation process?
- How can competition authorities deal with cross-border anticompetitive conduct?

3.1. HAS ENFORCEMENT OF COMPETITION LAW BENEFITED DEVELOPING ECONOMIES?

This section illustrates the benefits that have been observed to flow from the enforcement of competition law in developing countries. It also provides some evidence of benefits derived from trade liberalization, but provides caveats, illustrating where there may be a need to keep trade barriers in developing countries for the time being.

Since collusive business practices can be exclusionary or exploitative, or both, the rewards of competition law enforcement make a contribution to what could be called ‘economic democracy’, a term coined by David Lewis, Chairperson of the South Africa Competition Tribunal. The concept of economic democracy has two main fields of application in this context. First, it speaks to the direct social welfare effects of competition law enforcement. Competition law promotes the sovereignty of the consumer. Consumers pay the price for anticompetitive behaviour when they are overcharged for goods and services. Maintaining competitive consumer prices and improving consumer choices enlarges citizens’ economic power in their capacity as consumers. Secondly, when firms’ exclusionary behaviour is directed at rivals, it either depresses the profits of incumbent firms or erects entry barriers to new firms. Removal of entry barriers allows new firms to flourish wherever persons with entrepreneurial flair can identify profitable opportunities. Accordingly, we examine some examples of the benefits of competition law enforcement in terms of the distribution of assets as well as prices.

It is important in this connection to note that anticompetitive behaviour is not limited to large firms. Comprehensive implementation of competition law forces even the smallest entrepreneurs to refrain from engaging in anticompetitive conduct. This gives more individuals a stake in the productive assets of the country. In electoral democracies, citizens can only occasionally express their political opinions through the ballot box. By contrast, as David Lewis noted, economic democracy, made real through competition law enforcement, is a continuous process.
PROTECTING COMPETITION BENEFITS THE ECONOMY

It is widely accepted among academics and practitioners that competitive markets – open to free entry and exit – have a compelling effect upon the agents operating in that market. It is not just that the anticompetitive conduct will restrict output to raise prices – what economists refer to as extracting rent and causing allocative inefficiency – but there will also be productivity effects particularly over time. To remain in a competitive market, market players must maintain constant evolution in their product offerings and vigilance over their internal procedures. This requires a constant streamlining of their operations, and a close eye on the products being offered by their competitors. Without this pressure to reduce costs, increase efficiency and innovate, productivity will tend to slow down (or not rise to the potential).

A case in which enhancing competition in the market yielded benefits is demonstrated by the study of productivity increases observed across a spectrum of industries in Tanzania after the Fair Trade Practices Act was adopted by the government of Tanzania in 1994 proscribing anticompetitive behaviour. The author, Godius Kahyarara (2004), gathered firm level data to examine the changes wrought upon industries as a result of this law, and built a comprehensive database upon which the interaction of competition law and productivity could be modeled. The analysis revealed that markets with five or more competitors achieved 13-24% increases in firm productivity. The sophisticated econometric modeling and intricate firm level information used by the author gave strong support to these findings.

That increased efficiencies can apply to the country as a whole is seen in the case of Korea. Two sets of regulatory reforms were studied in Korea, one study looked at reforms that began in the early 1980s (see below) and another set looked at the reforms after the 1998 financial crisis. Mikyung Yun as part of an IDRC-supported project (Yun 2004) studied the post 1998 reforms. The impact of these reforms on employment, reduction of public burdens and the curtailment of government cost were measured. The regulatory reforms included more than just competition law – more than 324 regulations across 30 different government bodies were examined in total – but all were closely linked to competition law principles because they were specifically designed to work in combination to break down the system of large industrial conglomerates known as chaebols.

The discriminatory buying practices and supplier relations of chaebols, which had dominated the South Korean economy prior to the financial crisis in 1997, systematically disregarded competition law principles. According to Yun, application of the new measures had the potential to create one million job opportunities, with a ‘reduction of burden’ (meaning a reduction in the amount to be paid by the private sector for regulatory compliance) of 4.9% of GDP. This latter figure can also be interpreted as a gain to the economy of the same proportion. In major Korean industries such as electricity, construction, distribution and transport, gains were in the magnitude of between 4.3 and 4.8%. The impact of regulatory reform in the telecommunications sector was estimated to be in the order of 15%.

A study of plant-level data for the period 1990-1998 by Hahn (2000, quoted in Yun, p. 252) showed that plant entry and exit rates in the manufacturing sector are high, and that entry and exit accounted for as much as 45% and 65% of productivity growth during cyclical upturn and downturn, respectively. It seems that firm selection is an important part of productivity growth and market competition. Entry and exit are important whether through mergers, acquisitions or greenfield (newly established) operations.

Several studies have pointed out the social benefits accruing in Korea after the outlawing of the monopolistic and oligopolistic structures that were formed during the period of chaebols-led rapid economic growth. For instance, a study by Joseph Seon Hur (2004) demonstrated the benefits of a general application of competition law and its challenges. He pointed out that the annual social welfare loss fell from an estimated 8.45% of GDP in 1981 to 3.31% by 1995, with the improvement
attributable to the implementation of monopoly control regulations in Korea, which resulted in steady increases in social welfare.

Enforcement of the competition law uncovered the existence of some interesting cartels. One was among manufacturers of student uniforms, involving three firms whose combined market shares totalled approximately 50% of the market, and which had acted in concert to fix prices to increase their joint profits. The annual consumer burden imposed by the cartel was estimated by the Korean Fair Trading Commission (KFTC) at 60 billion won (about US$64 million). The antitrust measures taken to correct the market distortion included 11.5 billion won in surcharges and an injunction order.

The KFTC also uncovered a set of anticompetitive practices in bid rigging for public construction projects. The projects involved the construction of a bridge, the purchase of rolling stock and the construction of the West Coast Expressway. These projects were separate from each other and the instances of bid-rigging did not emanate from the same companies in each case. The price of each of these projects was 20-30 trillion won (US$ 21 - 32 billion at present exchange rates) each year. The overcharges paid to contractors in the bid rigging scandal diverted resources that could have been spent on vital infrastructure such as roads, hospitals and education. The discovery of these bid rigging practices led the government to construct a permanent information collection system on public bids and to reduce the number of bid contracts the government puts out every year. The saving to the public finances from these measures has been estimated at 4 trillion won (US$ 4 billion) (Hur 2004).

In Jordan, a clear link has also been established between market concentration, barriers to new market entry and stagnant productivity. The authors, Ibrahim Saif and Nesreen Barakat (2005) examined productivity in textiles and clothing, beverages, paper and paper products, electrical machinery, pharmaceuticals, transport equipment, dairy products and plastic industries to measure the impact of concentration and barriers to market entry on firm productivity. The authors examined both capital and labour market productivity, while controlling for the unique aspects of the Jordanian economic environment, such as traditionally easy access to capital combined with incentives to invest in certain domestic industries, alongside a growing labour force.

The results were interesting. As expected, the authors found that firm productivity declined over the period during which market concentration and barriers to entry were at their highest. Conversely, productivity tended to improve as external pressures forced businesses to innovate. Furthermore, the study found that in some sectors there was a transition period of low productivity once the markets had been opened to competition from abroad, as firms struggled to compete against new market entrants. Overall, however, concentration and the protection of industries from competition were strongly associated with low productivity. The authors suggested that the results of their study demonstrated an important policy finding: concentration does not lead to exploitation of economies of scale, but tends to be misused by the beneficiaries to increase their profits and has a negative impact on productivity.

In South Africa, the application of a vigorous competition law has been the catalyst for greater efficiency in the steel sector. Following the withdrawal of the government from the sector in the late 1990s, new players were able to join the industry and existing players undertook a series of manoeuvres to maintain and increase their profitability and productivity.

The South African case also shed light upon the complicated nature of mergers (Roberts 2004). Post-liberalisation, the largest steel companies began to consolidate operations: Baldwins Steel was acquired by Trident Steel in 2000, Baldwins/Kulungile and Abkins become one entity, and Iscor steel acquired Saldhana in 2002. These mergers covered large portions of the market. Problems arose because, as the numbers of market players went down, the potential for anticompetitive behaviour increased. Indeed, high market concentration often signals that firms are working together to increase barriers to entry or to coordinate prices or output. In some instances,
however, the nature of an industry such as steel may, for reasons of production technology, demand a small number of players due to the minimum efficient scale of plants. In South Africa the competition authority was called upon to determine whether market consolidation between market players was a sign of anticompetitive behaviour. It decided that it was not. The authority chose to tolerate some concentration of the industry on the grounds that the combined operations of the merged steel companies would enhance efficiencies of production. It considered that although Saldhana had been a ‘failing firm’, its acquisition by Iscor, which was also losing money, would create an immediate efficiency effect in terms of scale and scope of production. The end result was that Iscor quickly became profitable, as did the newly-merged Trident steel. This result may indicate that the merged entity became more efficient or that its market power enabled it to raise prices, which shows how tricky the assessment of mergers can be (Roberts 2004, p. 238).

In Uzbekistan, a recent study funded by IDRC drew attention to a particular economic problem that had arisen as a side-effect of the country’s transition from a state-led to capitalist economy. The geographic and linguistic remoteness of Uzbekistan arguably had made it susceptible to market dominance in the area of foreign currency remittances, due to the high numbers of Uzbek workers sending money from abroad and the low level of sophistication in the finance industry. Many Uzbek families are dependent on the salaries of family-members working outside the country. Foreign remittances are largely spent on essential items such as food and education.

The research uncovered evidence of overcharging of migrant Uzbek workers remitting their foreign earnings back to Uzbekistan with direct impact on the social welfare of the people. Service providers such as Western Union and Travelex had penetrated the market in Uzbekistan and established dominance by signing a number of exclusivity deals with remittance agencies. This allowed them to raise the charges for remittances transfers to high levels because their market power gave them a significant advantage in being able to dictate the charges on any money that was remitted into the country. The Uzbek competition authority acted upon this finding to modify government legislation controlling such foreign remittances and the finding provided justification for the government to establish a new foreign remittance provider through the national postal service.

The foreign remittance providers then entered into negotiations with the authority and took steps to comply with the new regulation. The company in question had not technically broken any competition law, and amended its behaviour once the results of the initial study had become clear. The study had the further benefit of outlining the size and social and financial importance of this sector. The dissemination aspects of the project alerted government ministries, banks and potential players in this market (such as the domestic postal service, which had ambitions to set up its own remittance project) of the importance of the foreign remittance market to direct investment into Uzbekistan and as a social welfare mechanism supporting many Uzbek families.

These findings are all consistent with the broader academic literature. A study of transition economies, which provide a fertile base for observing changes in productivity under competition, has shown that competition has a positive impact on firm performance (Carlin et al. 2001; Carlin et al. 2004). Another study, using a longer time period and encompassing more firms, using antitrust policy actions as a measure of the intensity of competition law, also showed that in both the developed and developing worlds, competition law enforcement has a clearly beneficial impact on growth (Dutz and Hayri 2001).

**GOOD GOVERNANCE AND PREDICTABILITY IN BUSINESS AND ECONOMIC DEMOCRACY**

Competition law forms part of a cluster of regulatory activities that constitute good governance, as reflected in predictability and stability of government policies, the rule of law and so on. It is widely believed that investors (both domestic and foreign) are reassured by a stable regulatory environment in which they can be
assured that their assets will be protected by the local law in case of disputes.

Competition law plays a role in ensuring that market entry and exit will remain open and that an investor entering a new market for the first time will not be subject to abusive practices from other market players, including the government. Competition is often distorted through interference in the market by politicians engaging in cronyism or taking bribes in the awarding of contracts. For instance, in Nepal, the manufacturers of polythene pipes engaged in bid rigging claimed that they felt obliged to adopt bid-rigging practices because of the pressure from officials in the public sector to share rents from their contracts (Adhikari 2004). A study of CARICOM describes several instances of alleged cronyism and bribery in granting of contracts in Belize and other CARICOM countries (Stewart 2004).

The inclusion of competition provisions in RTAs contributes towards policy stability in this connection. National commitments are difficult to rescind because the reciprocal benefits offered by the partner country may likewise be withdrawn. A good example of the spread of governance measures through competition agreements in RTAs can be seen in the text of the Morocco-EU treaty. Morocco undertook to adopt certain regulatory policies and to harmonize standards between Morocco and the EU over a ten year period. Competition law enforcement, as the centerpiece of the entire regulatory package, is a central part of an ongoing dialogue with the EU. In addition, EU RTAs with the Palestinian Authority, Turkey, Tunisia, Jordan and South Africa all include various types of special and differential treatment for the less developed partner as do the European Free Trade Association's RTAs with Jordan and with the newly-acceded members of the European Community. These typically allow developing country a measure of flexibility and progressive adoption of competition legislation for a number of years (in the EU-Morocco treaty the transition period is ten years). During the transition period the more developed partner usually provides funding and training for the nascent competition regime to ensure that the competition law is fully understood by market actors, the judiciary and the staff of the authority.

The case study of Nepal (Adhikari 2004) also shows clearly that when there is no competition law or political will to protect competition in the market, there is regulatory capture, widespread cartelization, bid rigging, tied selling and predatory behaviour and consumers pay considerably more. For instance, in 1999, leading sugar industrialists in Nepal, in the face of stiff competition from imports from Brazil, succeeded in pressuring the government to raise the tariff on imported sugar to 40%, arguing for protection of the infant industry and claiming that they were able to supply market demand. They then allegedly withdrew supply from the market and succeeded in raising prices still further, in the absence of any competition from imports. Consumers were forced to pay 29 rupees per kg instead of 20 rupees, which would have been the landed price in Nepal for imported Brazilian sugar (including the tariff).

Let us turn now to the concept of economic democracy. The competition law of South Africa is notable in this connection. It contains a clause related to Black Economic Empowerment (BEE), which is a measure designed to assist in the redistribution of wealth. The concentration of wealth in the hands of a racially distinct elite during the years of apartheid rule had created inequalities in the ownership of capital, which the BEE is intended to partly rectify.

An example of inequality that the competition law and the BEE are designed to address was brought to light in an IDRC study undertaken in South Africa in 2002 (Chabane 2003). The South African economy under apartheid had operated under a dual structure in which the white population operated in a formal economy with a developed infrastructure, while the economic activity of the black population was predominantly informal and suffered from many structural deficiencies. On taking power in 1994, the African National Congress (ANC) government initiated a number of economic reforms that included a reassessment of South Africa’s competition challenges and the efficacy of the existing competition law in light of
the challenges of diluting the highly concentrated economic power. The law was therefore drafted to include reference to the encouragement of small and medium enterprises – viewed as a way of spreading economic wealth more broadly through the population – and “to promote a greater spread of ownership, in particular to increase the ownership stakes of historically disadvantaged persons.” (Government of South Africa: Competition Act, No.89, 1998).

In response to the law, companies have begun changing their ownership structure towards the ratios set out in various industry charters. A recent study on the effect of these charters upon three South African industries (Chabane 2003) revealed that BEE measures are indeed increasing the ownership of businesses to persons who were previously excluded from these sectors. Chabane analysed a case in which a merger between a large multinational company, Shell, and a local partner – a subsidiary of a black empowerment holding company - had been advocated before the Competition Tribunal as a means of promoting black empowerment. Scrutiny of the proposed merger led the investigating Competition Commission to opine that, although the merger would increase black ownership within the merged entity, the merger risked the disappearance from the market of an independent empowerment firm. Accordingly it recommended approval of the merger only on condition that the black-owned firm retain its independent status, under joint control of Shell and the black-owned holding company, and that the company’s line of branded products be maintained. However, the Tribunal disagreed with the Commission’s reasoning on the grounds that the smaller firm was failing and maintaining its separate identity and the existence of its brand was not viable. It approved the merger unconditionally arguing that BEE public interest objectives were best served in this way. As the years go by, the full potential of the South African competition law to broaden economic empowerment through wider asset ownership will be revealed.

**COMPETITION POLICY CONSIDERATIONS**

**Examples of benefits of market liberalization**

Developing countries are particularly concerned about unqualified application of liberalization policies. Some countries retain border barriers to specifically protect themselves from unfair trade practices such as agricultural subsidies in the US and Europe. Further, they use industrial policy as a tool for development to give support to sunrise industries, particularly in the Information and Communications technologies sector. However, IDRC funded studies have demonstrated cases where the domestic economy gained through application of wider competition policies, such as removal of border barriers.

A recent IDRC study, Ghoneim and Latif (2005) looked at the effect of market liberalization on the cement sector in Egypt. The authors describe changes in the market that took place after deregulation of the industry (i.e. the privatization of formerly state-owned enterprises and dismantling of barriers to entry in that sector). Up until 1999, the cement sector was government-controlled and the active firms, which operated far below capacity, were all state owned. Chronic undersupply forced the government to open the sector to private sector participation in the late 1990s. Foreign as well as local investors entered the sector.

Output in the sector grew immediately to meet domestic demand for cement: three new entrants alone provided almost 7.5 million additional tons of cement to the market. The new market entrants quickly adopted innovative distribution strategies and aggressive marketing techniques and took market share away from incumbents and rivals. More efficient methods of production generated a competitive advantage for others. The liberalization of the market therefore increased the production of cement without raising prices.

Increased private sector activity in the cement industry dramatically altered the industry: production increased and the efficiency of firms took a leap forward as each firm undertook innovative management techniques to gain a
foothold over market rivals. The productivity increases were so marked that domestic Egyptian cement suppliers soon had excess cement to offer on the international market. The low capital and labour costs in Egypt that had attracted foreign multinationals to invest in the cement sector also gave it a price advantage that enabled it to expand into markets abroad. In March 2000, when excess production of cement was driving Egyptian producers to look for export markets, the average price of Egyptian cement was US$35.5 – US$55.7 per ton. The world market price during the same period ranged between US$39 – US$110 per ton, giving the Egyptian producers a clear cost advantage and a geographical advantage in African, Middle Eastern and Spanish markets. Exports of cement from Egypt grew rapidly by between 61% - 320% across all cement producers between 2002 and 2003.

By contrast, where competition policies are not applied robustly in conjunction with liberalization, there have been smaller gains. In Morocco, membership of the WTO since 1995 has lead to the opening up of its domestic markets through the abolition of import restrictions and subsidies on the majority of products. In a paper examining the issue of whether competition and efficiency are linked in the Moroccan market, the authors set out to establish whether or not the lack of a well functioning domestic market may be due to the absence of effective competition. This question had previously been raised in the academic literature with respect to changes in Egypt, where liberalisation of the economy had transferred publicly monitored, state-owned sectors into sectors dominated by private rent seeking.

After controlling for various non-competition factors that might have impacted upon the productivity of the firms (such as a severe drought that affected the country during the years under examination), the authors, Lahcen Achy and Khalid Sekkat (2005) found markedly lower levels of output per worker in Morocco proportional to the degree of imperfect competition in the relevant market. Morocco has had a competition law since July 2000, but enforcement has been constrained. Interviews carried out by the authors confirm that there has been no effective implementation of the law’s provisions. The authors’ general conclusion is that low competitive pressure resulted in low levels of efficiency. Furthermore, the sectors in which the phenomenon was most pronounced – food, apparel and chemicals – are also the largest in shares of employment, which magnified the deadweight loss that accrued to Moroccan society as a result of these market imperfections. This shows one way in which the social welfare effects of low competitive pressure can manifest themselves. It was also found that factor productivity responded better to competition from foreign goods than to competition from domestic firms, though this is not always the case and should not be taken as a general rule. The implication is that sheltering domestic firms from foreign competition, i.e. conferring trade protection, was specifically damaging to industrial competitiveness in this case.

The structure of a domestic industry may naturally exclude foreign presence, thus allowing domestic cartels to form. For example, an IDRC study in Peru (Boza 2005) showed that the market for live poultry is not substitutable with the frozen imported poultry due to consumer tastes. In the 1990s, the domestic live poultry producers were able to take advantage of this fact to coordinate output and prices through local industry associations. This led to a long-running cartel in which domestic producers were able to extract unfairly high profits (meaning profits that would not have been achievable in an openly contested market) from consumers. Arguably, foreign entry to the poultry market would have undermined the organisation of the cartel and returned prices to a competitive equilibrium. Without the influence of foreign entry, the authority was forced to intervene and dismantle the cartel. This is an example of a situation in which cross-border market entry would have been beneficial for competition in the domestic economy.

**Caveats**

A major challenge faced by developing countries is to find the right mix between trade liberalization and protection from foreign competition. The Peruvian case study (Boza 2005, p. 10) states that
trade liberalization too frequently resulted in inefficient companies in the developing countries closing under pressure from more efficient international firms. While the elimination of inefficiency is economically a laudable goal, the projected transfer of resources from less productive uses to more productive uses did not occur due to a lack of capital and entrepreneurship. Thus, rather than creating new jobs, trade liberalization resulted in the destruction of many of the few jobs that existed.

The CARICOM study (Stewart 2004) revealed restrictive trade barriers for import of agricultural products into Belize, and pointed to the fact that Belize is almost self-sufficient in food with the agricultural sector generating more than 50% of employment in the economy. The barriers were justified because prices in Belize, while competitive under conditions of no market distortions, would not be able to withstand competition from subsidized agricultural products from the EU and the United States. Clearly then, the approach to liberalization in developing countries has to be nuanced to meet legitimate development goals.

3.2. HOW CAN COMPETITION LAW BE TAILORED TO MEET THE NEEDS OF A SPECIFIC ECONOMY?

For best effect, competition law should be drafted to respond to economic conditions in a particular country, rather than simply copied from elsewhere. Such conditions include market structure, extent of competition in important sectors of the economy, including entry barriers, and the most prevalent anticompetitive behaviour. For instance, in the Uzbekistan case cited earlier, the research funded by IDRC assisted the authority to identify a gap in the existing competition legislation and helped government legislators to modify financial laws relevant to this type of exploitation. This was a clear case of a government enacting competition legislation to suit its particular needs.

This approach provides flexibility in drafting the law and acknowledges the importance of efficiency as a goal of competition law, but also includes concepts of fairness and promotion of small and medium enterprises. Developing countries may also need to introduce and implement provisions progressively to ensure law enforcement obligations are consistent with institutional capacity. For instance, having per se prohibitions initially, which are easier to investigate and enforce, followed by abuse of dominance requiring rule of reason procedure, and finally, merger control regulation. Such an approach does not compromise the goal of drafting a strong law, but acknowledges that competition issues in economies at different levels of development manifest differently according to the incidence of market failures, and should be treated appropriately, but with equivalent rigor.

In international negotiations on commitments to introduce competition legislation, countries have sought various forms of special and differential treatment with respect to the implementation of competition legislation. These flexibilities have been justified on various grounds, such as the need to promote sectors or industries in the domestic economy, or particular needs due to economic size or geography. Submissions by member states in the WTO WGTCP on the need for flexible treatment are summarized in the Working Group’s report in the following way:

In developing an industrial strategy, a balance was needed to ensure that, on the one hand, enterprises could attain the size needed to be internationally competitive and, on the other hand, that they were subjected to appropriate competitive disciplines to ensure that they were not in a position to abuse their market power and, indeed, faced appropriate incentives for continual improvement of their productivity and performance.

[Progressive implementation periods] allowed a country to build a firm foundation for the competition regime by fully assimilating one aspect of competition rules before progressing to the next. To give an example of how progressivity could be put into practice, in the initial stage of the development of a competition regime, a small developing economy might do better to introduce only
measures against hard core cartels and blatant abuses of dominance or, possibly, not even the latter, in view of its complexity. (Annual Report of the WGTCP, 2001)

The recognition of the need to tailor competition law and policy to the needs of economies at different levels of development is these days seen most clearly in the exceptional provisions laid down in competition clauses of RTAs. An IDRC study by Brusick and Clarke (2005) has identified numerous examples of larger, developed countries making allowances for the needs of comparatively smaller developing nations. The text of the EU-Egypt RTA, for example, makes allowances for exemption of various state aids and state monopolies. The RTA signed between the EU and Estonia (prior to its accession to the EU) took into account the economic situation of the country in its (non)application of competition laws and policies. The Brusick and Clarke study identified flexibility of this type between Canada, the European Communities and the United States and less developed countries, most of which were designed to safeguard the economic interests of the less-developed partner by conferring allowances for transitional periods, structural adjustments and technical assistance, that is, special and differential treatment.

**Approach to Public Interest Considerations**

Of several countries that introduced special provisions into their laws to deal with specific features of their economies, South Africa is the most notable example. The preamble to the 1991 Competition Act expressly refers to the discriminatory harms of the former apartheid regime, and it specifies opening the country’s economy to ownership by a broader number of South Africans as a policy purpose. It asserts that a competitive economy balancing interests of workers, owners and consumers would foster development to the benefit of all South Africans. The Act sets out the orthodox aims of most competition laws: efficiency, adaptability and development of the economy. But it goes on to state other competition-law objectives that are unique to South Africa:

- To promote employment and advance the social and economic welfare of South Africans;
- To expand the opportunities for South African participation in world markets and to recognize the role of foreign competition in the Republic
- To ensure that small and medium-sized enterprises have an equitable opportunity to participate in the economy; and
- To promote a greater spread of ownership, in particular to increase the ownership stakes of historically disadvantaged persons.

The law specified that the Commission or Tribunal must consider, when evaluating a merger, the effect that the merger will have on a particular industrial sector or region; on employment; on the ability of small businesses, or firms controlled or owned by historically disadvantaged persons, to be competitive; and on the ability of national industries to compete in international markets. In order to do its work, the Commission or Tribunal may require input from those affected by public interest considerations.

There have been several cases where the public interest provision has been considered. One such case was described at the end of the previous section in which the Commission (the investigating and decision-making body in the first instance) had sought to impose conditions on mergers based on public interest, but the Tribunal (or appeal body) disagreed with the Commission’s reasoning, overturned its recommendation and approved the merger unconditionally. The reasonings used in arriving at the decisions are contributing to development of jurisprudence in this new area of law.

Chetty (2005) gives some examples of how the provision is being applied in practice. In the case of DB Investments SA v De Beers Consolidated Mines Ltd. (2001-2002), the merging parties responded to concerns expressed about employment with an undertaking that their conditions of employment would not change following the merger. In another case the public interest clause influenced the acts of the Minister of Finance in the Nedcor/Stanbic bank merger
case (2000). The Minister of Finance was to act after consultation with the Competition Authorities. The Minister refused to approve the merger on the basis of the Competition Commission’s recommendation that “the proposed transaction should be prohibited on the grounds that it will have significant social costs (primarily), potential abuse of market power in the retail banking market and potential job losses, which represents a net loss to society, which cannot be offset by any potential efficiency gains....” This case also illustrates how competition authorities can work effectively with other government departments. It also demonstrates that it is possible to embed non-economic aims such as Black Empowerment in a system that is primarily oriented to the promotion of competition, and indeed, that there need be relatively little tension generated by the need to achieve these two aims.

Other countries’ competition laws have also addressed issues specific to developing countries. IDRC research in Central America examined situations of exceptionally high levels of concentration of economic and political power, along with pronounced social inequality (Rivera and Schatan 2006). The provisions in the Mexican Competition Law allowing the government to fix prices on essential basic consumption goods are in part a response to this situation. In the Costa Rican law, the government retained the right to restrict import and export licenses for some products on the grounds of public interest, although the provision can only be used temporarily and must be reviewed every six months. In the Guatemalan draft law, it is proposed that the Competition Law should defer to any existing laws or regulations which aim to coordinate supply and promote exports, in order to deal with the existence of idle productive capacity and other social considerations.

Given the extent of market failure in some developing countries, it is politically desirable to have provisions that cater to public interest considerations. However, it is important that these be viewed as special measures contingent on previous market failures, to be reviewed as markets develop and the need for such provisions is lessened. There may be costs as well as benefits associated with their implementation, for instance inefficiencies may be encouraged which may become less warranted as markets develop over time.

**Dealing with Cooperation amongst Small Businesses**

A general problem faced by small economies is the difficulty of achieving minimum efficient scale (MES) because of the small size of the domestic market. One instance of this relates to small economies’ heavy dependence on imports for consumption, given limited production capability. Where there are already large businesses controlling the import trade, market entry becomes very difficult for small firms. Cooperation amongst small firms to import in bulk helps to achieve economies of scale and reduce prices and be able to better compete. To facilitate this, the United States Virgin Islands (USVI) Antimonopoly Law, Article 1505 specifically exempts

“… the establishment of formal agreements between small entrepreneurs engaged in the retail sale of the same or similar commodities for the purpose of bulk purchase of those commodities in order to meet in good faith, competition of businesses with substantially larger sales volumes.”

The law defines small entrepreneurs as merchants with gross receipts from all sources in any year not normally exceeding US$250,000, with not more than 12 employees. In other settings, different thresholds might be appropriate.

The IDRC CARICOM and Central America research projects showed that this same situation exists in these economies, particularly in the non-tradable sectors which are particularly susceptible to control by dominant groups who control the import and retail trade and bar entry to newcomers. The CARICOM study (Stewart 2004) highlighted the fact that one cannot rely on deregulated import markets to deliver free competition since the channels of import distribution can be monopolized or cartelized. In these small economies, distribution of wealth is
stratified along racial lines, and the dominant white group tightly controlled the import, wholesale and retail sectors; sole distributorships and interlocking directorates and family ties across companies are commonplace. Entry of other enterprises into these sectors had proven to be very difficult for the non-white population. Interestingly, the research revealed that there is great reluctance of local small black businesses to collaborate to import in bulk, pointing to a culture of business that is very individualistic.

In recent times, however, there has been erosion of that dominance in the import and retail sector through entry of small firms owned by newly arrived migrant families from Asian countries whose business culture is cooperative, and who come together within their ethnic circle, import in bulk to achieve economies of scale, and retail in their individual outlets, agreeing on the price to sell the products. They are underselling the incumbents and taking a significant share of the market. Having provisions in the law that facilitate the ending of historical patterns of dominance is absolutely necessary in small economies. It may be advisable for CARICOM countries to include in their law, specific mention of exemption for collaborative bulk buying by small entrepreneurs using the example of the USVI law (Stewart 2004).

**CIRCUMSTANCES WHERE FLEXIBILITY IS RECOMMENDED**

In some developing countries (as in rich ones), protecting and improving the wellbeing of indigenous peoples, racial communities and disenfranchised groups is an explicit policy objective. Competition law can help by making specific provision for these purposes. In societies where there is heavy concentration of wealth, there may be a need to protect the indigenous and disenfranchised groups. Such groups are also frequently racially distinct.

For instance, the CARICOM study examined the case of taxi drivers in St. Lucia, who are black, largely come from the lower income bracket, and support many dependants. Dominant white families already control the tourism management sector, and are keen to enhance their market power by also making inroads into the transportation sector (perhaps with a view to establishing market power in that sector as well). Clear inefficiencies within the taxi industry could be removed through introducing such competition, but this could lead to serious displacement of existing taxi drivers, and, given that racial divisions are also economic divisions, racial tensions and possibly violence could erupt.

In the circumstances, opening up the sector to full competition is not viable. There may be a need to apply a trade-off but with regular review of the exemption. The problem can be addressed in the law through exemption of the sector, possibly with the requirement to re-evaluate every six months, along with adoption of a set of requirements for improving efficiency in the sector. Another approach would be to include in the law prohibition of vertical integration in some sectors in order to ensure spaces for small entrepreneurs to enter the market, or to prevent dominant players from crowding out small entrepreneurs. The US Virgin Islands Anti-Monopoly Law also sets a precedent in this connection; it provides for such a prohibition in the import, wholesale and retail sectors.

**DISCIPLINING SMALL FIRMS WHERE NECESSARY**

On the other hand, the authority may need to censure small firms in remote areas where they may have a substantial share of a small local market, and therefore hold a dominant position in that market. The Peruvian Competition Authority, INDECOPI, tackled the problem in an innovative way which might bear replication elsewhere. It set up a number of local corresponding chapters under a franchise arrangement with universities and NGOs interested in competition issues. This enabled some apparently small scale, local cases to be pursued. One such case is described in detail in Section 3.4 (below). It relates to anticompetitive practices among small producers that were pervasive throughout the country, albeit in geographically separate markets. The findings were thus of national relevance. The adjudications of these competition cases could be disseminated.
throughout the country at sub-national authority level and lay the ground for compliance throughout the country.

**Relevance of Merger Control Regulation for Developing Countries**

Many developing countries assert that merger control regulation (MCR) is not appropriate for their economies. It is argued that firms cannot achieve international competitiveness without economies of scale and that in small economies this could require the creation of monopolies or substantial market power in the domestic market. Research suggests that this approach has to be nuanced and that the non-tradable services sector is particularly vulnerable to abuse of dominance. The case of Belize is instructive in this connection.

Belize has a very small population (less than 300,000) but a very large land mass (22,995 sq. km). Transport services are crucial. Until 2003, Belize’s main cross-country bus route had been served by seven companies. One company, Z Line, undercut its rivals by predatory pricing and other tactics, and then bought five of them outright. At this point, the only surviving competitor, Novelo, bought Z Line, monopolized control of the whole route and not long afterwards almost doubled fares. Travellers rioted. Merger-control regulation could have prevented this monopolization of an essential public service (Stewart 2004).

Those who argue against the need for merger control regulation based on the economies of scale argument do not take sufficiently into consideration that investigations by the authority require full “rule of reason” evaluations of proposed mergers, that is, the level of concentration that would result in the product and geographic markets, taking into consideration market contestability and efficiency enhancing objectives. It is therefore unlikely that mergers that would increase international competitiveness would be prohibited.

The other reason given for the inappropriateness of MCR in developing economies is that the technical expertise to evaluate merger cases is beyond the capacity of these countries. This argument has some merit. There is a need to find a balance between having merger control regulations and crafting them so that the staff of the authority has the discretion to intervene only where potential mergers could be very harmful to consumers and the economy, such as the case in Belize cited above. Careful consideration has to be given to whether notification should be required, given the burden this would place on staff of the Authority, or whether special provisions can be developed to deal with merger control regulation in a unique way.

In any event, the yardsticks used to evaluate proposed mergers in large economies should not be applied unthinkingly in other situations. In small economies it would be necessary to develop a set of relevant criteria, based on features of smallness and minimum economic scale considerations, rather than simply prohibiting a merger if competition is substantially reduced in the market. Michal Gal (2001) recommended that the threshold in terms of market share for merger notification should be set higher than in developed countries. But this ignores the problem of anticompetitive conduct in the non-tradable sector in developing countries: the offending firms can be relatively small in relation to others in the economy but they can have quite damaging effects. The CARICOM study (Stewart 2004) recommended pitching the threshold at a low enough level to capture the major local actors in the economy.

**Informal Production**

In many developing countries, the vast majority of productive entities in existence are informal (i.e. not part of the registered business sector, not paying tax and outside bureaucratic purview) and they often generate a significant portion of output in many sectors. The existence of the informal sector is sometimes partly attributed to the existence of regulations (including onerous bureaucratic procedures) or anticompetitive behaviour (including, for example, barriers to entry resting on lack of access to funding from formal financial institutions) which unnecessarily restrict competition. Gesner Oliveira (2006), in his
presentation, “Can competition help nations meet the Millennium Development Goals?” pointed to very high levels of informal production in several developing countries, with Peru being the highest at 60% of economic output, Uruguay at 50% and Nigeria at approximately 42%. It follows that moving toward more competition may actually reduce the size of the informal sector.

In Oliveira’s view, the existence of the informal sector has important implications for competition enforcement: it leads to dual markets in several sectors, the market power of dominant formal firms may be overestimated, cartel analysis becomes more difficult, and predatory pricing analysis becomes more complex. The informal sector’s contribution to the economy impacts on the level of competition in markets and impinges on decisions of even large firms. For instance, a practice of “fronting” has developed in the Caribbean whereby a large, formal firm hires vendors to peddle the firm’s goods outside the store on the pavement seemingly as part of the unregistered trade sector and to compete with the informal vendors. This strategy takes back market share from the informal traders. Market analysis is further complicated, according to the CARICOM study, because informal operators were able to undersell formal businesses by evading payment of duties on imports (with assistance from corrupt custom officers) and taxes on profits. This “unfair” competition has to be addressed through bureaucratic reform and introduction of good governance measures, rather than through competition enforcement (Stewart 2004).

An even greater problem in the region is that the drug trade has infiltrated the informal sector. It is alleged that businesses are established, particularly in the retail sector, such as car parts supplies in Trinidad, as a strategy to launder money, and they undersell bona fide businesses. Theories of competition do not address situations where markets are impervious to regulation because competition enforcers are at risk for their lives if they try to investigate such cases.

**Exceptions and Exemptions**

Another way in which competition law provisions have been crafted to meet the specific needs of economies is through use of exceptions and exemptions to the law. Almost all competition laws, both in developed and developing countries, contain some exceptions and exemptions. For instance, the EU provides *de jure* exemption for agriculture. Exceptions may be written into the law itself or the authority may have the power to exempt firms on a case-specific basis. This explains the difference between “exceptions” included in the law and “exemptions” granted by administrative authorities.

In the case of Thailand, state-owned enterprises (SOEs) are exempt from the competition law. The analysis provided in an IDRC study shows that this has not been beneficial, because of the extent to which SOEs pursue anticompetitive practices. However, SOEs were exempted in that case because the newly established competition authority did not have the technical expertise to deal with SOE cases (Nikomborirak 2004, pp.91-109). The provision could have been made temporary and linked to capacity building. This recalls the concept of progressivity, meaning that a country progressively introduces a commitment based on capacity to implement, which is now broadly accepted in the international trade field.

Morocco allows for exemptions at the discretion of the competition authority when their purpose is to improve small to mid-sized enterprises’ (SMEs’) management or the marketing by farmers of their products, providing such practices produce a “net public benefit” and the burden of proof falls on firms (Achy and Sekkat 2005). The Jordanian competition law exempts agreements with minor importance (where market share of firms does not exceed 10 percent) provided that they do not involve price fixing or market sharing agreements. The competition authority can exercise its discretion to serve the public interest and attain outcomes such as improving the competitiveness of enterprises, improving production and distribution processes and providing benefits to consumers (Saif and Barakat 2005).
There are instances where the rationale for providing exemptions may not be clear, or may simply be a function of developing countries copying examples from the regimes in industrialized countries. For instance, Jamaica exempts agreements related to intellectual property. Yet, there is little or no innovation requiring conferring of industrial property rights on locals, and there is ample historical evidence of firms using monopoly power derived from intellectual property rights to create barriers to entry by other or to divide up markets geographically (Stewart 2000).

In many cases, exemptions have been used politically to protect large vested interests, rather than being based on sound economic reasoning.

As a general rule, it makes good policy to fence in exceptions and exemptions with conditions. They should be openly arrived at (to prevent secret favours); they should be subject to scheduled periodic review; and they should reflect the best available knowledge of the market sector and the economy. Applied pragmatically and with care, exceptions and exemptions can indeed contribute to the tailoring of competition law to a country’s specific needs. Criteria for exemptions from competition law could include instances where consumers are adversely affected or where small producers, such as agricultural cooperatives, are exempted because of efficiency gains.

3.3. WHAT ARE THE CHALLENGES TO LEGISLATING AND IMPLEMENTING COMPETITION LAW?

The process of introducing and implementing competition law is fraught with problems. Drafting the bill and getting it through the congress or parliament has to overcome opposition by powerful businesses that gain rents through engaging in anticompetitive conducts. They will seek to undermine the effectiveness of the legislation by having provisions that are perceived to be against their interests removed from the draft bill and lobbying for inclusion of exceptions and exemptions to protect their interests. The natural allies of governments in the process of introducing and enforcing competition law are the small and medium enterprises that are adversely affected by exercise of market power or collusion, and consumer groups who would benefit from enforcement of competition law. Firms purchase inputs from other firms. If these markets are uncompetitive, then firms suffer as well from higher input prices, and so are less able to compete in international markets. So firms themselves are potentially allies – but as buyers, not as sellers. This is clearly important for goods producers and services providers in many developing countries. However, these stakeholders are generally ill-informed about the law and how it serves their interests.

The prospective impact of a new competition regime has a similar pattern to that of trade liberalization and it gives rise to the same political economy problem. Those opposed to the new measures, because they may lose from their implementation, are far fewer and are far better organized than the large number each of whom stands to gain in small measure. Michal Gal (2004), in her chapter, “The Ecology of Antitrust: Preconditions for Competition Law Enforcement in Developing Countries, points out that in most developing countries consumer groups are very weak or non-existent, and that society is riddled with corruption and lack of transparency and burdened by excessive bureaucracy and inadequate judicial systems. The IDRC funded Central American study notes the existence of weak institutions in that region, susceptible to abuse and serviced by deficient judicial mechanisms. Gal sets out a very useful framework for understanding these challenges. In this section her framework is utilized and case examples from IDRC funded studies are used to demonstrate how competition authorities are managing these challenges.
**COMPLEMENTARY IDEOLOGICAL ENVIRONMENT NEEDED**

According to Gal, the level of acceptance of competition law is determined by the societal-ideological environment into which the law is being introduced. There needs to be acceptance by all spheres of government that development strategies are underpinned by market principles. Gal pointed out that countries like Israel, Argentina, Brazil, South Africa and others had competition laws for many years, but they were weak early versions that were not effectively enforced. It was only when market reform was undertaken that the competition law was revised and implemented successfully. In brief, there must be political will to introduce competition.

Other countries had draft laws for decades without being able to legislate. For instance, in Korea, as Joseph Seon Hur (2004) shows, proposals to legislate the Fair Trade Act were submitted to parliament in 1966, 1969 and 1971, with criticisms of monopoly issues; each time efforts were thwarted because of protests from the industries that felt threatened. The concentration of economic power in chaebols, ineffective over-investment, and protection of the heavy and chemical industries eventually led to economic stagnation. The government, determined to adopt a market economy, instituted changes by liberalizing the economy, opening markets and legislating the “Monopoly Regulation and Fair Trade Act” in 1981.

Similarly, efforts had been underway in El Salvador (1993, 1996 and 1997) to introduce competition law, but resistance from the business sector prevailed. It was only when economic stagnation made it necessary to change economic strategy that consensus was finally obtained to introduce competition legislation in 2004. Honduras had a similar experience, initiating efforts to draft a law in 1994, but not getting it passed in Congress until 2005. In Guatemala, there is little interest in competition law. Domestic markets are highly concentrated with monopolies and oligopolies and some powerful businessmen occupy high levels in government. This is now changing, and a competition law is under discussion, because Guatemala is the only country in the region still without a law, making it extremely vulnerable to becoming the regional seat of collusive behaviour. In India, political will has been galvanised and business opinion has swung in favour of a new, stronger competition law as a way of improving export competitiveness.

**REGULATORY CAPTURE**

There is always the danger of regulatory capture by vested interests seeking to undermine the effectiveness of the legislation by, among other strategies, lobbying to dilute the law or actions of the authority in their favour. The drafters of the competition bill must be wary of pressures that may be brought to bear to weaken the provisions. In Central America and Mexico, notably in Honduras, the draft laws included restrictions in scope, relatively soft sanctions, many exclusions and exemptions, and other forms of limitation on the powers of the competition authorities. Such limitations may reflect and/or promote regulatory capture.

Regulatory capture can also explain the weak application of the law and non-compliance with legal rulings. For instance, in Panama, only 10% of fines levied have been paid since the establishment of the current competition regime, and in Mexico only 14% of fines have been paid since 1994. Attempts are underway to correct these limitations through reforms of the laws in Mexico, Costa Rica and Panama, including the removal of many exclusions and exemptions. However, in Panama, the review of the legislation has brought some loss of powers to the Commissioner (Rivera and Schatan 2006, p. 18). This is a retrograde step. It is important that the authority is independent from routine control by politicians, although it is unrealistic to believe that it could or should ever be fully independent of government.

Lack of political will in enforcing the law is also a problem. In the case of Morocco, the IDRC supported MENA study (Achy and Sekkat 2005, pp. 65-66) revealed that there has been no effective implementation of the Competition Law. Staff of...
the authority have received a number of complaints (secretly) but have taken no concrete action. A Competition Council with an advisory role has been established, with a retired former Minister as its President, but it lacks human and financial resources and expertise and has met only two or three times over the last three years. The researcher concludes that this reveals a very low degree of government commitment towards effective liberalization of the economy.

All of the relevant studies sponsored by IDRC indicate that the mere existence of a competition law is not enough to ensure the existence of a competitive environment. The law needs to be part of an overall competition policy that fits into an overall development strategy.

**Securing the Legitimacy of the Competition Authority**

A competition authority needs to attain legitimacy, that is, have public support for its regulatory activities. The IDRC sponsored study in Peru (Boza 2005, pp. 14-19) emphasizes the importance of this point. Gal also argues that the level of deterrence which the competition law enforcement inspires depends on market players’ awareness of the objectives and scope of the law. Therefore, there is a need to design and implement efficient mechanisms for disseminating information about the competition law and its enforcement. The authority must issue guidelines and notices on interpretations of the law and how the law is applied.

Gal also stressed that there must be transparency in administrative procedures and regulations, stakeholders must have the right to appear before the enforcing body, and the authority must publish its fully reasoned decisions. This is particularly so because the general public may find it difficult to understand the appropriateness of competition decisions, which can be highly technical. Transparency measures, including public consultation, increase accountability. There must be consistency in its application of the law and due process must prevail (p. 41), that is, procedures that are fair/equitable, accessible, open and consistent in treatment. Due process also involves the right for firms accused of acting anticompetitively to have a hearing before the authority or courts.

The good reputation of the authority also requires overcoming some other impediments. Caution has to be exercised in devising accountability mechanisms since the supervisory body may have lower expertise than that of the authority (as the Peruvian study pointed out). The concept of peer review as exercised by the OECD and UNCTAD is one way of obtaining an evaluation of performance and recommendations for reform from impartial experts.

**Training of Judges needed**

One obstacle is the lack of competition law skills in the judiciary, and particularly amongst judges. Judging a competition case requires some training in economic analysis, which judges usually lack. The quality of judgments in review of decisions of the authority affects the legitimacy of the authority. Jordan’s Competition Law provides for one or more specialized judges to preside over competition cases, and to be appointed by a decision of the Judicial Board (Saif and Barakat 2004, p. 44). This is a good strategy as it allows for training of selected judges in competition principles. Major efforts to train judges have been made in Costa Rica but some decisions continue to be inconsistent with competition principles. Jamaica has had similar experiences of inconsistency.

**Strong Leadership needed**

It is important also that the authority lives up to its title and commands authority in the public’s eye. A key determinant is the personality of the authority’s director who should be strong, fearless in pursuing the goals of the authority and very active. IDRC case studies suggest that some Directors were instrumental in putting the competition regime on a sound footing through his/her sheer determination to bring the work of the authority into the public eye and create respect (and fear from businesses). Such examples are George Lipimile in Zambia, David Lewis in South Africa, and Allan Fels in Australia. All were able to
give the authority a very high profile. Fels in an interview with the Australian Broadcasting Corporation (2002) said, “The role of the ACCC is to apply the Trade Practices Act without fear or favour to whomever it applies to, big or small”. He emphasized the importance of aggressive outreach to the community, “In this organisation we're in show business... show business first, law enforcement second.” An independent press is a great advantage in this respect. The media in Zambia followed George Lipimile so closely that his travels out of the country were reported in the press and a special column was given over to competition issues in a major newspaper.

To ensure that the authority is seen as impartial, and to avoid political interference, the Director should be appointed by a non-political process, and his or her term of office should not be linked to the tenure of the government in power. Similar criteria inform the appointments of Governors of Central Banks and other such institutions.

**Prosecutorial discretion needed**

In order to gain a reputation for effectiveness, and to win credibility with the private sector and consumers, new Competition Authorities should exercise prosecutorial discretion. They must choose cases to investigate and prosecute that have public appeal, that is, that impact on the average consumer's pocket, can be easily understood, and can be easily won. A comparison of Jamaica’s experience with that of Peru illustrates the importance of this point.

In Jamaica, the Commission chose as its first case a challenge to the Bar Association, claiming that the Canons of Professional Ethics, including restrictions on advertising and fixing of fees, were inconsistent with the Fair Competition Act. The issue got wide publicity but the Commission lost the case on the grounds that the General Council of the Bar Association and the professional ethics that govern the legal profession were not subject to the Fair Competition Act (Stewart 2004). By contrast, Peru chose as its first major case investigation of price fixing carried out in 1993 by three associations of public transport enterprises that operate in metropolitan Lima and, as its second major case, a wheat cartel whose activity had a direct impact on the price of bread. By targeting a service and a product important to the masses of the people, INDECOPI hit the headlines and came across as champion of the consumer (Boza 2005).

The Peru study proposes that a competition authority should follow an explicit enforcement pyramid strategy: from persuasion, to warning letters, to more drastic measures such as fines or license revocation. A two-pronged strategy is best: to explain the law and try and induce its observation, which is less costly than prosecution, and to select cases for prosecution which will clearly display the authority’s concerns about rule breaking and demonstrate its powers. Gal (2004, p. 40) offers two other possible criteria for choosing a case: that the enforcement cost is less than the harm caused, or that the likely deterrence effects would prevent cases of a similar degree of harm.

**INSTITUTION BUILDING**

The authority needs adequate human and financial resources, must have legal enforcement tools, and must be able to apply appropriate sanctions.

**Adequate Human Resources**

Competition law enforcement requires both legal and economic expertise, so the staff must have lawyers trained in competition law, and economists, preferably with training in industrial organization. Moreover, Gal suggests that there must be attorneys with litigation experience and sound knowledge of administrative law and civil procedure, reaffirming Kovacic’s observation that the authority might be required to convince the courts that cases are procedurally sound and substantively meritorious (Kovacic 1997). Yet, attracting high quality staff is very difficult.

In most developing countries, particularly ones where competition law is newly introduced, there are very few professionals with knowledge of competition law. Young authorities take in staff and train them, but are plagued by high turnover and loss of staff to the private sector or abroad, as
happened in Jamaica and some countries in Latin America. The CARICOM study suggests that scholarships and other training should be tied to a minimum number of years of service to the government (Stewart 2004, p. 210). Good salaries should be offered. High status for the authority within government helps in staff retention.

To avoid being limited by the salary structure in the civil service, the authority could possibly be granted special status with independent terms and conditions of employment. This strategy was employed by INDECOPI with the result that jobs in that institution were viewed as prestigious and therefore desirable to young professionals. IDRC considers this to be an important issue. To motivate and support the profile of staff, IDRC has initiated a high-profile project that gives research funds to competition authorities in developing countries. This increases the staff’s research skills, challenges them with new projects and gives them international exposure. The expectation from this project is that staff turnover will be reduced and that they will become more expert in the competition issues relevant to their economies.

Other devices are to retain outside counsel, funds permitting, in important cases, and/or ask for assistance in an investigation. For example, in the wheat cartel case in 1995, INDECOPI formed an ad hoc investigatory task force and drew in personnel from other institutions. The Ministry of Economy and Finance seconded economists to INDECOPI for the duration of the investigation.

Methods for training staff include sending staff on internships to more mature authorities, in-house training, and asking more mature authorities to second staff to their authorities. Technical assistance is offered by International Financial Institutions, UNCTAD, USAID, and other donors. In more recent years, the USDOJ and FTC have begun to assist, seconding staff to young competition authorities in Eastern Europe and South Africa among other countries, to train investigators. Provision of competition courses at local universities is important; international faculty can be brought in most easily to participate in modular courses. Young competition authorities also need to build institutional memory through careful record-keeping of cases and approaches to investigation.

One of the reasons put forward by developing countries for not adopting a competition law is the cost of maintaining an authority dedicated to routing out conspiracies and prosecuting them. The expense of such an authority may seem high, especially in developing countries where government budgets are devoted to the provision of essential resources and where policy makers may hesitate about allocating scarce funds to an authority. Indeed, several authors (for example, Hoekman and Mavroidis 2002) have made pointed reference to the unsuitability of prioritising funds for an authority in the context of pressing development needs.

During the negotiations for a multilateral competition framework, several delegations raised the same point. Developing countries cited expense as a major reason for not adopting such a regime.

Concern was also expressed that, regardless of whether competition law was enforced through administrative decisions or judicially, it could entail enormous costs and difficult institutional adjustments, especially for developing countries in the early stages of implementing a law.² (WTO 2003)

² M/22, paragraph 113, see also M/21, paragraph 114.
Clarke and Evenett (2003) examined the cost of running an authority and compared it to the overcharges from just one cartel - the vitamins cartel. The results (see table) showed that the deterrent effect of an authority would have saved enough to pay the costs of three competition authorities in Colombia or six competition authorities in Mexico – the expense of an authority is likely to be recouped several times over. More recent studies support this conclusion (for example, Connor and Bolotova, 2006).

### Adequate and Independent Financial Resources

Without adequate financial resources, an authority is unable to function effectively. The operational revenue needs also to be independent of politicians or Ministries, so that they are not able to sway decisions or control activities of the authority. In El Salvador, Panama and Honduras, the authority develops its own budget and submits it to Congress. That puts those authorities in a strong position. Some laws allow the authority to fund itself through retention of fines, but this is generally considered inadvisable. The authority may either be tempted to fine excessively in order to increase its funds or - just as damaging to its credibility - the public perception may be that the authority is behaving in this way.

### Legal Enforcement Tools

The case of Jamaica illustrates the importance of ensuring that the draft law adheres to general legal principles, such as separating out the investigative and adjudicative responsibilities of the competition authority. The Fair Competition Act erroneously gave investigative and adjudicative responsibilities to the Commissioners, whereas these responsibilities should be separate. The FTC was taken to court for breach of natural justice and lost the case and the appeal. The process of revising the law has been drawn out. The Commission has been crippled because it could not pursue any cases until this breach of general legal principles was corrected (Stewart 2004).

The Costa Rican experience also illustrates flaws in the legislation that hindered the operation of the authority. In that law, only business persons (natural or legal) competing among themselves are recognised as constituting a cartel. In fact, business chambers and associations are in many cases instrumental in the formation of and execution of cartels, but they cannot be prosecuted (Sittenfeld 2007).

The law must provide the authority with broad investigative powers, such as the power to initiate an investigation, to request information from any public or private business person, and the legal right to enter into business premises to collect information and seize documents (known as dawn raids). Without these powers the authority is severely handicapped. In CARICOM, the Community Commission cannot initiate an investigation on its own initiative, but only at the request of a member state or the regional body, the Council for Trade and Economic Development. This provision handicapped the Commission from the outset. It reflects the unwillingness of member states to relinquish power to a supranational body (Stewart 2004).

The Costa Rican law does not grant the Authority the right to enter premises. This has severely hampered its ability to obtain vital information on cartel activities (Sittenfeld, 2007). As Sittenfeld points out, in the early stages of the life of a competition regime, it is relatively easy to get information. Cartels carry on past practice, publicly announcing their agreement in the newspaper or recording the decision in the minutes

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**Costs and Benefits of Anti-Cartel Laws**

Cartelized vitamins import overcharges versus authority costs

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<tr>
<td>Zambia</td>
<td>0.01</td>
<td>0.13</td>
<td>5.9%</td>
<td>CUTS (2002)</td>
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<td>Tanzania</td>
<td>0.02</td>
<td>0.07</td>
<td>29.5%</td>
<td>CUTS (2002)</td>
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<tr>
<td>Peru</td>
<td>6.62</td>
<td>10.05</td>
<td>65.9%</td>
<td>Authority’s web page</td>
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<td>Kenya</td>
<td>0.18</td>
<td>0.26</td>
<td>70.9%</td>
<td>CUTS (2002)</td>
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<tr>
<td>South Africa</td>
<td>9.91</td>
<td>8.76</td>
<td>113.1%</td>
<td>Authority’s web page</td>
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<tr>
<td>Columbia</td>
<td>16.50</td>
<td>5.47</td>
<td>302.0%</td>
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<td>Mexico</td>
<td>58.27</td>
<td>9.70</td>
<td>600.8%</td>
<td>Hahn &amp; Layne-Farrar (2002)</td>
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<tr>
<td>Venezuela</td>
<td>12.13</td>
<td>1.36</td>
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<td>Argentina</td>
<td>23.94</td>
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<td>1710.3%</td>
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<td>Brazil</td>
<td>63.13</td>
<td>1.15</td>
<td>5499.6%</td>
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[1] Reduction in vitamin overcharges due to anti-cartel law (average annual, 1990s)

[2] Annual cost of running the nation’s competition authority (not just their anti-cartel law). Data refers to latest year available, always 1999 or later

Clarke and Evenett (2003)
of the business association, not realizing the illegality of the agreement. With time, they become more educated on competition law and cover up their agreements much more effectively. Strong investigative powers for the authority then become indispensable. It may be necessary to include heavy sanctions for non-cooperation in investigations in the law, so that MNEs will supply information to young and weak competition authorities. According to George Lipimile, Zambia experienced such difficulty in getting information from Coca Cola in its investigation of the company’s subsidiary located in Zambia that the government had to pass legislation that imposed a jail sentence on CEOs of companies for non-cooperation in an investigation, after which Coca Cola relented and cooperated in the investigation (Stewart 2004).

In this regard, the Costa Rican study recommends that it is advisable for a young authority to tackle cases involving agreements that are per se prohibited. Under this rule the action is sanctionable so long as the authority can prove that an agreement has taken place, regardless of whether that agreement has caused damage or not. The alternative “rule of reason” procedure requires the authority to gather substantial amounts of information and prepare complex analysis of product and geographic markets to show that the agreement has adversely affected other agents in the economy.

An authority needs, however, to be careful when applying the per se rule, that there be a sole, reasonable explanation of why the agreement has been deemed illegal. In Costa Rica, investigation into the actions of a number of airlines supposedly using their monopsony power to reduce fees paid to travel agents was aborted by the Commission because information surfaced that the lead airline in the market had publicized its reduction of agents’ commissions months before, opening up the possibility that other airlines had simply ‘followed the leader’ rather than conspired actively to fix the fee rate (Sittenfeld 2007).

**SANCTIONS**

An important tool for achieving compliance is the perception that fines are sufficiently high to make it unattractive for firms to engage in anticompetitive conduct. Perceptions depend on both the level of fines and the real payment rate. In several countries including Peru, Mexico, Panama and Costa Rica, the competition law has been revised to increase sanctions. These fines must be large enough to act as a deterrent for all firms including large MNEs that are resident in most developing countries.

Many countries have moved from setting fines as a fixed sum to setting them as a percentage of the yearly turnover rates (usually 10 percent) or of actual or potential profit from the anticompetitive conduct. Research suggests that this has not always been successful. In Costa Rica, the legal sanction, which set an absolute rate of 10 percent of sales or assets, was considered inappropriate because a fine at that level could bankrupt small firms. This may be the case if the ability to finance such a fine was disproportional to the size of the firm measured in sales or assets. It has been argued the law should have been worded to allow the authority either to impose a fine up to 10 percent of sales or assets, or allow use of a range of fines (Sittenfeld 2007) but such discretion could breed corruption or political pressures. There is a trade-off here. But if there is confidence that the authority can withstand the temptations and political influences, the evidence from Costa Rica suggests that such flexibility could be useful.

Interestingly in El Salvador, fines can be imposed, but if the company cooperates with the authority in eliminating the anticompetitive behaviour, the sanction will be removed. The rationale for this is that it is very difficult to get the evidence to prove cases, and cooperation would achieve the same objective. Mexico has introduced the same provision in its revised law (Rivera and Schatan 2006, p. 19).
3.4. HOW AND WHY ARE STAKEHOLDERS INVOLVED IN THE IMPLEMENTATION PROCESS?

This section explores the ways in which competition authorities in developing countries have addressed the challenge identified previously: the fact that parties opposed to competition measures are more organized and more politically active than those who will gain from the application of a strong competition regime. The answer lies in purposeful relationship-building with the main groups and bodies that stand to be affected – either positively or negatively – by enforcement of the law, or that could contribute to the authority’s operations. These groups are all “stakeholders” in the work of authority. They include businesses and business associations in the private sector; government ministries and agencies; mass and special-interest media; consumer organizations, labour unions, farmer groups and other non-governmental organizations, and academics and researchers. But an even larger group of important stakeholders lies behind them: all those citizens who do not identify themselves as members of any interest group, but whose lives will be affected (and improved) by competition law, even if they do not know it. Competition authorities need to keep the totality of this audience in mind and devise an engagement strategy accordingly.

These stakeholders will change depending upon the constituencies that gain or lose from particular actions of the authority. People who support competition policy when it reduces the prices of things they buy may be violently opposed to the same rules when they reduce the prices of things they sell. Governments are more likely to support the actions of the authority when it accords with their legislative agenda, and not when the authority calls that agenda into question. And the same people can be on one side, then the other on consecutive days. The subtle task of the authority is in engaging those stakeholders who are likely to support the envisaged changes from case to case.

Engaging stakeholders is also of course germane to the prior phase of formulation of the legal instrument. Preparing the draft legislation in a consultative fashion lays the ground for successful implementation in due course. Once the law is passed, stakeholder engagement has three main purposes for the authority (see box). Substantial work on the last two fronts is necessary to build the credibility of the authority.

There is an inevitable and important political dimension to stakeholder engagement. Once the

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**STAKEHOLDER ENGAGEMENT**

**Main Purposes**

- A consultative process needs to be in effect for periodic reviews of the efficacy of the law, taking into account both scope and content of the law and interpretation of the principles governing its application. A standing consultative committee should be struck to address this function.
- The actions of stakeholders can effectively augment the operational resources at its disposal.
- The authority has to win stakeholders as cooperative partners to secure its own position as defender of competition principles and enforcer of the law.

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authority begins to enforce the law, it can become extremely vulnerable. Businesses that feel themselves threatened will take more care to conceal anticompetitive acts (which puts greater demands on the authority’s resources) and will seek to discredit and undermine the authority to nip in the bud any prospect of it becoming a heavyweight arbiter. Beyond that, the precise objectives of relationship-building require that parties be identified case by case, to address the overlap between the interests of the authority and the other party involved.

The goal of establishing good relations with private sector representatives and the business community is to maximise voluntary compliance with the
competition law on the part of those who could be the subject of enforcement actions.

Civil society organizations of all kinds and the media can assist the authority in notifying and investigating complaints, but only if they understand the principles, functions and scope of application of competition law.

Other government departments and bodies are potential allies of the authority, but some may also be potentially hostile. The objective of engagement in these cases is to establish effective collaborative working relationships on competition issues, recognising that, while the authority is the enforcing institution for the most explicit instrument of competition law, it is by no means the only – and may not be the most senior – institution involved. This is particularly the case with other regulatory bodies such as the Financial Regulator, the Utilities Commission and the Securities Commission. The authority is always, however, the appropriate institution to take the lead in the articulation of competition principles, and in discussion of their application to the work of different government bodies. This mapping of mandates and activities related to competition can express, and be a contribution to the delineation of the government’s competition regime. In the case of other regulatory bodies, it is advisable that this delineation of responsibilities is explicit in the legislation, as are mechanisms for cooperation and consultation. There have been several cases of bitter struggles between the competition authority and regulatory authorities over jurisdiction, as in South Africa with the Financial Regulator over a bank merger.

In any event, for each type of stakeholder engagement - as in any type of relationship-building - the competition authority needs to think through what it can offer to the other party in terms of that party’s own mandate and objectives. This approach can significantly help diffuse potential tensions and differences with the particular interlocutor.

Nevertheless, common cause is very difficult to build with stakeholders without a general understanding in the society of the nature of the law and recognition of its benefits. But the level of public awareness can be extremely weak. Interviews with businessmen and government officials in 22 COMESA member states in Africa in 2002 showed that there was a general lack of knowledge and understanding of competition law and policy. Many were undecided whether their governments should divert resources from other scarce priorities to introduce competition law in their country. In some of the countries, citizens were not convinced that lack of competition law in the region constituted an economic problem worthy of their respective government’s attention (Lipimile 2004, p. 175). The IDRC study of Central American countries similarly makes clear that the absence of industry associations and NGOs is symptomatic of a low background level of public awareness of the issues. In such circumstances, competition authorities also need to find ways of enhancing the culture of competition in order to create the basis for the acceptability of their work.

**HOW TO INVOLVE STAKEHOLDERS IN THE IMPLEMENTATION PROCESS**

We now draw out lessons for engagement with particular stakeholders in developing countries based on experiences described in IDRC studies. The Peruvian study (Boza 2005) recommends a gradualist approach that focuses attention on the organization and activities associated with implementation in order to provide a framework for changing the perceptions of the players.

**The Private Sector**

The level of deterrence inspired by competition law depends on market actors’ awareness of the objectives, scope and enforceability of the law. Information about the competition law and its enforcement needs to be widely disseminated. Participation by authority staff in seminars and conference on competition and economic performance is important. Press releases and conferences on new rulings are useful. In Peru, INDECOPI publicised legal rulings and the reasonings that informed them so as to explain the law and deter anticompetitive acts. By entering into mediation with offending companies rather than proceeding immediately to court, INDECOPI was
able to disseminate its message about competitive conduct to key players.

The authority can dialogue with the private sector at two levels: with businesses which can, through their conduct, have a substantial effect on the market, and with small and medium enterprises which, along with consumers, are often victims of anticompetitive conduct.

The authority must explain the law to businesses, particularly big businesses, and thereby demystify its provisions and bring comfort to the market players. With large businesses, the authority can explain that the law encapsulates the new “rules of the game” and point out that it is a mistake to see competition law as just another piece of troublesome regulation. There will be resistance from businesses if the law is perceived only to increase competition against their products. The authority can draw upon experiences of other countries to show that adherence to the provisions of competition law can also be beneficial in supporting competition for supplying their inputs – companies are consumers too! This can lead to improved company level productivity, innovation and ability to compete in international markets. Enforcement of the law facilitates firm entry into new sectors and so holds promise of new opportunities for business investors. And it can remind domestic firms that competition law enforcement imposes equal disciplines on foreign-owned corporations that could otherwise dominate the domestic market.

To a small business audience, discussion could emphasise that complaints against anticompetitive acts can be brought to the authority for investigation and relief. Large firms can abuse their position at various points in the value chain. When acting as a buyer, they can impose low prices upon those firms they buy products from. When acting as a supplier, they can withhold supplies to small businesses, thus forcing up the price, or oblige these firms to buy more of their output than desired. They may try to dictate the price charged on their goods to the final customer. Research has revealed many instances of such behaviour. Nevertheless, the authority must also convey the fact that it is alert to, and prepared to act as necessary, against anticompetitive behaviour within the small business sector itself.

### Relations with other governmental bodies

At the policy level, the relevant officials of all government branches and agencies need to understand why competition law needs to be central in drafting other laws, and certainly in the conduct of other government operations, such as privatization. In constitutional terms, however, other national regulatory agencies and ministries of state usually have the same standing as the competition authority, or higher. Even if the authority believes that the economic logic underlying its mandate is of general scope and fundamental importance, and that actions of other agencies of the state sometimes flatly contradict the competition law, its authority to advance its views is, in a governance perspective, tightly circumscribed (Wilson 2006). To avoid accusations of meddling and threats of withdrawal of its powers, the authority should consider initiating tactical alliance-building discussions with other government bodies in sectors and on issues where the introduction of greater competition would contribute to the other body’s professed objectives. It should initiate confrontations only where there is evidence of egregious anticompetitive conduct, especially where they can be demonstrated to be harmful to the other institution’s own policy objectives.

There are in fact many situations in which interactions with other branches of government may benefit the authority. First, it is always good strategy to seek out and make alliances with any part of government with overlapping or parallel interests. Some procurement officers, for example, might suspect or detect bid-rigging and share the authority’s interest in stopping such practices (others might not be keen to have the authority involved for obvious reasons). Government auditors and others responsible for tracking and enforcing the probity of government expenditures may be even more likely to wish to engage the skills and support of the authority in their work. They will have expertise and knowledge of particular market sectors that could be helpful. Cooperation with like-minded departments often
begins with information-sharing about market situations and investigative methods (Sittenfeld 2007, p. 11).

A competition authority is particularly well positioned to influence policy in markets that deal with new and fast-changing technologies. Telecommunications are a prime example. The early adoption of competition principles in telecoms regulation has shown startling value in many developing economies – yielding value in widely accessible service, lower prices and newer, better products. This result is familiar from the literature and is supported unambiguously in IDRC-supported research across Africa, the Americas and Asia.

Let us turn now to the larger number of situations where the authority’s relationship with other government bodies is at least potentially on a collision course.

In these situations the authority may first need to persuade other government institutions of its competence, particularly where it challenges activities that have been accepted in the past. Before Peru’s competition authority, INDECOPI, launched its wheat cartel case in 1995, the society was used to political intervention to control prices. INDECOPI met with the political directorate and economic advisors on both sides of the ideological divide to discuss the complaint, explain the provision of the law that made the action illegal, and to explain that the market requires an autonomous technical institution to act as referee (i.e. INDECOPI) to guarantee the correct functioning of its rules. After that, it was possible for it to investigate the case and come to a decision without political interference (Boza 2005, pp. 36-37). As the cartel proposed to raise wheat prices, this argument was not politically difficult to win. In other circumstances, the authority has a harder task in explaining that low, controlled prices are not necessarily “fair” prices, e.g. that a low price may be predatory, and would be followed by a price hike.

Municipal and other lower level authorities are especially prone to regulatory capture in local markets that are isolated from the rest of the economy by poor communications and difficulties of terrain. Such situations are common in developing countries, many of which are geographically large and thinly populated. As a national institution, the authority may be able to intervene and carry strong weight in the local context. The national competition authority in Peru, INDECOPI, after many legal struggles, managed to set competitive standards for regulation of local taxi transport. It was able to gather evidence for the case because it had established local offices in secondary cities in cooperation with local NGOs and academic institutions. Cases like these are small in economic terms, but can set a national precedent. They may also naturally lead into discussions with the relevant line ministry – Transport in this case – with beneficial results. The situation here is different from the case of the taxi drivers in St Lucia discussed above (page 23) for two reasons: firstly, the challenge in St Lucia is not of regulating the taxi service sector, but opening it up to competition. The sector is already regulated. Secondly, the case study in St Lucia was of taxis that catered entirely to the tourist trade, not locals. The tourist industry is very fragile, being notoriously sensitive to any kind of social conflict in the tourist destination.

Finally, last but certainly not least, arguably the most important relationships that the authority must build within government are with the ministries of trade and industry. The policy-making and regulatory mandates of these departments have a strong influence on business behaviour and the structure of markets. Nevertheless, competition considerations are not usually made explicit within the mandate of either ministry. This is a weakness which can undermine attainment of a country’s development goals and be in direct conflict with the authority’s own operations. However, IDRC research suggests that respecting competition principles will often assist these departments’ ability to address their own professed objectives. This provides the basis for constructive engagement.

In principle, the interests and mandates of the trade ministry and the competition authority are complementary. The general issue is that, where
trade barriers are reduced as a matter of public policy, anticompetitive practices in the domestic market can restrain trade and prevent price reductions from cheaper imports reaching the domestic market. Exploitative and exclusionary practices in the transportation and goods distribution sectors are common bottlenecks. Competition law enforcement thus helps to ensure that the gains of trade are distributed as expected among personal and business consumers of imported products.

However different dynamics can arise. A case in Costa Rica provides an example. In this episode, several domestic manufacturers of wooden pallets widely used to transport goods jointly asked the trade minister to increase the tariff against imported pallets — promising in exchange to maintain an agreed maximum price of $9.50 a unit. The ministry obliged by raising the tariff by 10 percent. A Costa Rican pallet importer promptly complained to the Competition Commission, which found that the agreement to fix prices was illegal. The Commission did not concern itself with whether the Minister acted within his powers in raising the tariff. But it expressly said the Ministry should not use its own powers to facilitate action proscribed by the (competition) law. As it happens, Costa Rica’s trade ministry controls the Competition Commission’s budget; by demonstrating its independence in defence of principle, the Commission greatly enhanced its credibility.

Notwithstanding its mandate to advance competition in markets, Competition Authorities need to adopt a balanced approach in dealing with trade ministries on the issue of trade liberalization, taking into account market failures both at the national and international levels, referred to in the caveats in Section 3.1 above. This requires discerning instances where protection may be needed as opposed to those where inefficiencies need to be weeded out through increased competition from imports.

Different issues arise in the services sector. In this sector, liberalization of trade is not primarily concerned with levels of import taxes. Instead, it reduces to easier terms for foreign investment into the financial, business services, transportation and other such industries. Since the authority’s principal role here is to prevent anticompetitive conduct in the market (including by incoming firms), thus ensuring that domestic competition is enhanced, synergies with the Trade Ministry’s activities is obvious. However, in most developing countries, governments have been discriminating in investment policy for many decades by providing foreign investors with economic advantages such as tax holidays, exemptions from paying duties, site allocations etc., that are not offered to local investors. The treatment of investors should not be on a discriminatory basis under competition law. This may provide an effective vehicle for domestic investors to lodge a complaint of unfair discrimination (Lipimile 2004, p. 180).

Another dimension of the interface between foreign investment and competition is that some investors may be discouraged if there is active competition law enforcement. However, the likelihood is that those investments would not be beneficial for the country, because such foreign investors would have been counting on monopoly rents being extracted from local consumers.

In respect of ministries of industry, interaction with the authority opens up a wide canvas involving privatization and industrial policies.

Privatizations in developing countries were often initiated as part of Structural Adjustment Programmes preceding the introduction of competition law. This resulted in the transfer of state monopolies to private monopolies. The lack of foresight on the part of the International Financial Institutions in failing to see that these two policies are complementary and synergistic undermined their value for economic development, according to Lipimile (2004, p. 177). He notes that it is the degree of competition, not ownership that determines economic performance. The onus on the authority to discipline the conduct of a newly created private monopoly is technically and politically demanding and, where the monopoly concerned falls under supervision of a sectoral regulator, it may not even be authorized to act. It is preferable that privatization policy
clearly specify that the modes of sale chosen should ensure that private monopolies are not created. He recommends that privatization authorities should be obliged to consult with the competition authority on the competitive position of the market when selling a state owned company, and/or there should be a provision to compel it to take into account competition considerations.

In contrast, there is widespread belief that competition law is in open contradiction to policies designed to support local industry. Industrial policy serves many objectives. Its salience is increasing as globalization advances. Governments may look to industrial policy to reduce disruptions to business and employment from shocks associated with integrating the national economy into international markets. In COMESA countries, for instance, it is generally felt that local industries are not strong enough to withstand competition from incoming foreign companies (Lipimile 2004, p. 176). The Peruvian and CARICOM studies expressed the same concern. Widespread de-industrialization in Africa in the wake of trade liberalization in the 1980s and 1990s is also often mentioned. Industrial policy advocates sometimes argue that a necessary component of support packages is that the normal rules on collusive behaviour among (domestic) companies need to be relaxed, or that dominant (domestic) firms should be allowed to emerge, in order that local industry can withstand competition from imports, resist the market power of foreign enterprises and attain economies of scale sufficient to invest and expand into international markets. These are politically tempting claims.

It helps to recall that the fundamental professed goals of industrial policy are to facilitate and sustain productivity increases at firm and sector level and, by extension, to see improved export performance by domestic industry. Research indicates that industrial policies – tax measures, training assistance, R&D support and the like – are consistent with competition law when they apply horizontally (within sectors). These initiatives are accessible to any firm, without discrimination.

But there is another category of interventions - sector-specific, vertical supports – that tend to work against competition by singling out firms for special treatment. These are not only discriminatory but have a poor record of success, particularly in cases where sunset industries are favoured, as opposed to sunrise industries. The failures come at taxpayers’ expense. Safe from competition and comforted by subsidy, protected firms tend, in all countries, to fail at sizeable cost the public treasury. These experiences have been vividly described by the Korean government, in its submissions to the WGTCP, as well as by Michael Porter in several studies, amongst many other authors. But composite policies are possible. The East Asian countries, usually seen as exemplars, frequently combined sectoral measures with mechanisms to maintain competition in the relevant markets, e.g. firms had to compete among themselves for access to subsidised finance.

Politicians in smaller countries sometimes put forward an additional argument for seeking exemption from competition law or limiting the provisions in the law to exclude merger control regulation. They suggest that some firms should be allowed to grow large enough to compete with foreign firms in domestic markets or internationally as “national champions”, even if that gives them a dominant position in the domestic market. In response, competition advocates can point to the universally observed slackness of innovation and poor record of cost-cutting by monopolies, alongside their exploitation of consumers. The studies of Jordan and Morocco cited above (pages 15 and 19) showed that firms economically underperform when local markets are less competitive. Consumers should not pay to support a national champion, especially since there is no mechanism by which they may realise any return from its subsequent success (if any) in foreign markets. In general, it is not clear why a firm that can grow only with special exemption from normal competition rules, and not through superior performance, can ever be expected to be able to compete in international markets (Geroski 2005). Shielding firms from the discipline of competition law at home prepares them for failure abroad.

“Rule of reason” analysis under competition law in merger cases, as noted above, identifies whether
markets are contestable, that is, a firm will be exposed to competition or the threat of competition in the market, which may be domestic or international. Local dominance is certainly not proscribed in principle. When a firm is permitted to attain a locally dominant position, on the grounds that it is active in the international arena, then the law does however require that it must not abuse that dominance in the domestic market.

In general, therefore, enforcement of competition law should not be curtailed when industrial policies are implemented. It is helpful to recall that competition law can be applied simultaneously with border barriers, so there should be no confusion between trade liberalization policies and competition law provisions. Hence, national champions may be protected from foreign entry through trade rules, and still be subjected to the discipline of competition law. Competition law enforcement is a proven mechanism for encouraging the emergence of strong firms. It facilitates the entry of new firms, some of which may prove exceptionally efficient and profitable, encourages failing, low productivity ones to leave the market and, by disciplining monopolistic behaviour, encourages innovation. The best firms will be revealed by gaining market share without recourse to anticompetitive conduct. Having earned champion status in this way they should not be permitted to abuse their dominating position in their home market.

Educating the media is as important as using it as a communications outlet. The media can not only raise the level of public knowledge about the value of a strong competition law but its reporting of successful cases enhances the credibility of the authority. It is a watchdog capable of sniffing out anticompetitive activity. In all competition regimes, the authority routinely scrutinizes media outputs for clues on possible anticompetitive conduct, particularly cartel activity. Sometimes a Trade Association announces an agreement on price, or a CEO of a company may, in a speech, “innocently” refer to horizontal collaboration with competitors. These kinds of reports are followed up where there are grounds for suspicion and may eventually lead to the opening of an investigation by the authority.

In general, therefore, enforcement of competition law should not be curtailed when industrial policies are implemented. It is helpful to recall that competition law can be applied simultaneously with border barriers, so there should be no confusion between trade liberalization policies and competition law provisions. Hence, national champions may be protected from foreign entry through trade rules, and still be subjected to the discipline of competition law. Competition law enforcement is a proven mechanism for encouraging the emergence of strong firms. It facilitates the entry of new firms, some of which may prove exceptionally efficient and profitable, encourages failing, low productivity ones to leave the market and, by disciplining monopolistic behaviour, encourages innovation. The best firms will be revealed by gaining market share without recourse to anticompetitive conduct. Having earned champion status in this way they should not be permitted to abuse their dominating position in their home market.

Investigative journalists should be given feedback on the value of the material they provide and instructed on necessary standards of evidence. TV footage provided INDECOPI in Peru with compelling evidence to support its arguments in a consumer case, demonstrating that racial discrimination was the sole reason why some consumers were refused entry to nightclubs in Lima. It has to be acknowledged, though, that INDECOPI was able to intervene in this case because its mandate includes consumer protection. Where there is a separate consumer protection agency, the competition authority might need to be sensitive to the consumer agency’s established position and role.

A large database of allegations of anticompetitive practice reported in the media in Sub Saharan African countries was the basis for a presentation at an IDRC supported seminar (Evnett 2006). Analysis of these allegations revealed many interesting features. Allegations covered all sectors and all countries of the region and comprised a very broad range of anticompetitive acts, clearly demonstrating the need for robust competition regimes across countries of all sizes, development orientation, economic structures and level of development. The large majority of allegations of damaging practices related to domestic, not foreign firms.
For all these reasons, competition authorities advance their work when they make themselves open to the media, inform reporters of their rulings, and encourage journalistic interest in their objectives and activities.

**Consumer Organizations and NGOs**

Other allies of the authority are consumer organizations and non governmental organizations (NGOs), the latter being very important if there are no consumer organizations. These organizations can represent the “person in the street” and can be the ears and eyes for the authority on concerted price hikes or anticompetitive behaviour of dominant firms. Consumer Unity and Trust Society (CUTS) of India, perhaps the best known NGO active internationally in the competition field, was founded to give voice to consumer complaints, but quickly saw the relevance of competition law. The Peruvian competition authority, INDECOPI, is constituted somewhat unusually with multiple responsibilities to implement both the consumer protection and the competition (and intellectual property) laws. It used these powers astutely to gain enormous public support and credibility for the institution from its consumer protection activities, which spilled over to its competition work. Other authorities without a consumer policy enforcement mandate have to make allies of free-standing consumer organizations.

Even without a competition law in place, consumer mobilization can have an effect. In 2001, consumers in Belize showed their strength in dramatic fashion, forcing a dominant firm to retreat from abusive conduct. In December 2001, Belize Telecommunications Ltd. (BTL) raised tariffs to major public outcry. BTL’s response was that the increased charges were being used to cover the cost of purchasing the GSM system (US$60 million) that had been installed. Consumers were outraged at having to pay the full cost of this system up-front, without any signal that the price would be reduced after the GSM system had been paid for, allowing the company to reap unfairly high profits in the long-run (taking a short-term loss against almost certain long-term gains). An association was formed and obtained signatures of some 65 percent of the population petitioning the government to take action. The government then drew up a Statutory Instrument to stop the new rates (which was appealed in the courts but upheld) (Stewart 2004, p. 162). In 2002, possibly as a result of the action taken by consumers, a Telecommunications Act was passed that empowered the regulatory authority to regulate rates, protect consumer interests and oversee the orderly development of the sector. The foundation is laid for introduction of a stronger competition law regime in that country.

**The research community**

Last but not least, academics and research analysts can be a valuable ally to the authority.

IDRC’s mandate and perforce its interest in the competition field is premised on the belief that research-based evidence is an essential input to the policy process. Economic theory yields fairly strong predictions about the damages caused by anticompetitive practices and, conversely, the benefits of competitive markets. Such claims are by now well supported in the context of developed market economies. But they require specific and rigorous empirical investigation in developing country settings where markets are less well developed and fundamental and comprehensive economic reforms are underway. Without scientifically sound, local validation of the fundamental tenets of competition law enforcement, not only is the credibility of the whole effort at risk, but its purpose and potential to contribute to developmental goals can be held up to question. Research is needed more specifically to estimate the scale of the problem, identify the specific effects of market concentration, to categorize and quantify the impacts of anticompetitive practices, and to push forward accurate and locally appropriate techniques of market analysis and other aspects of investigations and enforcement.

The research community comprises a number of players in most countries, including university faculties, independent or state sponsored research institutes, sometimes local or international non governmental organizations, local or international
consulting firms with expertise in development policy matters, and, of course, relevant parts of the public sector, notably the authority itself. Competition authorities have much to gain from research studies by any competent party which yield relevant empirical material and evidence-based analysis. Governments can use their influence with donors to request that resources be provided to support research into competition and other economic policy matters, whether as a free standing item, e.g. within a technical assistance agreement, or as part of the activity plan for general budgetary support. Competition authorities themselves, either on their own or in conjunction with a local research institution, can apply for research support from a new competition research facility implemented by IDRC. This started in 2005 as a project giving grants to selected proposals on Competition Issues in the Distribution Sector. Competition authorities from eight countries, Argentina, Armenia, Costa Rica, Jamaica, Malawi, Peru, Uzbekistan and Zambia, were awarded grants on the basis of open, competitive responses to a Call for Proposals assessed by a scientific committee of experts. In a new phase of the project from July 2007, the facility will be widened to consider proposals into any aspect of competition in the distribution, transport and construction sectors as well as regulatory obstacles to competition in any sector. The academic community can and should be encouraged to contribute to knowledge of competition matters by carrying out research activity. But its educative function is also highly valuable. It can increase technical expertise in the country by including courses on competition law in the economics and law syllabuses at Universities. Inputs from and the support of the authority are needed for this be done well. Research studies develop knowledge by refining the theoretical understanding and empirical knowledge of the relationship between competitive markets, economic performance and producer and consumer benefits in the country concerned. Direct collaboration between the authority and research institutes adds to in-house resources for analytical work and helps keep staff up to date on the ever-expanding literature and new analytical techniques developed elsewhere.

In practical terms, and in relation to the operational challenges of implementation, researchers and academics also have an important part to play. They help build interest in the issues at a well-informed level. The principal researcher on an IDRC-supported project in Jordan put the knowledge of competition law he gained through the research project to good effect after the study was completed. With colleagues, he formed an NGO, the Jordan Competition Association, to organise public meetings with other stakeholders (notably the private sector), make submissions to political bodies, and prepare material on competition for the media. An authority benefits strongly from this sort of activity, which relieves its own staff of a major task. Coming from an independent source, it is also impartial and may thus be able to facilitate more open discussion. Furthermore, activities of this kind can encourage critical assessment of the authority’s activities, in response to which it can improve its procedures and operational methods.
3.5. HOW CAN COMPETITION AUTHORITIES DEAL WITH CROSS-BORDER ANTICOMPETITIVE CONDUCT?

Markets have become increasingly open to foreign entry since the inception of the WTO in 1995. Consumers have benefited in terms of greater variety, better quality and lower cost of products available to them. But the situation has also been exploited by foreign firms seeking to dominate markets in developing countries. This manifests itself in a number of ways. First, several studies have shown that MNEs are able to organise an anticompetitive conspiracy in one location that takes effect in another. For example, an MNE may use a neighbouring country to plot a cartel involving other multinationals, which imposes itself upon consumers in the country next door.

Investigations by the United States Department of Justice (USDOJ) in the late-1990s uncovered a string of high profile international cartels of this kind. These cartels challenged existing thinking in a number of ways. First, many of them had been long-lived and had not collapsed under their own incentive structures as economic theory had predicted. Furthermore, they were well organised, internally well-documented and stretched across national boundaries. The conspirators planned their output and divided markets amongst themselves in jurisdictions in which competition law enforcement was lax or nonexistent. They seemed deliberately to extract the most economic rent from jurisdictions in which competition law was weakly enforced, notably developing countries. Their startling nature was revealed in a paper by Clarke and Evenett (2003). The authors analysed a vitamins cartel that had operated for some time under the guidance of executives of multinational vitamin producers in the United States and Europe. It was uncovered in the late 1990s and incurred fines from both the USDOJ and the European Commission. At the time, these were the largest monetary penalties ever levied on firms.

Cartels particularly victimise those countries without competition legislation, or in which competition legislation is weakly enforced. Clarke and Evenett (2003) illuminated this aspect of cartels by focusing on the relationship between the enforcement of competition legislation and a country’s vulnerability to cartel overcharges. The paper looked at the vitamins cartel, vitamins being vital inputs into livestock feed, medicines and food products. The authors determined that the value of vitamins exports from those countries in which the conspiracy had originated to destinations in Asia, Western Europe and Latin America rose more in those countries that did not have competition legislation or in which competition legislation was weakly enforced than in other countries. Given that the demand for vitamins is inelastic, the only conclusion to be drawn from this result was that effective competition legislation and enforcement was a deterrent for the cartel and resulted in less exploitation of national markets. This conclusion is broadly in line with those of Connor and Bolotova (2006), Levenstein and Suslow (2002) and the theory of punitive deterrence originally developed by Landes (1983).

The publicity emanating from this and other high-profile cases encouraged competition authorities in developing countries to research the activities of subsidiaries of MNEs located within their own jurisdictions. Many cartels were revealed. The well-documented nature of these conspiracies should, in principle, have allowed the local competition authorities to prosecute the local conspirators. However, the relevant documents were normally located outside the local jurisdiction, and the low level of cooperation between competition authorities and restrictions on sharing information due to confidentiality laws meant that few cross-border legal processes were successful.

MNEs may also use their large size relative to most developing country markets to carry out exploitative and exclusionary practices in those locations. This scenario frequently plays itself out in the retail sector, where a large foreign retailer will enter the market, displacing a large number of ‘mom and pop’ stores, and impose conditions upon the purchase of inputs or products from
upstream suppliers. The enormous size of the retailer enables it to lower the prices paid to its suppliers, perhaps below the competitive rate that would have existed in an open and competitive market, without fear of reprisal because of its position as the main purchaser in the market.

Findings from the following IDRC supported research studies have yielded evidence of many of these problems, some of which are presented below.

**Foreign cartels**

In Costa Rica, for instance, ten airlines (some international, some regional) announced that they were halving commissions to Costa Rican travel agents, to six percent from twelve percent. Costa Rican authorities opened a case against the airlines and in due course won partial victories against some of them. But investigating and prosecuting international cartels calls for domestic capacity and cross-border cooperation between governments (an element missing in this Costa Rican example) as will be seen below.

The CARICOM study cites the example of the control exercised by International Tour Operators that dominate the tourism industry in developing countries. They manage, through their monopsonistic buyer power over their suppliers to force hotels, restaurants and local tour operators in destination countries to provide their services at drastically reduced prices (Stewart 2004).

**Large foreign entrant**

The image of the powerful multinational retailer crowding out local competition is readily recognized, but it is far from unique. The case of remittance agencies in Uzbekistan, mentioned in Section 3.1, showed how Western Union was able as a “first mover” to enter a market and create its own network of local outlets for its international money-transfer business. Its dominance allowed it to charge uncompetitively high commission rates for money transferred into Uzbekistan, whose cost was borne by Uzbeks relying on those remittances from relatives working abroad. Moreover, Uzbekistan’s weak legal infrastructure was unsuited in the first instance to deal with competition issues in the foreign money remittances sector and also impeded its ability to cooperate with neighbouring jurisdictions. International cooperation requires adequate domestic policy capacity to secure success.

**Market entry through mergers**

Besides foreign-based cartels and foreign-owned dominant firms, mergers represent a third channel whereby cross-border anticompetitive activity may be realised. Here again, a foreign firm gains local dominance, this time by merging with a local business. Regulating mergers is a central part of a comprehensive competition law regime. But deciding whether to approve a merger, or to attach conditions to any approval, raises complex issues.

The more closed an economy is from the disciplines of international trade, the more likely a merger will exact social and economic costs. In an open economy, however, a merger might carry fewer risks and lower costs. When the South African competition authority assessed the merger of two domestic steel companies (a case described above), it concluded that economies of scale, volume-based price discounts and better capacity utilization outweighed any anticompetitive effects. A key factor was South Africa’s openness to international competition. The potential entry of foreign companies would be enough, it was judged, to deter abuses by the merged firms.

**Jurisdiction issues**

The key problem for the competition authority is that its power is geographically limited to the country in which it is situated. In practical terms, this means that the authority may experience difficulty finding persons and documents required for the prosecution of the anticompetitive practices being undertaken by foreign operating in its markets.

In an IDRC-supported seminar in Turkey, Tekdemir (2005) described the complications arising from cross-border anticompetitive practices. He referred to a cartel that had been formed in the market for seized (pieced) coal and described the difficulties faced by the Turkish
Competition Authority (TCA) in prosecuting foreign members of this cartel.

According to Tekdemir, the TCA’s investigation was prompted by complaints from consumers that the price of seized coal had undergone sharp price increases. The investigation revealed that these price increases were the result of price-fixing by several companies, two of which were headquartered overseas – one in Switzerland and the other in Austria. While prosecutions of the domestic companies resulted in fines being imposed on them, the internationally headquartered companies remained out of reach of Turkish justice. Despite the fact that one of the undertakings was found guilty, the TCA could not impose a fine as the procedure envisaged in the competition law was not completed properly.

The reasons for this failure are illuminating. The Swiss company had no office in Turkey. The Austrian company closed its local office when the investigation began. As a consequence, the Turkish authority had to resort to diplomacy to lay its hands on the evidence – only to meet still more frustrations. Members of Turkey’s own diplomatic service were unfamiliar with competition questions, did not fully understand the case or its significance, and were reluctant to invest their energies in the prosecution. Additionally, the governments of Switzerland and Austria gave Turkey only token assistance in pursuing their own nationals. In all, the case illuminated the jurisdictional obstacles, and the need for intergovernmental collaboration, in the prosecution of cross-border competition cases.

While the major concerns of developing countries are the cross border effects of anticompetitive conduct of MNEs, there is, conversely, concern that domestic firms would hinder their entrance into local markets by engaging in anticompetitive conduct, as for instance, denial of access to distribution networks or denial of access to essential facilities (e.g. network interconnection agreements in telecommunications). This is the major reason that some developed countries, particularly the EU, were pressing for a competition regime in the WTO. The concern was that even though tariffs would be lowered as a result of the Doha Round of Negotiations, market access benefits might be negated by domestic industries colluding or exercising monopoly power to bar entry of foreign goods and investment.

**The Need for Cooperation**

Competition authorities in developing countries do currently have various means at their disposal for tackling the problem of international anticompetitive practices but none is fully effective. One approach would be to strengthen competition cooperation agreements in RTAs. Another is to initiate and enlarge informal cooperation between authorities facing similar abuses or being targeted by the same companies. A third approach is for partner countries to adopt “positive comity” provisions that allow transgressions of competition law carried out in one jurisdiction to be prosecuted in another; but these are rare and limited to industrialized countries.

In Uzbekistan, for instance, competition law has played a role in creating regulatory linkages with neighbouring countries. Close examination of the potential welfare benefits of fuller application of the competition law led the Uzbek government to enter discussion of cross-border issues with other competition authorities in the region as a means to harmonization of treatment of particular sectors.

Intergovernmental collaboration can be limited to the sharing of competition-law information, experience and advice, in what is known as soft cooperation. Hard cooperation is something more: real enforcement by competition authorities working together to investigate, disrupt and punish anticompetitive behaviour. It usually entails the exchange of data and information about actual cases, the conduct of dawn raids and so on. However, developing countries’ experience is that industrialized countries are not willing to extend deep cooperation modalities to their competition authorities.

The Turkish coal case demonstrated what can happen when cooperation fails to operate. Turkish officials believed they had the legal machinery for
cooperation in place. Their government had a free trade agreement with the European Free Trade Association, which includes Switzerland; the trade agreement includes explicit competition provisions. But the Swiss refused to help, arguing that Swiss law did not cover the matter. Austria likewise refused meaningful cooperation, notwithstanding EU law that Turkey believed should have been applied to the case by the Austrian authorities. Austrian officials contended that the EU law did not require the action requested by Turkey, and that domestic legal obligations to safeguard business confidentiality would be breached if information was shared between the EU and Turkish competition authorities. Most competition laws explicitly authorize the authority to take action only if there is harm to domestic consumers. Therefore, if harm is caused in another country by a multinational company, the government of the home country of the MNE is under no legal obligation to take any action.

This case confirms three general propositions. First, a small or developing country can face challenges getting practical cooperation from the authorities in developed countries. Second, developed country governments may seek to protect their own MNEs against competition investigations and prosecutions launched by outsiders. Third, even full cooperation between authorities will not be fruitful if the national legislation does not require the authority to collaborate in investigations into harms caused by firms located within its territory that cause harm abroad, rather than to its own citizens.

Costa Rica’s prosecution of the airlines, noted above, also pointed to the difficulty of prosecution when evidence lies outside the prosecutor’s jurisdiction. It meant that the Costa Rican competition authority had to fall back on circumstantial evidence of collusion. This left the authority with a weaker case; as proceedings continued, rulings against some of the airlines were reversed. Equally unsatisfying was the later discovery that Panamanian officials had been prosecuting the same airlines for the same offences—neither government knowing of the other’s parallel action. As Sittenfeld (2007) argued, the case demonstrates that developing countries’ competition authorities should cooperate with each other, not just with those of industrialized countries.

Regional bodies offer some solution to the cooperation problem. In the Andean Community, the competition laws adopted by the regional body are applicable in both Bolivia and Ecuador. In the case of anticompetitive practices occurring in either jurisdiction, the regional law would provide a basis for cooperation between the two jurisdictions. A similar arrangement could, in future, facilitate the prosecution of anticompetitive acts in the Common Market for East and Southern Africa (COMESA), where it has been proposed that if a COMESA member does not have a competition law, the regional law would have domestic effect. In CARICOM, a regional competition law has been accepted as part of the undertaking of the Single Market, and is being put into effect, with a Community Competition Commission being established to deal with cross-border issues. The law requires that Member states cooperate with each other and with the Community Commission on competition cases.

More generally, however, competition authorities try to overcome obstacles to cooperation by including competition provisions in RTAs signed between governments. Alvarez et al (2005) discussed the results of this cooperation in an IDRC-funded book published through UNCTAD. Alvarez and other authors find that cooperation could be enhanced by competition provisions in RTAs but that impediments to good cooperation remained from the fact that competition provisions in RTAs tended to be written by trade negotiators rather than the competition authorities themselves. A more direct means of strengthening cooperation between competition authorities is through agency-to-agency agreements (ATAs) such as the one signed between the US and Brazil.

Supplementary cooperation agreements of this kind may lead to a relationship extending beyond the explicit clauses contained in the RTA. Cooperation between Zambia and South Africa is an example. Respondents to a questionnaire reported in the UNCTAD study (Lipimile 2004)
gave several interesting insights into exchanges of information between the two authorities. For example, a Zambian respondent noted that his bilateral arrangement with South Africa was the starting point for deeper recognition of anticompetitive behaviour taking place in each other’s jurisdiction, which has since led to successful prosecutions. Information and assessment reports are now routinely exchanged between the two authorities. But for Argentina and Brazil the competition provisions of MERCOSUR were insufficient to the needs of each authority, which frustrated the authorities in each country so much that they initiated an agency-to-agency agreement (ATA) to facilitate cooperation and information exchange. In both the latter examples, the competition provision in the RTA was the stepping off point for more useful forms of cooperation.

Young competition authorities have reported, however, that the most effective cooperation they have received is through informal cooperation (Stewart 2004). Thus, getting to know individuals in mature agencies, and building relationships and trust, is the most important course of action for a young authority in its bid to deepen cooperation with other agencies. Therefore, senior staff should attend conferences such as the International Competition Network annual conference in order to get such exposure.
PART 4: RECOMMENDATIONS

The introduction of a competition law and its implementation is fraught with problems and requires that the government undertake carefully planned strategic processes. Both require political will and adroit strategies. Political will is necessary every step of the way, from the conception of a coherent competition policy to the design and execution of a competition law. Competition law will not be broadly accepted or fully enforced unless key leaders in government have adopted market principles as the underpinning of economic development—and as the foundation of the government’s economic policy. This does not preclude a nuanced approach.

The following ten recommendations, experience-tested in many developing countries, suggest practical strategies for introducing a competition law and carrying out its provisions for best effect. The recommendations are grouped in three clusters, addressing in turn the challenges of drafting the statute and setting up the competition authority, engaging public support, and contending with anticompetitive conduct that cross national borders. Taken together, they represent a pragmatic and proven design for success.

4.1. DRAFTING AND IMPLEMENTING COMPETITION LAW

4.1.1 Draft and enact strong law – respectful of legal principles, enforceable and flexible.

Successful execution of competition policy starts with a competition law that is soundly drafted, and well crafted for effective enforcement. To the maximum extent possible, the law must be armoured against capture by interests hostile to its basic purpose of preventing and punishing abuses of market power. In particular, governments and legislators must resist pleas for special exclusions from the law’s coverage. Any exceptions or exemptions granted to industries or firms must be based on solid economic justification. They should be openly decided. And they must be regularly scrutinized afterward with an expectation that they will be terminated. The OECD/APEC checklist of regulatory reform\(^3\) states,

“When exclusions from competition law exist, they need to be narrowly targeted and no broader than necessary to achieve other legitimate public policy objectives that cannot be better served in other ways.”

It is important, also, that developing countries ensure that the provisions of the draft law are appropriate for addressing the specific conditions in their economies by applying the principles of flexibility and progressivity when developing their competition regimes. This may require special provisions to address serious market failures leading to social injustices that may require government intervention to protect the poor, or it may require the government to protect particular sectors from open competition or exclude small and medium enterprises from the application of the law. Or, the government may want to progressively introduce the law giving the young authority the capacity to strengthen the law over time.

As well, any competition law must possess three elements as listed in the box overleaf.

COMPETITION LAW IN ACTION: EXPERIENCES FROM DEVELOPING COUNTRIES

Elements of an Effective Competition Law

The competition law must:

Adhere to widely accepted legal principles. It will otherwise run a much higher risk of failure when it is challenged in court. The law must at minimum meet a country’s constitutional requirements and conventional standards of natural justice.

Expressly endow the competition authority with sufficient powers of investigation, including powers of search and seizure. In particular, the authority must be empowered to undertake investigations on its own initiative, independently and without need of any other institution’s authorization. These powers of investigation should extend as well to regional competition authorities established by intergovernmental agreements. To ensure that decisions of the Authority are subject to review, the law must provide for an appeal process.

Allow the authority the flexibility and scope to set fines and other penalties, and make other orders, to punish breaches of the law. Assuming corruption and political interference can be negated, the authority should have and exercise the discretion to calibrate fines according to the size of the firms involved—making them high enough to function as effective deterrents, but not so high as to unintentionally bankrupt violators. It is recommended that, rather than fines in fixed sums, the fines should be based on a percentage of the company’s annual turnover, with a range up to ten percent.

In most cases, countries that are introducing competition law do not have the expertise to vet the draft law to ensure that it meets the above criteria. It is advisable to have draft laws scrutinized by experts from more mature regimes. This can be done at no cost through technical assistance or informal cooperation.

While these criteria represent an appropriate law enforcement regime, the reality is that the government may encounter resistance and hostility both within the government and from the private sector. It is necessary, therefore, that those responsible for developing and advancing the competition regime be aware of the types of problems and hurdles that could be encountered and strategize to pre-empt them through skillful coalition formation with allies and effective advocacy.

Where achieving the appropriate regime is not possible all at once, and concessions have to be granted in order to get the process moving, then provision should be made to ensure that those concessions are temporary and subject to review. While Central American states encountered major problems with political cronyism and opposition from powerful groups, and gave many concessions, they are now, a few years later, able to revise their laws to strengthen the provisions. Also, a progressive approach may allow a competition regime to be introduced in a limited way. With time and the implementation of a sound advocacy programme, the provisions could be extended and strengthened.

Further, governments which are introducing competition law in a potentially hostile environment could follow the strategy of providing a moratorium period of up to two years, during which time the stakeholders are properly educated and opinions on firm conduct are provided without fines or sanctions being imposed. This would allow familiarity of the law to grow amongst stakeholders inducing greater compliance, and technical expertise to grow in the authority. Such a moratorium would also generate the network of allies that the government needs to counter powerful opponents.
4.1.2 Appoint and encourage strong leadership in the competition authority – energetic, non-partisan and competent.

Leading a competition authority—especially in its early years—demands determination, independence and a tireless facility for public engagement. These are qualities valuable in the establishment of almost any new public institution. They are doubly necessary for overcoming the natural resistance that arises against the implementation of effective competition law. Strong leaders of competition authorities in settings as different as Australia, South Africa and Zambia have demonstrated the power of lively media relations and public engagement. Successful leaders secure an authority’s reputation and build its legitimacy by rallying public support behind its objectives and applying the law without fear or favour.

Competence is crucial to sustainable leadership. Appointments to competition authority leadership positions should be non-partisan both in process and outcome; appointees should be chosen for their abilities, not their connections.

Once in office, leaders of competition authorities must exercise their competence with tenacity and discretion. From the outset, they should pick their early prosecutorial targets carefully—selecting cases that they can win, that are based on readily available and convincing evidence, and that will attract popular understanding and approval. People understand price-fixing when it comes to bread prices and bus fares. In the early stages, the competition authority should avoid challenging strong opponents against whom a case would be difficult to win.

4.1.3 Recruit the diverse and expert staff that a competition authority requires – and support the authority with reliable funding.

New competition authorities in developing countries have frequently been disabled by insufficient quality and diversity of professional staff. A common mistake is to underestimate the varieties of staff required to meet the institution’s range of obligation – policy advocacy, investigation, economic analysis, litigation, media relations, public outreach and much more.

The solutions are to hire lawyers with courtroom experience and knowledge of administrative procedure and competition law or to retain outside counsel in difficult cases and economists trained in industrial organization. As professionals, they must be well paid and prestige built into the job status. Staff need to be trained through workshops, scholarships, internships with mature competition authorities, and secondments of foreign competition-law experts into the new organization. To offset inevitable staff turnover, institutional memory needs to be built.

All this, and carrying out the authority’s day-to-day mandate, will require money. Inadequate resources hobble operations and impair independence. The best strategy is to grant the authority the statutory power to develop its own budget and submit it for legislative approval. It is generally unwise to force an authority to subsist on the fines it levies. The temptation to impose self-serving and excessive fines – or the appearance of giving in to that temptation – undermines a competition authority’s credibility and influence.

4.1.4 As a priority, give specialized competition-law training to judges likely to hear cases from the competition authority.

Lack of competition-law skills commonly afflicts judiciaries, especially in jurisdictions new to competition-law administration. Adjudicating competition-law questions will demand more than ordinary legal analysis. It also requires specific economic analysis and familiarity with the underlying principles and assumptions of competition law. A few judges, strategically assigned, can be trained to handle competition cases, as has been done in Jordan where the competition law provides for one or more specialized judges to preside over any competition case. The cases are thereby competently heard and decided, while more judges are exposed to the complexities of competition-law issues.
4.2. Engaging Stakeholders in Implementation

4.2.1 Build alliances with competition-law beneficiaries, counteracting opposition and mitigating the risk of regulatory capture.

Vigorous enforcement of a competition law will incite opposition from interests profiting from anticompetitive conduct. In some cases, opponents of competition law enforcement will try to capture the regulatory process and win exemption for their own anticompetitive endeavours. Family and financial affinities between business and political elites will tend to work against effective enforcement of any competition law.

One of the remedies is to forge coalitions between the competition authority and those who will benefit from predictable and lasting implementation of the competition rules. These can include consumer organizations, farm groups, labour unions, non-governmental organizations interested in good governance and economic justice, small businesses victimized by monopolists, and others. Mass media and specialized journals can publicize the harms of anticompetitive abuses and the benefits of rigorously enforcing the competition law.

An effective competition authority needs the autonomy to build these alliances, even when it means mobilizing public opinion against some anticompetitive action by the government itself. An independent, respected authority can act as a trustworthy counsel to government—and from time to time as a fair-minded critic.

4.2.2 Activate popular interest in competition questions, starting with journalists.

In countries with little history of competition policy and law, citizens will have scant knowledge of the law and initially show little interest in its prospects. An authority, with allies in government, business and civil society, must take the lead in educating and animating broad public understanding of competition law aims and processes.

The authority should put in place a strategy of openness to the press within limits of commercial or judicial confidentiality from the start. That includes regular briefings for media of all kinds, from mass-market newspapers and broadcasters to sector-specific journals and NGO newsletters. It means encouraging media reporting of prosecutions—coaching journalists in the legal and economic details, and reminding them of the overarching economic and social objectives in fostering competitive markets.

Stimulating public education and support also requires personal connection between the competition authority and people in their own communities. That can entail the creation of authority offices in outlying cities and regions, and staging seminars and giving speeches to specific audiences about the law and its significance. And it always calls for the genuine and lively willingness of the authority’s chief executive to publicize the authority’s work and invite public participation in its work.

Not least, this involves bringing hope and reassurance to the victims of anticompetitive predations – encouraging consumers, and businesses, to inform the authority of abuses and to seek relief from the offences being committed.

4.2.3 Collaborate with other government departments and agencies whenever possible and oppose them when necessary.

Governing any country is complicated, and governments usually pursue multiple policy objectives simultaneously. To achieve its own objectives and fulfill its mandate, a competition authority should search out and foster coalitions with like-minded departments and agencies of government. It should actively engage with public officials, legislators, judges, lawyers and others to explain the authority’s mandate and competence. Aligning competition law and regulation with other governmental activities can reinforce the effect and strength of competition legislation.
At the same time, a competition authority must be prepared to carry out its policy obligations even when they might collide with other governmental pursuits – and specifically, when these other pursuits lead to anticompetitive conduct. A new tariff against imports, for example, might encourage domestic price-fixing by newly sheltered companies. The privatization of a government enterprise might create a privately owned monopoly. The government should apply competition principles to the privatization process. Trade protection for an “infant industry” or “national champion” can confer on firms a government-approved monopoly power over a domestic market. Such companies should be subject to the competition law to prevent abuse of monopoly power.

The competition authority should not hold back from resisting and correcting the anticompetitive outcomes of such governmental actions. It should prosecute anticompetitive practices even if they have been blessed – expressly or tacitly – by other government offices. Where it does not itself have the authority to conduct an investigation, it should work to persuade sector regulators to stand against any abuses by newly privatized monopolists. Ensuring that there is clear demarcation of responsibility in the law and mechanisms for cooperation would limit conflict with other regulators. And it should ensure that any policy support or protection for an industry or company be informed by sound competition principles.

4.3. CONTENDING WITH ANTICOMPETITIVE CONDUCT ACROSS NATIONAL BORDERS

4.3.1 To crack a foreign-based cartel, shelter the first defector and levy heavy penalties against the rest.

Liberalization of trade and investment has increased the penetration of markets by MNEs, thereby exposing them to excessive price increases created by international cartels, such as the vitamin cartel. Experience shows that a competition authority can respond effectively to cartels, domestic or foreign, with a leniency program by which the first cartel member to admit to anticompetitive misbehaviour is provided with immunity from prosecution in return for cooperating in the investigation and handing over all available evidence of wrong-doing. The strategy often succeeds since leniency programmes provide incentives to destabilize cartels which are vulnerable to defections as the costs of maintaining the conspiracy rise along with the risks of discovery.

A critical element of the leniency policy is the credible threat of meaningful punishment against remaining colluders. Competition legislation should provide the authority with both the power of leniency for defectors and the power of punishment for the rest. However, where the conspirators are powerful MNEs, and/or the authority is young and weak, the effectiveness of this strategy is limited. Also, in connection with local cartelization, whistle blowing may go against cultural practices. In some societies, particularly small ones where relationships between business persons are very close and familiar, a leniency programme's potential may be weak.

4.3.2 To overcome jurisdictional impediments, develop cooperation among competition authorities and entrench competition provisions in trade agreements.

The legal reach of a national competition authority generally stops at the border, while the economic and social costs of anticompetitive conduct can extend globally. Intergovernmental cooperation against anticompetitive abuses across borders is an obvious imperative.

One mechanism of cooperation consists of formal collaborative agreements among competition agencies. Agency-to-agency arrangements between developing and developed countries can be useful. They enhance the capacity of the developing-country authority, while engaging the authorities of
industrialized countries where most cartels originate. These agreements between specialized agencies also relieve both sides of the need to rely on non-specialist diplomatic services to negotiate cross-border investigations and prosecutions.

However, it is problematic for a young competition authority, particularly in a developing country, to successfully negotiate deep cooperation provisions with a mature authority. Indeed, informal cooperation has proven to be the most effective instrument in such circumstances, and so young competition authorities should strategize to use opportunities where senior staff could meet staff of mature authorities and build relationships. Travel costs should therefore be catered for in the budget.

The other important mechanism of cross-border cooperation is the inclusion of competition provisions in RTAs. Such provisions should, at the least, encourage information-sharing between national competition authorities and facilitate investigative and prosecutorial cooperation. Some regional integration agreements go further, creating intergovernmental institutions for making and enforcing competition regulations.

4.3.3 Stay vigilant against market abuses by very large foreign entrants into domestic markets.

The entry of large foreign-owned companies into a developing-country market can bring sizeable benefits to the domestic economy, including lower retail prices and greater consumer choices. But the arrival of foreign enterprises that alter the structure of the market can also be damaging, putting local competitors out of business and unfairly squeezing local suppliers who now confront a buyer with considerable market power.

To guard against abuses of market power – whether achieved through mergers, acquisitions or greenfield investments – a competition authority should keep itself fully informed about the efficiencies introduced by a big new market entrant as well as the harms caused. It must pay close attention to signs of possible abuse of market power through uncompetitive high prices imposed on suppliers, predations against smaller competitors and the like. And when anticompetitive practices are found, they should be prosecuted and penalized severely. It may be necessary to impose heavy sanctions for non-cooperation in investigations to ensure that MNEs surrender information.
PART 5: A VISION FOR THE FUTURE

Let us imagine a small developing country which has lived comfortably for many years from minerals exports in some isolation from the world economy. It is now facing exhaustion of those resources, given current extraction technologies. A progressive government is in office, which has managed to contain the unequal effects of resource-based growth through active social protection policies. In anticipation of the tailing off of resource-based revenues, policymakers are now investigating growth options for the economy.

The government understands the need to deepen and/or broaden the range of economic activity. It recognises the value of attracting foreign investors to help in the diversification of economic activity, but also sees a risk that many of them would be large, powerful and experienced market operators, which could not only extract (and send out of the country) unwarrantedly high levels of rent but also swamp the local market and squeeze out local enterprises. There is also concern for the prospects of the indigenous entrepreneurs who operate small businesses, which, by some estimates, contribute as much as half of national output (excluding minerals) and seem mostly to be stuck in traditional industries and service occupations and not flourishing in any new, fast growing sectors. Finally, it is known that small farmers and makers of simple consumer goods see their products reaching the consumer through a complex, multilayered distribution system managed by a rich merchant class.

Contemporary understanding of the determinants of growth and development places much emphasis on the institutional foundations. Policymakers in this imaginary country have therefore been examining their institutional options, with special reference to the internal consistency and coherence of the sets of rules embodied in the various institutions that would govern economic behaviour under different scenarios. In essence, these options reduce to the place to be occupied by the state in economic activity. A senior policy adviser is tasked with investigating whether an explicit competition policy, specifically the establishment of a competition authority and the passing of a competition law to be enforced by that authority, would be useful to the development effort.

The adviser comes to the unexpected conclusion that the setting up of a solid competition regime in this sense, though not a panacea in itself, is a key part of the way forward, under any plausible scenario. The provisions of competition law, if well applied, could curb the excesses of large firms regardless of their ownership (local or foreign, private or state owned). Application of competition principles, whether by the authority itself or by sectoral regulators, would ensure that the energies of dominant firms and natural monopolies are directed towards innovation and operational improvements, rather than defensive measures and rent-seeking.

Competition legislation could include investigative techniques and measures to address a range of market manipulations by firms, familiar worldwide. In particular, great advances have been made in penalising cartels, which the evidence suggests are the most damaging form of business collusion and occur at every level of activity from industrial giants to tiny local businesses. Enforcement of competition law would discipline the behaviour of foreign entrants and remove barriers to entry of new firms (local or foreign) attributable to the actions of incumbents, which competition investigators are adept at exposing; induce improvements in efficiency and innovation across sectors; and allow for the growth and productivity...
enhancement of small firms; and all this without being incompatible with effective public support for the development of local businesses, whether in agriculture, manufacturing or services.

Indeed applying competition principles would help ensure that measures to improve the competitiveness of the domestic industry, such as infrastructural improvements, benefit all economic agents and were not subverted by powerful groups to benefit themselves. It would also protect local consumers (whether individuals or businesses) against exploitation by foreign enterprises acting in collusion, and maximise the benefits of development expenditures by government.

Moreover, the presence of a competition law would reassure foreign investors that they would not be subject to devious conduct by incumbent rivals familiar with the local norms of economic exchange.

Thus, a strong competition regime addresses a surprisingly large part of the developmental challenges facing our imaginary country. Foreign MNEs could be invited in, in particular sectors or more generally, without fear that they would exact inappropriate levels of profit. In turn, those MNEs would know that they could seek redress from any domestic firms’ attempt to behave anticompetitively. While this may be a disincentive to some MNEs, if it is only the freedom to reap monopoly profits that draws those MNEs, the benefit of their activities to the country would be low. Productivity and revenue stagnation in the small business sector could improve through greater ease of entry for newcomers, better distribution options for sale of their products and so on (in combination with measures to provide public supports such as market intelligence, training, R&D support, etc.).

Incentives to engage in productive activity and accumulate capital and business skills on their own account would be enhanced for the population at large. The public would have a known method of redress against exploitative business practices that reduce quality and raise the cost of consumer goods. Moreover, this redress would be possible through the actions of a public institution, adding to the political credibility of government. Public investment in infrastructure or provision of health and education and other essential services would attain full value for money with the prevention of bid rigging. As in all small countries, specialist production capacity would always be limited to a narrow range of products and services. The enforcement of competition law would allow many or selected trade barriers to be lowered with confidence that consumers (whether of intermediate or final products) would benefit from access to the lowest cost, highest quality and most innovative products made anywhere in the world, without the domestic distribution system manipulating its margins to prevent price reductions reaching the final purchaser.

The real challenge then, in real developing countries no less than in this imaginary one, is twofold. The first need is to understand and overcome the opposition to competition law from powerful lobbies that benefit from rent seeking. They see only the short term pain likely to follow the disciplining of their behaviour, not the longer term gains that will result to themselves and others from conformity to rules (doubtless more demanding, but more productive and equitable) which determine that rewards come from innovation and increases in efficiency. As pointed out earlier, some Latin American countries such as Panama and Mexico have been able to reduce the influence of these powerful groups over time to the extent that they were able to revise their laws to remove excessive exclusions and exemptions that were initially included in the law under pressure from these groups.

The second, related requirement is to draft a strong law appropriate to the country’s situation – or to amend and strengthen an existing one – and to put in place the resources and institutional processes to ensure the emergence of a solid, credible and effective competition authority able to enforce the law intelligently and without fear or favour, bringing credit to the government which has sponsored its creation. This book has sought to distil the lessons from the experiences of efforts at competition law enforcement in many developing countries towards this end. The evidence presented demonstrates the validity of the argument put forward by many developing countries that “one size does not fit all” and that
competition law must be tailored to specific circumstances. The experiences explored in this book should help young authorities map the terrain they must traverse on their journey towards the successful implementation of a competition regime in their country, highlighting the dangers and pitfalls that may be encountered on this journey, and pointing to the safer paths that can be followed.
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**SHORT GLOSSARY OF COMPETITION LAW TERMS USED**


The purpose of this short glossary is to help the casual reader focusing on terms used within this book. It has been assembled by Jonathan Gage. Terms denoted with a * or ** have been drawn most significantly from the EC and OECD glossaries mentioned above respectively (although sometimes been abbreviated). Online readers of an electronic version of this book will find the ♦ will link to the EU website definition of the following term. A ♢ implies the term is defined elsewhere within this short glossary.

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
</tr>
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<tbody>
<tr>
<td>Abuses of dominance*</td>
<td>Anticompetitive business practices (including improper exploitation of customers or exclusion of competitors) in which a ♢dominant firm may engage in order to maintain or increase its ♢market power.</td>
</tr>
<tr>
<td>Allocative inefficiency</td>
<td>In the context of competition, the deadweight welfare loss to an economy caused by a firm with ♢market power reducing output, raising prices and extracting ♢rent. Besides allocative inefficiency, ♢anticompetitive practices can also cause inefficiencies of reduced ♢productivity particularly over time.</td>
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<tr>
<td>Anticompetitive agreements</td>
<td>A general classification of agreements between rival or potentially rival firms to limit ♢competition, see ♢cartels.</td>
</tr>
<tr>
<td>Anticompetitive conduct/practices</td>
<td>Any activity which has the intent of limiting ♢competition to extract ♢rent. The activity will involve an ♢anticompetitive agreement, ♢abuse of dominance, or ♢merger.</td>
</tr>
<tr>
<td>Cartels*</td>
<td>Arrangement(s) between competing firms designed to limit or eliminate ♢competition between them, with the objective of increasing prices and profits of the participating companies and without producing any objective countervailing benefits. In practice, this is generally done by fixing prices, limiting output, sharing markets, allocating customers or territories, ♢bid rigging or a combination of these. Cartels are harmful to consumers and society as a whole due to the fact that the participating companies charge higher prices (and earn higher profits) than in a competitive market.</td>
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<tr>
<td>Comity*</td>
<td>Principle applied in the field of ♢international cooperation on ♢competition policy. By negative comity, every country that is party to a co-operation agreement guarantees to take account of the important interests of the other parties of the agreement when applying its own competition law. By positive comity, a country may ask the other parties of the agreement to take appropriate measures, under their competition law, against anticompetitive behaviour taking place on their territory and affecting important interests of the requesting country.</td>
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<tr>
<td>Cost of capital</td>
<td>The cost of financing a project or firm expressed as an opportunity cost for an equivalent investment alternative. This typically requires judgements of risk of the project or firm: assessing what components will make up the capital (debt, share equity, etc) and assessing the opportunity costs for those components in the market.</td>
</tr>
<tr>
<td>Hard core restrictions*</td>
<td>Refers to restrictions of ♢competition by agreements or business practices, which are seen by most jurisdictions as being particularly serious and normally do not produce any beneficial effects. They therefore almost always infringe competition law.</td>
</tr>
<tr>
<td>Market power*</td>
<td>Strength of a firm in a particular market. In basic economic terms, market power is the ability of firms to price above ♢marginal cost and for this to be profitable. In ♢competition analysis, market power is determined with the help of a structural analysis of the market, notably the calculation of ♢market shares, which necessitates an examination of the availability of other producers of the same or of substitutable products (♢substitutability). An assessment of market power also needs to include an assessment of barriers to entry or growth (♢entry barriers) and of the rate of innovation. Furthermore, it may involve qualitative criteria, such as the financial resources, the ♢vertical integration or the product range of the ♢undertaking concerned.</td>
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<tr>
<td>Merger**</td>
<td>An amalgamation or joining of two or more firms into an existing firm or to form a new firm. A merger is a method by which firms can increase their size and expand into existing or new economic activities and markets. A variety of motives may exist for mergers: to increase economic efficiency, to acquire ♢market power, to diversify, to expand into different geographic markets, to pursue financial and R&amp;D synergies, etc. Mergers are classified into three types: Horizontal: between firms that produce and sell the same products, i.e. between competing firms. Horizontal mergers, if significant in size, can reduce competition in a market and are often reviewed by competition authorities; ♢Vertical integration between firms operating at different stages of production. Vertical mergers usually increase economic efficiency, although they may sometimes have an anticompetitive effect; and Conglomerate: between firms in unrelated business.</td>
</tr>
<tr>
<td>Monopoly/ Monopsony*</td>
<td>Market situation with a single supplier (monopolist) who - due to the absence of ♢competition - holds an extreme form of ♢market</td>
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</table>
power. It is tantamount to the existence of a dominant position. Under monopoly, output is normally lower and price higher than under competitive conditions. A monopolist may also be deemed to earn supra-normal profits (i.e. profits that exceed the normal remuneration of the capital). A similar situation on the demand side of the market, that is with a single buyer only, is called monopsony.

**Oligopoly**: A market structure with few sellers, who realise their interdependence in taking strategic decisions, for instance, on price, output and quality. In an oligopoly, each firm is aware that its market behaviour will distinctly affect the other sellers and their market behaviour. As a result, each firm will take the possible reactions from the other players expressly into account. In competition cases, the term is often also used for situations where a few big sellers jointly dominate the competitive structure and a fringe of smaller sellers adapt to their behaviour. The big sellers are then referred to as the oligopolists. In certain circumstances this situation may be considered as one of collective (also joint or oligopolistic) dominance.

**Productivity**: The most common usage of this term is the value of output per worker’s hour. This is an example of factor specific productivity (i.e. labour). We would say one is more productive if one produces more output for a given hour of work. But a worker may be more productive with a new, more expensive machine; labour productivity may rise with more investment in capital (another factor of production). Hence in economic studies of competition, where we focus on improvements in welfare caused by competition through innovation, efficiency, etc., we use total factor productivity: the value of output as it exceeds beyond the value of the input factors of production (traditionally land, labour and capital).

**Regulatory capture**: is the circumstance when a government regulatory agency (such as a competition authority) which is supposed to be acting in the public interest becomes dominated by the vested interests of the existing incumbents in the industry that it oversees.

**Rent**: A firm (or group of firms acting anticompetitively) can extract rent when it has market power by restricting output forcing consumers to pay more than they would otherwise pay in a competitive market. Rent generates economic profit (revenue less economic opportunity costs). Economic opportunity costs usually differ from explicit accounting costs. Most of this adjustment typically reflects the opportunity cost of capital.

**Rule of reason**: An evaluation of the pro-competitive features of a restrictive business practice against its anticompetitive effects in order to decide whether or not the practice should be prohibited. Some market restrictions which prima facie give rise to competition issues may on further examination be found to have valid efficiency enhancing benefits. The opposite of the rule of reason approach is to declare certain business practices per se illegal, that is, always illegal. For instance, price fixing agreements and resale price maintenance agreements in some jurisdictions are per se illegal.

**Vertical integration / restraints**: Relationship, ownership or control of different stages of the production process, e.g. petroleum refiners, pipeline companies and oil explorers. A vertical restraint is an agreement setting conditions under which the firms within a production process may purchase, sell or resell certain goods or services.