

Competition Policy and Law - An Overview

The principal objective of competition policy is to foster competition as an instrument for accelerating growth. The policy is meant to fuel innovation and create market efficiencies that offers better products and lower prices thus benefitting consumers and maximizing welfare. . Competition law is the enactment of that policy and achieves its objectives in three ways:

- (1) Prohibiting anti-competition agreements and practices that harm free trade and competition;
- (2) Preventing abuse of dominant position and anti-competitive practices that lead to such a dominant position;
- (3) Regulating mergers and acquisitions.

Competition is irrefutably beneficial for every market participant. Competitive markets give consumers wider choice and lower prices. It gives sellers stronger incentives to minimize their costs through innovation and other productivity enhancing techniques. This enables firms to pass on cost savings to the customers and offer better products and greater choice at lower prices.

Nonetheless the gap between the assumptions of such theories and the market realities and practices both in developing and developed countries remains pervasive. While there is a broad consensus on the competition policy objectives there is considerable divergence in the application and practice of competition law leading to question marks about its effectiveness. Even in a mature jurisdiction like United States with over a century of experience, the application of antitrust laws has not moved beyond semantics. The alternating views on the reductive and expansive interpretations of the law have led to confusing and apparently contradictory judgments on antitrust cases that have belied the hopes and aspirations of lawmakers and the stakeholders.

Competition law poses more a public policy challenge than a legal argument. Indeed US antitrust decisions in the first half of twentieth century exhibited hostility to large successful firms. This has since changed. Recent judgments, on the other hand have shown greater understanding of the social context and market economics. Nonetheless defining monopolies continues to remain a big challenge. In a seminal case known as the Grinnell Test, the US Supreme Court distinguished between the willful maintenance of monopoly power as opposed to power resulting from growth or development as a consequence of a superior product, business acumen, or historic accident.

The Supreme Court in *United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966), held:

The offense of monopoly under § 2 of the Sherman Act has two elements: (1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.

As Joseph England, an eminent authority on competition law, points out, “The Court’s language, however, provided scant guidance regarding how one could distinguish the type of conduct that violated

Section 2 from that which did not. The Court noted that the mere building of a better product did not violate Section 2, apparently recognizing that the antitrust laws were designed to enhance competition and that prohibiting product improvements so as to ensure that firms offering old, undesirable products could maintain their market position would subvert that objective. A logical extension of that proposition appeared to be that – at least until some lower limit was breached – acquiring or maintaining monopoly power by offering low prices did not offend Section 2. After all, whether a product is “superior” depends to some extent on its price. It would make little sense to encourage a company to manufacture a light bulb that would last twice as long, but then to condemn it for not charging double the price. Construing Section 2 to condone price competition, moreover, was faithful to the origins of the law. The U.S. antitrust laws, after all, sprang from a concern that the late nineteenth century trusts had burdened consumers and businesses by charging excessive prices. It was one thing to hold that charging excessive prices by itself did not violate the antitrust law, but it would be quite another, in all but the most exceptional circumstances, to use the antitrust laws to require firms to charge high prices.”

“Business acumen” is a double edged sword. It can be used to develop a more innovative product that would benefit the consumer or “a complicated scheme to undermine one’s competitors without offering a better or lower-priced product, and it did not seem that those two types of conduct should be treated the same. It would be curious indeed if one could defend against a claim of monopolizing conduct simply by arguing that it was clever monopolizing conduct.”

Predatory pricing is extreme form of abusive exclusionary pricing, where the dominant firm charges low prices, with a strategy designed to drive rivals out of the market. Most often, they are evidence of vigorous competition and beneficial to consumers. Loyalty and bundled discounts can be used strategically to exclude small rivals. Tying arrangements can be barriers to entry and innovation, but they may also be a means for achieving manufacturing or distribution efficiencies. Exclusive dealing agreements can limit distribution channels available to small manufacturers, but they are also used to achieve efficiencies by aligning the incentives between a manufacturer and its distributors.

In certain circumstances even pricing above average variable cost can be “predatory” or “exclusionary”. It can be argued that it can inhibit competition to the detriment of competition and consumers. Yet, the Supreme Court has created, and probably the majority of commentators support, a safe harbor for pricing above average variable cost (or some other cost standard). They arrive at this result by appraising, at least in a qualitative way, the likelihood of false positives and false negatives, and the consequences of each. The Supreme Court, for example, recognized that predatory pricing involves incurring losses in the short run which the predator hopes to recoup in the long run if it succeeds in driving out competition and being able to charge supracompetitive prices. Comparing the certain short-run loss to the conjectural long-run gain, and recognizing that one must recoup more than a dollar in the future to compensate for a lost dollar in the present, the Court noted a consensus among commentators that predatory pricing is “rarely tried, and even more rarely successful.”

A similar challenge arises with respect to the prohibition of abuse of dominance, the focus of Article 4 of the Act, says William Blumenthal, former General Counsel of FTC. “It may be obvious, but an “abuse of

dominance” violation requires proof of “abuse” and proof of “dominance,” and both of those elements present doctrinal complications. Whether a firm is dominant can be difficult to measure. Market shares alone are ordinarily insufficient to establish dominance – their predictive power is highly sensitive to accurate determination of the denominator (the universe, or the “market”), and they fail to account for factors that may defeat a firm’s ability to exercise market power, such as ease of entry. And whether conduct is abusive is even more difficult to measure. The practices that provide the basis for a finding of abuse are usually identical to practices that, in most contexts, are efficiency-enhancing and beneficial to the public. The market context shifts, but the practices themselves are the same. That is, depending on market context, a particular practice can be anticompetitive or neutral or procompetitive. Most often, the practice will be neutral or procompetitive. In a small percentage of cases, the practice will be anticompetitive. Because the practice itself is ambiguous, policy makers face great difficulty in framing sensible legal rules. We can’t simply prohibit certain practices, because we’ll be prohibiting things that we generally want to encourage. Policy makers have recognized this problem for a long time.

Public restraints are far more effective and efficient at restraining competition. Unlike private restraints, there is no need to maintain backroom secrecy or to incur the costs of conducting a covert cartel. Public restraints can be open and notorious. Public restraints are also a more efficient means of solving the entry problem. Rather than ceaselessly monitoring the marketplace for new rivals, a firm can simply rely on a public regime that, for example, provides for only a limited number of licenses. Perhaps the clearest advantage of public restraints is that they frequently include a built-in cartel enforcement mechanism. While cheating often besets private cartels, public cartels suffer from no such defect. Cheaters, once identified, can be sanctioned through government processes.

As a matter of competition advocacy, it is now commonplace for competition authorities to express concern over the anticompetitive consequences that often flow from regulatory capture and rent-seeking. Thus, in the United States competition authorities have conducted advocacy to address governmental restraints that reduce competition in a wide range of industries and services – physicians, lawyers, funeral homes, and other professional licensing; advertising claims; sale of wine or real estate using electronic commerce; transportation; and many more.

The problem of governmental restraints may be more pronounced in developing economies, in which we are more likely to observe recent privatization, former state-owned enterprises, and significant licensing requirements and other governmental entry barriers. A too-common pattern is that former state-owned monopolies, now privatized and nominally open to competition, rely on their regulators to adopt rules that impede entry and discourage the emergence of new competitors.”

Notwithstanding these arguments, such controversial aspects in the implementation of competition policy could hardly be thought to outweigh the enormous social and economic benefits accruing from competition. There is growing empirical evidence that more competition leads to more innovation and accelerates productivity growth and there is a strong positive correlation between the effectiveness of competition policy and growth.

The need for competition law becomes even more evident when foreign direct investment is liberalized. The impact of FDI is not always pro-competitive. Very often foreign direct investment takes the form of a foreign corporation acquiring a domestic enterprise or establishing a joint venture with one. By making such an acquisition the foreign investor may substantially lessen competition and gain a dominant position in the relevant market thus charging higher prices. Another scenario often encountered in developing and transition economies, is where the affiliates of two separate multinational companies (MNCs) have been established in competition with one another in a particular market, following the liberalisation of foreign direct investment in that country. Subsequently, the parent companies overseas decide to merge. With the affiliates no longer independent of one another, competition in the host country may be virtually eliminated and the prices of the products artificially inflated.

The real question that needs to be addressed is not 'whether or not to have competition policy' but "how to maximize the expected benefits arising from competition". In this context, one has to be careful of not seeking too narrow definition of competition policy objectives which may harm developing countries. An important paradox is that promoting transparency in market transactions can harm competition by enabling companies to sell at high prices through tacit collusion. Likewise, aiming at very high quality standards for products to ensure consumers get good quality products may act as entry barriers and limit dynamic competition. Excessive competition also adversely affect the sustainability of small and medium enterprises

Most of these adverse consequences of mergers and acquisitions by MNCs can be avoided if an effective competition law is in place in the host country. Furthermore an economy that has implemented an effective competition law is in a better position to attract foreign direct investment than one that has not. This is not just because most multinational corporations are expected to be accustomed to the operation of such a law in their home countries and know how to deal with such concerns but also that multinational corporations expect competition authorities to ensure a level playing field between domestic and foreign firms, including among MNCs. . During the past decades, many developing countries have instituted programmes of microeconomic reform, involving greater reliance on markets and less emphasis on state intervention. Among the more important changes have been a lowering of tariff barriers, the removal of many quantitative import restrictions, the reduction of subsidies to domestic producers, the privatisation of government business enterprises, the easing of foreign exchange controls and the encouragement of foreign direct investment.

Underlying these reforms is a renewed confidence that market forces and the individual decisions of consumers and privately owned businesses, can make a greater contribution to economic and social development than an inward looking centralised economic system. However, the potential benefits of a shift towards a more market oriented economy will not be realised unless business firms are prevented from imposing restrictions on competition. Deregulation of previously regulated sectors, including state-controlled monopolies such as utilities and "network industries" considered for the most part to be "natural monopolies," need to be subject to competition review by competition authorities or sectoral watchdogs to ensure that these firms do not abuse their dominant position in the market.

It has to be emphasized that a robust competition policy is central to economic reforms. For instance price liberalization, if not accompanied by competition laws and policy aimed at controlling economic behaviour and structures, can result in substantial price increases and reduced benefits for the overall economy. If monopolistic structures are allowed to continue unchecked, price liberalization will not be effective. The same can be said of privatization of state monopolies into private monopolies. Finally, opening of markets through import competition and FDI liberalization might bring enhanced competition, but if no safeguards exist, foreign firms might also engage in anticompetitive practices and abuse dominant market position. Hence the need for a strong and effective competition law which will ban anti-competitive agreements and encourage conduct where there are demonstrable net public benefits.

Merger control is emerging as one of the most important area of competition law. The worldwide Mergers and Acquisitions in the first half of 2008 totaled US\$1.6 trillion. Mergers and Acquisitions in India totaled US\$33.1 billion in 2007. The World Investment Report, 2005, by UNCTAD designated India as the third most attractive research and development centre in the world. India is the largest foreign investor in the UK outpacing even the US. India decided to abolish its archaic Monopolies and Restrictive Trade Practices Act and passed the Competition Act 2002 thus shifting its focus from curbing monopolies to promoting competition. The Act came into force on 20 May 2008. Recognising & realising that the trade agreements have the potential of preventing, restricting, distorting, discouraging, impeding or scuttling competition in markets, Section 3 (1) & (2) of the Act declares that 'No enterprise or association of enterprises or person or association of persons shall enter into any agreement in respect of production, supply, distribution, storage, acquisition or control of goods or provision of services, which causes or is likely to cause an 'appreciable adverse effect on competition (AAEC) within India and that such agreement being anti competitive, is void'.

The Act stipulates 5 kinds of vertical agreements. Section 3(4) of the Act provides that

Any agreement amongst enterprises or persons at different stages or levels of the production chain in different markets, in respect of production, supply, distribution, storage, sale or price of, or trade in goods or provision of services, including— a) tie-in arrangement; b) exclusive supply agreement; c) exclusive distribution agreement; d) refusal to deal; e) resale price maintenance,

shall be an agreement in contravention of sub-section (1) of Section 3 if such agreement causes or is likely to cause an appreciable adverse effect on competition in India.

These vertical restraints are only illustrative (not exhaustive and have been defined inclusively in the Act. By and large, vertical agreements are not subjected to the rigours of competition law. However, where a vertical agreement has the character of distorting or preventing competition, through exclusive distribution, it comes under the anti competitive behaviour.

IPR is an important part of competition law and is designed to give protection to patent holder with a view to encouraging innovation. Mark Twain's famous statement that a country without a patent system is like a crab, destined to move only sideways and never forward speaks of the importance of patent law

and other categories of intellectual property law such as copyright, trade secrets, trademark, right of publicity, in shaping an open, democratic, market-based society.

The design of intellectual property rights rests on the recognition of these four baselines and the choice among them for the particular market environment the legislature seeks to regulate. For example, the first mover baseline may be appropriate for pioneer innovations while the pro-consumer baseline may be appropriate for mature inventions of high social value, such as pharmaceuticals. By recognizing that competition and intellectual property rights inform each other, policy makers can use these competitive baselines to calibrate intellectual property rights to the particular market and social context in order to reach the desired policy goals. I am, of course, not suggesting that this analysis works in a particularly mechanical way. Rather, the recognition of competitive baselines for intellectual property rights emphasizes the need for a richer policy debate about the relationship between intellectual property rights and competition.

India's accession to the World Trade Organization in 1998 occurred as the country suffered a foreign reserve crisis in the 1990's that followed a privatization of the economy in the late 1980's. In March, 1999, the Indian legislature passed emergency measures to comply with TRIPS agreement and deal with a backlog of over thirty thousand patent applications. The Indian government established a mailbox where patent applications could be sent and an administrative structure for the processing of applications with patent offices in Kolkata, New Delhi, Mumbai, and Chennai. In 2005, the parliament extended patent protection to chemical compounds amending the 1970 Patent Act that had denied such protection. Despite these efforts in the area of patent law, as well as concomitant efforts in the areas of copyright, digital rights, and trademark, India continues, as of this writing, to be on the United States Trade Representation Priority Watch List under Section 301 of the General Agreement of Tariffs and Trade. The Indian government's moves to privatize and to reform its intellectual property laws is in part the basis for Goldman Sach's prediction in 2003 that the Indian economy could surpass that of German, Japan, and the United Kingdom in thirty years.

Jurists in the United States and the European Union have struggled to reconcile the exclusionary prerogatives of intellectual property law with the goals of antitrust and competition laws. Whether in the field of licensing practices, parallel importation, or exclusionary dominance, the laws of the United States and the European Union have attempted to balance intellectual property and competition law by creating exceptions, safe harbors, and limitations on rights that allow the two areas of law to progress accordingly.

At the WTO level, agreements on IPR and services are increasingly being assessed from a competition perspective. In India, though laws against unfair competition and for the protection of IPR have existed for a long time, the competition policy has been recently put in place by the enactment of the Competition Act, 2002. The Preamble to the Act states its aims thus:

An Act to provide, keeping in view of the economic development of the country, for the establishment of a Commission to prevent practices having adverse effect on competition, to promote and sustain competition in markets, to protect the interests of consumers and to ensure freedom of trade carried on

by other participants in markets, in India, and for matters connected therewith or incidental thereto. Though competition law and IPR have coinciding philosophies, their interface is challenging because of the dynamic nature of each of them. Competition law uses the elements of markets and pricing which are continually in flux. IPR is also in flux, with the advent of newer categories of IPR. How the two can be held together in spite of the dynamic scenario that faces us is the problem that competition policy should seek to solve.

There are currently about 80 developing and transition economies that have competition laws, but not all of them have adopted a formal merger review system and fewer still are actively enforcing their merger provisions. Many competition agencies in these countries are receiving expertise and advice on the design and enforcement of their competition laws from international organizations such as the OECD, World Bank, UNCTAD, and the recently established International Competition Network, NGOs such as CUTS International of India and from the more experienced competition law jurisdictions.

In the words of William Blumenthal “the integrity of competition law in India foreseeably will face a related challenge: intervention by various political forces to alleviate the pressures that are imposed by the political process itself. I have just described political intervention in the form of government-imposed restraints, but there are other forms as well. You should anticipate that there will be calls for industries to be exempted selectively from the scope of the Competition Act. And you should anticipate that the Competition Commission from time to time will be buffeted with demands to grant favor, either by standing down where intervention would be justified or by intervening where a complainant is complaining of the rigors of the competitive process itself. Here, too, I hope you will offer CCI the support and encouragement that it deserves. As we observe in the United States, “Living with competition is hard. Living without it would be harder.”

Blumenthal continues, “Overcoming these doctrinal, institutional, and administrative challenges can be difficult. Even in mature competition regimes such as my own, they are sometimes daunting, and efforts to address them require frequent attention of both public and private leadership. But the efforts and attention are worthwhile and probably necessary, for a well structured competition regime can be a source of economic efficiency, consumer welfare, innovation, and development. If implemented poorly, though, a competition regime can subvert the goals it was intended to serve; it can leave the public wondering whatever came of the promised benefits. As you implement the Competition Act, you may feel pressed for speed, but take the time to get the implementation right. Five or ten years hence, you will be grateful that you did”.

Competition policy is a complex, cross-cutting policy instrument which is affected by a number of interconnected factors. Its effective implementation requires a holistic and integrated mind with ability to hold two opposing views in mind and still have the capacity to function. Its practitioners, more than anyone, need to be men of “significant learning”, learning more than a mere accumulation of facts and presentation of a carefully constructed argument couched in legal rhetoric.

Competition law is essentially an economic law. It is anathema to the purists and doctrinaires. Its effective implementation would require a cultural change and change in the mind set of legal

practitioners. Legal and political theorists from the time of Plato have wrestled with defining distinction between law and justice. There is a constant debate whether justice is part of law or simply a moral judgment. Owen Dixon, Chief Justice of Australia when asked whether it was part of the duty of a lawyer to contribute towards the progress of society, replied it was not. The duty of a lawyer, he said was “to keep a hand on and hold steady the framework and foundation of law”.

We have come a long way since. US Supreme Court judge, Justice Brandeis, the author of famous Brandeis Brief that has motivated social and economic legislation in US, says, “A lawyer who has not studied economics is very apt to become a public enemy”. These are harsh words but as Lord Keynes said “Words have sometimes to be harsh since they represent an assault on the thought of the unthinking”.

ECS Wade, a Cambridge Professor of law says in “the Aims of Legal Education”: “We should teach and provide law as a great human institution serving social and economic end and in relation to the world in which we live.” This world has changed beyond recognition during the 70 years since these words were written. Of the 100 most successful companies listed by Forbes in 1917 not one is making money. The CEO of world’s most powerful country is a black man whose father came from Africa. In this multi reality, meta-digital world of change, tumult and turbulence, where the very nature of change is changing by the hour, perceptions of truth cannot be constant. So each judgment becomes a “work in progress” and learning experience. We would realise the significance of TS Eliot, in Little Gidding: “And the end of all exploring will be to arrive where we started and know the place for the first time.”

With these judgments placed on the internet in full view of the millions of Tweeters, users of Facebook and MySpace, humility and transparency will be best armour. Instead of being driven by the desire to defend our challenge will be to make it better next time. As Confucius said “Our greatest glory lies not in never failing but rising each time we fail.”

This would call for a paradigmic shift of the legal process as well as the minds of jurists and practitioners. Defensiveness would give way to exploration and herald “next level” jurisprudence which would take into account not only economic but sociological and environmental goals. An overriding aim of competition law is to promote economic justice. “It is a hand maiden of modern economics and should be part of laws that reflect societal values known as sociological jurisprudence”, says Mr Fali Nariman , one of India’s foremost jurists.

We are living in a world of harsh inequalities, inequity and injustice. There appears a widening disconnect between law and justice. In this interconnected and interdependent world where human aspirations are rising exponentially, people may be able to stand poverty but will not stand injustice. India, that has successively recorded the second highest growth in GDP and ranked third in Mergers and Acquisitions, is 128th on the Human Development Index. From Bogota to Bangkok our biggest challenge is to bridge the widening inequalities. The legal fraternity and jurists have a formidable challenge to use law as a driver of change, innovation and inclusive growth. This would mean bidding good bye to groupthink and capitalising the 5 Ds – disruption of status quo and valuing diversity, dissent, dialogue and disclosure. Lawyers are heirs to a noble tradition of inventiveness. The most ennobling element of a

lawyer's profession is that it can ensure justice for its client. Justice is the only weapon that can secure stability to society and provide sustainability to business. As Pope Paul VI said "If you want peace, work for justice." Competition law is essentially an instrument that helps us achieve that elusive goal.

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