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The role of competition policy in promoting economic development: The appropriate design and effectiveness of competition law and policy

Note by the UNCTAD secretariat

Executive summary

To be effective in supporting the development process, competition law and policy (CLP) need to be supported and compatible with other complementary pro-development policies that can bear on economic development. A spectrum of factors – including social, economic and political environment – dictate the choices for competition provisions and enforcement design. Moreover, the priorities adopted by governments in terms of budgetary support, manpower availability and political support are key determinants of agency effectiveness. States would want to exercise their policy space to adapt their competition laws and enforcement institutions to local conditions. The report also discusses the impact of competition policy on economic development. In particular, it addresses (a) How effective can CLP be in promoting economic development? (b) What are the factors that can augment or impede such effectiveness? (c) Given that countries are at different stages of their economic development process, should the design and enforcement of their CLP vary and, if so, in what ways?

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Introduction

1. Competition refers to rivalry among firms in the marketplace. It also extends to envisaged or potential rivalry. Competition policy refers to government policy to preserve or promote competition among market players and to promote other government policies and processes that enable a competitive environment to develop. Competition policy has two major instruments. The first is a competition law which contains rules to restrict anti-competitive market conduct, as well as an enforcement mechanism, such as an authority. The second major instrument, particularly important in the interface with other economic policies, is competition advocacy.

2. In recent years, there has been a trend towards convergence in the scope, coverage and enforcement of competition laws and policies worldwide. This is due to (a) the widespread trend towards liberalization of markets and adoption of competition policies; (b) greater emphasis upon consumer welfare, efficiency and competitiveness objectives in the provision or application of competition laws; (c) greater similarity in economic analyses and enforcement techniques; (d) the universal condemnation of collusive practices; (e) tightening up of enforcement; (f) a more prominent role for competition authorities in advocating competition principles in the application of other governmental policies; and (g) the strengthening of international consultations and cooperation.

3. However, there remain many important differences among competition laws and policies, including in (a) the priority attached to competition policy vis-à-vis other policies; (b) the importance attached to objectives other than consumer welfare or efficiency under many competition laws; (c) legal approaches to the control of anti-competitive practices; (d) analytical techniques utilized; (e) substantive rules applicable in particular to vertical restraints, abuses of dominant positions, mergers, joint ventures and interlocks; (f) the structure or scope of *de minimis*, intellectual property or other types of exemptions; (g) enforcement capabilities and actual strength of enforcement; (h) the legal doctrines under which competition laws are applied outside national territory; (i) the actual ability to apply them or frequency of application; (j) the extent to which different countries participate in international cooperation in this area; and (k) regulatory restrictions upon market entry.

4. Despite these differences, there are now sufficiently broad similarities in the objectives, content and application of competition laws and policies to form the substantive basis for designing appropriate competition laws that reflect the specific circumstances of developing countries and their enforcement capabilities.

5. Some national laws in developing countries and economies in transition have followed developed country models. A significant number of laws in Central and Eastern Europe, moreover, have replicated the main provisions of the competition rules of the European Union (EU). This is especially so for economies in transition that have entered association agreements with the EU and that aspire to full EU membership. For other countries, the UNCTAD Model Law on Competition (the Model Law) may provide a model. The Model Law reflects recent trends in competition legislation worldwide and is supplemented by related Commentaries that have proved to be important for the process. The text was also informed by the United Nations Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices adopted by the United Nations General Assembly at its thirty-fifth session on 5 December 1980 by resolution 35/63 (the United Nations Set), and has been revised and redesigned to make it reader-friendly, as called for in the tenth session of the Intergovernmental Group of Experts, which acted as a preparatory meeting for the Sixth United Nations Review Conference.

6. The United Nations Set emphasizes the competition policy goal of promoting economic development, and many developing countries view competition as having this role. In this context, "competition" is an intermediate objective and economic development is a final goal. Other relatively common objectives are the promotion of small and medium-sized enterprises (SMEs), restriction of undue concentration of economic power and ensuring fair competition. Public interest objectives – which may be relevant to development objectives – are fairly widespread among developing countries, but also present in some developed countries' competition laws.

I. The appropriate design of competition policy and law and their institutional framework in developing countries and economies in transition

7. To be effective, competition system design requires careful pre-reform assessment of existing conditions in the country and attention to how the country will implement the competition policy. A careful assessment of initial conditions not only will influence decisions about the substantive content of the competition law, but also will identify weaknesses in supporting institutions and offer plans to enhance their capability.

8. Decisions about the appropriate design of competition policy in developing countries must therefore acknowledge the distinctive features of their economic, social and cultural environment. Available information shows that, in most developing countries, implementation capabilities do not match up the demands of a modern competition system.

9. Concern about the mismatch between institutional capabilities and the demands of an effective competition policy are part of a wider challenge that developing countries face in introducing economic and legal reforms. These include the protection of property rights, setting up a system of enforcing contracts, creating legal frameworks for the establishment and dissolution of business entities and enhancing financial institutions and banks.

10. Institutions – both formal, such as legal frameworks, and informal – are part of the unnoticed but necessary architecture of markets. Institutional architecture surrounding well-functioning markets (including those for capital and labour) play a critical role for economic development and efficiency. Unlike developed countries, many developing economies do not have well-functioning factor markets – such as stock exchanges and bond markets – and have often been unable to create institutions that support the operation of markets, such as bankruptcy codes, efficient contract enforcement and the like. These "missing markets" and "missing institutions" alter the optimal, and perhaps feasible, policies with respect to competition in an economy. At the same time, these missing markets and institutions have implications for optimal enforcement of competition law.

11. Different countries will apply different approaches according to their circumstances, and it cannot be expected that an approach that works for one country could be imposed on another. The powerful forces that shape nations' competition and regulatory systems are often unique to particular nations, and national differences impose significant limitations on harmonization. However, the experience gained so far with formulation and the enforcement of competition law and policy in developed and developing countries suggests a number of critical issues that seem reasonably certain to apply in most developing countries and economies in transition. These issues are discussed below.

A. Independence of the competition authority

12. There is widespread agreement that independent regulators are at the core of regulatory governance in liberalized economies. Indeed, the UNCTAD Model Law on Competition is formulated on the assumption that the most efficient type of administrative authority for competition enforcement is likely to be one that (a) is quasi-autonomous or independent of the Government, with strong judicial and administrative powers for conducting investigations and applying sanctions; and (b) provides the possibility of recourse to a higher judicial body.

13. It is generally accepted that decisions by competition authorities should be based on objective evidence, that those authorities should maintain a consistent respect for market principles, and that the decision-making process should be neutral and transparent. The reasoning behind this view is that sound policy outcomes are assured only when decisions by the competition authority are not politicized, discriminatory or implemented on the basis of narrow goals of interest groups. This reasoning is typically translated as a requirement for competition authorities to be insulated from undue political interference. In practical terms, this necessitates a separation of policy implementation from policymaking and a departure from the traditional structure of the machinery of Government. Thus, Government is compelled to cede control over day-to-day functions and decision-making to the authority. As a direct consequence, private interest groups are denied the possibility to lobby ministers and lose the means for gaining favourable treatment.

14. In addition to prescribing the authority's structure, enabling legislation should also give legal meaning to the authorities' operational independence by prescribing functions, powers, the manner in which members of management and staff are to be appointed, their tenure and removal, and how the body is to be financed. Likewise, how the body shall relate to the executive and legislature should also be prescribed. These attributes assure organizational autonomy and establish the arms-length relationship with political authorities.

15. Tensions between the minister responsible for competition policy and the competition authority may arise from time to time as a result of insufficient clarity on the respective roles and responsibilities of the minister and the management of the competition authority, on how the competition authority is to be responsive to political direction, and on issues related to the streamlining of public expenditures for which the minister or another government department may be held accountable.

16. Since the competition authority has a legal obligation to correctly exercise this discretion, it is customary for the legislature to resort to judicial review to police the enforcement actions of the competition authority. The enabling legislation will often prescribe the role and authority of the courts in the enforcement of the competition legislation.

17. It is interesting to note that, in some cases, a competition authority might start out as a ministerial department but later gain more independence (e.g. Tunisia's council and Brazil's agencies) symptomatic of a dynamic and evolutionary process in play. There are also instances where the legal independence of the competition authority has been flouted. The Kenyan Monopolies and Prices Control Commission was part of the Ministry of Finance, but after UNCTAD peer review, a new law was drafted prescribing an autonomous institutional set up for the Commission. The draft bill is in Parliament.

B. Judicial review of competition cases

18. In most jurisdictions, legislators elect to police by judicial review. It is widely held that independent judicial review of the decisions of competition authorities, whether through the regular courts or through administrative tribunals, is desirable for the sake of the fairness and integrity of the decision-making process. Most jurisdictions appear to favour a procedural review of competition cases whereby the appeal body confines itself to a consideration of the law, including a review of procedures adopted by competition authorities in the exercise of their investigative and decision-making functions, rather than a consideration *de novo* of both evidence and legal arguments. Accordingly, the intention is not for the courts to substitute their own appreciation, but to ascertain whether the competition authority has abused its discretionary powers. Grounds for review will often include lack of jurisdiction, procedural failure and error of law, defective reasons, manifest error of appreciation, and error of fact. In this context, judicial review is generally seen as an end-stage process where judgement is passed on results or actions already taken – i.e. decisions already taken by the competition authority in line with whether decision-making powers are vested in the chief executive, a board of commissioners or a separate quasi-judicial body in the form of a specialized competition tribunal (e.g. Brazil, Peru, South Africa and the United Kingdom). The International Competition Network (ICN) asserts that structures of decision-making in which the investigative and adjudicative processes are strictly separated are more likely to pass muster at judicial review than are systems in which the exercise of these functions is conflated.

19. In the context of judicial review, it is notable that in many countries judicial review is either confined to administrative courts or the administrative court is the court of first instance (e.g. the Bolivarian Republic of Venezuela, Colombia, Croatia, Latvia, Tunisia and Turkey). In some jurisdictions, specialized competition appeal courts have been constituted (e.g. Denmark, Singapore, South Africa and the United Kingdom). There are cases in which the decisions of the competition review can be overturned by the executive in exceptional situations, e.g. Croatia (see TD/RBP/CONF.7/5).

C. Staffing and financial resources of the competition authority

20. Despite the apparent prevalence of autonomous agencies in many developing countries, the less favourable economic and fiscal conditions have exacerbated tensions and brought to light a number of pitfalls related to the creation of public sector bodies in the context of a wide gap between resource need and availability. The pitfalls are linked in the main to skills shortages, low public sector pay, risks of corruption and capture, tensions between the minister responsible for the competition policy domain and the competition authority, and weak accountability.

21. In most developing countries, civil servants are generally paid less than their private sector equivalents. Many developing countries have experienced declines in the real wage paid to public sector employees during recent years. The possibilities of recruiting and retaining highly qualified personnel in the public service, and especially in specialized areas such as competition enforcement, is thus negatively affected. Capable civil servants will tend to exit the public sector when their training and qualifications make them attractive to potential private sector employers.

22. The risk of corruption and capture in developing countries is a troublesome issue. The empirical evidence as to whether low public sector pay fosters corruption is mixed and theory does not predict that higher pay will always reduce corruption. Competition enforcement, particularly in jurisdictions that draw members of the board of commissioners

from the private sector on a part-time basis, raises some tricky issues relating to members' impartiality and independence.

23. Concerns also revolve around the ability of part-time board members holding senior positions in private companies to attain and maintain desirable levels of objectivity and the government–industry revolving door. This is a problem also for developed countries, but in smaller and poorer economies these concerns take on a particular significance because there is a relatively smaller pool of individuals of sufficiently high standing to choose from.

24. The general shortage of skills affects not only the competition authority but also the legal fraternity, the business sector, the judiciary and the legislature. Since competition enforcement is not undertaken in a vacuum, this renders competition advocacy by the authority a critical factor in gaining credibility and a constituency.

D. Exemptions and authorizations

25. While "best practice" advice suggests that competition law should apply to all sectors and firms in the economy engaged in commercial activity, in practice various types of exemptions are granted for social, economic and political reasons. The granting of exemptions, however, does not necessarily imply the weakening of competition law enforcement. On the contrary, granting exemptions may further various objectives of competition law and industrial policy. One example is research and development (R&D).

26. In many jurisdictions, certain R&D activities may benefit from exemptions under competition law. R&D may aim at activities ranging from pure research to improving production processes of specific products. These may result in new products and lower prices, which increase consumer choice and consumer welfare. In the pharmaceuticals and electronics sectors, for example, firms cooperate in R&D but compete vigorously in the pricing and sale of their respective products. In most instances, the exemptions are activity- and time-limited and apply only to the extent necessary for that cooperation. From a development policy perspective, R&D exemptions promote the objective of restructuring the economy towards more technology- or knowledge-intensive industries.

E. Competition advocacy

27. In addition to enforcement functions, competition authorities have advocacy functions. Other than business and the general public, Government as a whole (including other regulatory bodies) is a key target of competition advocacy, particularly as it relates to the shaping of competition policy and bringing about market-friendly reforms throughout the economy. Accordingly, the ability of a competition authority to freely comment on and recommend improvements in public policy, regulation and legislation is another attribute by which the operational independence of competition authorities is assessed. Many laws give competition authorities the responsibility of advising the Government on the impact on competition of proposed new laws and regulations. For example, in India, the Governments have the option to seek the commission's opinion when considering competition policy matters, while the autonomous government of Andalusia, Spain is obliged by law to seek an opinion. However, the opinions of the commission are not binding on the minister. Similarly, in Tunisia, the minister may consult the Competition Council on all new proposals for legislation and any other competition matters, but the opinions of the council are binding on the minister.

28. Competition advocacy is a tool to enhance voluntary compliance and policy coordination. Advocacy is a core activity, especially for young competition authorities

where stakeholders need to be informed of the existence and objectives of a new competition law, and their rights and obligations.

29. Competition issues may arise in the course of economic policy formulation and implementation. Therefore, competition agencies should sensitize policymakers on the possible synergies and/or tensions which may arise from certain policy measures, including but not limited to the creation and/or protection of national champions.

F. Relationship with sector regulators

30. Allowing private sector participation in a country's important sectors is creating increasing opportunities for and promotion of competition. As a result of technological advances, traditional sectors are converging with other sectors and the notion of what constitutes a natural monopoly is being revised. Despite these developments, however, a fair amount of government intervention has proved desirable, notwithstanding competition law. Competition authorities and sector regulators coexist under various conditions. Countries approach the question of regulated sectors differently, but some common choices include excluding some or all regulated sectors from the purview of competition law (e.g. Colombia) or awarding concurrent jurisdiction to the competition authority and the sector regulator over competition matters in some or all sectors (e.g. South Africa and the. United Kingdom). The variety of approaches can generally be classified into at least five permutations. The dominant pattern of distributing competencies between regulators and the competition authority is rarely one whereby competition authorities replace sector-specific regulators. Similar to competition authorities, it is desirable that sector regulators assume obligations regarding independence and accountability

31. Some areas of the economy remain susceptible to market failures and the role of the sector regulator remains relevant. See below. Despite a common goal, friction may arise as a result of differences in the prioritization of objectives and the methods used by sector regulators and the competition authority. Article 7 of the UNCTAD Model Law on the relationship between competition authority and regulatory bodies, including sectoral regulators, is one source of inspiration for governments grappling with this issue. The Model Law states that competition authorities should assess regulatory barriers to competition incorporated in economic and administrative regulations from an economic perspective, including for general interest reasons.

32. One of the key guiding principles that filters through all the generalizations listed above is that any particular form of regulation should be carried out at the level of governance consistent with regulatory effectiveness. Other principles that can facilitate this application are (a) principles that ensure access to the information necessary for making sound judgements (transparency); (b) the participation by all parties likely to be affected by a regulation (due process, e.g. competition advocacy); and (c) the elimination of unnecessary costs due to over-regulation (proportionality).

G. Privatization, concessions and competition policy

33. Economic reform in many countries includes the introduction of competition into markets with former government monopolies. There is a temptation to transform public monopolies into private ones. An important function of the competition agency is to advocate for competitive structures and competition-enhancing regulation. It is far easier to impose structural change – such as vertical separation and horizontal splits to create competitors – before privatization than afterwards. Private property owners will resist

value-destroying structural change. Thus, starting the reform process with structural change is key.

34. Competition law and policies are necessary to ensure that the potential benefits of privatization are realized. Competition issues need to be taken into account at the various stages of privatization, including its design, the award process and its execution, as well as in the regulatory framework for the markets concerned. Only if potential entrants have to compete against each other will they will be incentivized to offer more favourable conditions.

35. After privatization is completed, potential anti-competitive conduct should be constrained. In particular with respect to infrastructure services, concessions, for example, frequently confer a dominant market position. An infrastructure operator, whether public or private, has little incentive to lower prices or improve quality in such a situation. Competition law and policy, often combined with sector-specific regulation or concession contract terms, help to constrain anti-competitive conduct. Regulation and contract terms typically impose obligations with respect to quality, coverage and investments. Where competition in service provision is possible – as in mobile telephony – competitive pressure helps to maximize the benefits of private-sector participation in terms of investments undertaken, efficiency gains realized, quality and coverage of the services provided and the tariff level.

36. The design of privatization should allow for as much competition as possible. This means that the competition authority needs to get involved early in the process. It can do so by competition advocacy and by assisting in designing the structure of the privatization to maximize post-award competition. Advice on the most appropriate award criteria or the design of a public auction may be rendered by the competition authority, as well. In Chile, for example, the *Tribunal de la Defensa de la Libre Competencia* intervened in the award of seven licences for the Santiago–Lima air route. In order to enhance competition on that route, the tribunal obliged the concessioning authority not to award more than 75 per cent of the routes to the same bidder in a first round of the public auction. Only if no bidders participated in this first round would that limitation not apply to the second round. Advice on sector-specific regulation may also be required.

H. Public interest and competition policy

37. A number of jurisdictions have devised different procedures to outsource decisions relating to non-efficiency considerations, usually in the form of judicial (e.g. the United States) or ministerial powers to designate exemptions. Alternatively, other jurisdictions have procedures to import non-efficiency considerations in a sanitized fashion articulated in the competition law as public interest provisions that oblige the competition authority to either apply a specific public interest test (e.g. the European Union and South Africa) or grant the minister specific circumscribed powers (e.g. Italy, Jamaica, Singapore and the United Kingdom), frequently in respect of the review of mergers and acquisitions. In many cases, public interest provisions exist in some form or another, but the competition authority or the minister refrains completely from applying them (e.g. Italy) or they are seldom activated.

38. It is also important to recognize that decisions on competition law priorities are not necessarily one-off because countries often adjust their national laws or priorities in line with changing circumstances, including changes in Governments. In this context, some competition laws include a dispensation for the ministry responsible for the competition policy portfolio to issue directives from time to time in the form of general policy guidelines (e.g. Pakistan, Sweden and Zimbabwe). In some jurisdictions, successive ministers have refrained completely from exercising this dispensation (e.g. Zimbabwe).

I. Market size and regulation

39. A frequently cited argument relevant to developing countries and small economies (including developed countries) is that market-driven outcomes do not necessarily guarantee efficient and positive outcomes for consumer welfare because the origins of many competition problems in small markets are structural in nature. This argument reinforces not only the idea that there might be greater reliance on public interest provisions in competition laws in developing and small economies, but also points to the greater reliance on sector regulation with significant parts of the economy not yet open to free competition.

J. Informal sectors

40. In many developing countries, an important part of productive entities is informal. They are not registered businesses and they do not pay taxes. However, informal businesses often generate a significant portion of output in many sectors. This informality is partly attributed to the existence of cumbersome government regulations, including barriers to entry, and lack of access to infrastructure, banking training, or law enforcement. The inability to access the courts limits them from entering into commercial contractual transactions.

41. The extent to which informality affects competition law enforcement would differ from one competition authority to the other. In a majority of countries, competition laws apply to economic activity carried out by the informal sector. However, the application of the competition law may vary and the results may be diverse. Some competition authorities have taken enforcement actions against what they consider anti-competitive conduct of the informal sector. They have brought enforcement actions against firms that evaded taxes and thus competed unfairly with formal firms. However, enforcement actions by competition authorities to combat the informal sector remain a challenge.

42. To address the problems of informality and the design of a competition law, governments need to adopt strong policy measures for example, advocacy programmes aimed at communicating the benefits of operating in the formal markets. They need, among others, to identify regulations that restrict competition, strengthen tax collection and regulatory enforcement improving access to credit and procurement opportunities. This would enable informal firms to graduate to formal businesses where competition enforcement can be more effectively enforced.

K. Regional groupings and common competition rules

43. Regional economic integration in the developing is characterized by complex and overlapping memberships and subsets within certain groupings.

44. The emerging trend is that more and more regional groupings are looking for ways and means of developing regional competition rules and encouraging their members to enact domestic laws.

45. Decisions adopted by member States of a regional grouping may have cross-border effects. When enforcement is centralized, it may reduce or eliminate externalities. Therefore, there are economies of scale and transaction cost savings due to uniform application of common competition rules by supranational authorities acting as one-stop shops in dealing with anticompetitive cases.

46. There are concerns about the capacity to implement community competition rules. Despite political will at the regional level, institutional weaknesses, small size and the scarcity of human resources in some member States affect implementation capacity. For example, the Caribbean Community (CARICOM) Competition Commission, which was established on 19 January 2008, has nine of its member States that have yet to adopt a competition law. (Belize, Antigua and Barbuda, Dominica, Grenada, Saint Kitts and Nevis, Saint Lucia, and Saint Vincent and the Grenadines). Because they are very small islands with limited human and financial resources, they decided that the optimum size for a competition agency is a subregional institution representing the Organization of Eastern Caribbean States within CARICOM.

II. Assessing the impact of competition law and policy enforcement on development

A. Impact of competition policy and its enforcement

47. Developing countries are beset by a number of barriers to competition. There is an urgent need for an effective competition law and policy in these countries. However, owing to various market characteristics and legal and enforcement difficulties, it is much harder to implement competition law and policy in developing countries than in developed countries. Some of these factors include large informal sectors, problems relating to small size and large barriers to entry, difficulties in instilling a competition culture, and capacity and political economy constraints. It is important for each country to tailor its implementation of evaluation initiatives to promote competition while operating within these constraints.

48. These features suggest that uncompetitive markets are an even greater problem in developing countries. The need for effective competition law enforcement is great, but there are serious constraints on effective policy implementation.

49. Evaluation of the impact of competition agency activities can assist in addressing the more severe political economy problems, thereby helping provide legitimacy for the policy system. On the other hand, capacity constraints within developing countries hamper the proper performance of these evaluations. Nevertheless, when conducted appropriately in these contexts, evaluation can help to provide insights into the country-specific constraints to competition in these jurisdictions arising out of the characteristics listed above, as well as suggesting potential remedies.

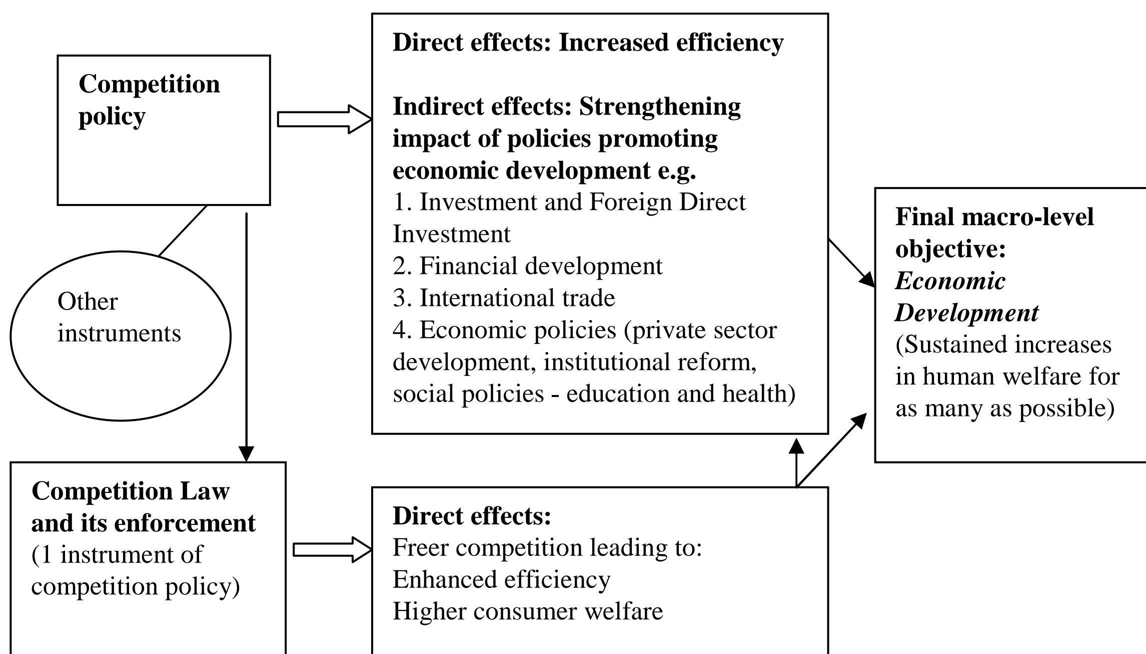
50. Consideration of the various above-mentioned criteria may be an important factor in developing country objectives. The priorities of developing countries may be quite different from those of developed countries. However, there is a risk of asking too much, when other policy instruments may be the most appropriate tools for achieving certain ends. This strengthens the case for evaluation. It is necessary to understand the effects of a country's programme of competition law enforcement in order to determine the potential and limitations of competition policy.

51. It is difficult to assess the impact of regulatory enforcement action on social phenomena as wide-ranging as compliance or non-compliance with competition laws. Empirical research clearly shows that a range of factors beyond enforcement are likely to affect levels of development. It is therefore difficult to disentangle the impact of

enforcement action on development from other factors that affect economic development. Even more difficult is the fact that "development" itself is a complex concept.[1]

Figure 1

Relationships between competition law, competition policy and economic development



52. There is an argument that "competition policy is both a direct contributor in its own right, as well as an indirect contributor through the enhancement of other policies". Figure 1 shows that CLP can have direct effects on economic development. One of the criteria by which one could judge the success of an enforcement action is the extent to which it helps build a shared understanding between regulator and "regulatee" of what compliance means and how it should be put into practice. In other words, the compliance impact of enforcement action cannot be judged merely by whether the regulator wins a judgment in court. It is argued that enforcement action must be judged by the extent to which it helps bring business norms and practices into alignment with regulatory expectations. Indeed, enforcement action is most successful in terms of its "compliance" impact, if it achieves not only alignment between business and regulatory understanding of what a particular regulatory rule requires in a particular situation but also a shared understanding of, if not commitment to the goals and purposes underlying the relevant regulatory rules. A shared understanding of the goals and purposes of a regulatory regime is more likely to lead to the same interpretation of the rules in different circumstances, and a shared commitment to those same goals creates an opportunity for habitual compliance.

53. The first set of criteria on which one might choose to focus is "input" criteria: These refer to the set of managerial processes and systems by which a country implements its competition regime. In this respect, one might choose to focus on case selection or staff turnover, etc., or other *sui generis* measures of agency effectiveness the authority determines to be significant.

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[1] Economic development is a process that involves increasing human welfare over time which necessitates among other things, increasing the quantity consumed, quality and variety of consumer goods over time.

54. Trying to weight the various input criteria by their relative importance requires an understanding of how the various criteria relate to effects on economic outcomes. There is a small body of literature that attempts to devise means of measuring the institutional capacities of competition authorities.

55. Another important criterion for evaluating the effectiveness of a competition policy authority is to compare the outputs it achieves with the stated goals of its competition policy regime. This is normally set out in the preamble of the legislation enacting the country's competition regime. Accordingly, one yardstick for evaluating the effectiveness of the competition agency would be to examine continuously whether the stated goals of the legislation are being met by the authority's enforcement activities. This idea was also taken into account in the case of Tunisia, which states that effectiveness can be measured by ascertaining to what extent the authority has been able to fulfil its mission. Consideration has to be given to the impact that the authority's existence actually has on the competitive situation in the country. If the mission is to improve competitiveness and the market is still dominated by a few companies, it would indeed be legitimate to question the authority's effectiveness.

56. Accordingly, an agency might instead choose to focus on "output" criteria, which contain some kind of attempt to include quantification of the success of the interventions such as, for example, an effort to quantify the cost savings arising from successful investigations and competition law infringements deterred.

57. The types of study an authority might undertake in this regard can vary from back-of-the-envelope calculation to detailed econometric analysis. The appropriate extent of quantification varies with the importance of the case and the capacity of the authority, but this does not undermine the fact that some measure of quantification is to be welcomed, if only because it gives the authority an understanding of the orders of magnitude involved. Even a brief calculation can feed into the authority's future enforcement priorities and strategic planning.

58. For example, the EC has reported in its "Merger Remedies Study" that overall effectiveness can be observed by looking at the remedies imposed, as this can reflect the degree of efficiency in reaching the expected results. Here, effectiveness can be quantified in terms of the percentage of remedies that have attained their intended objectives. The study showed that 57 per cent of the remedies analysed were fully active, i.e. they had fulfilled their intended objective, 24 per cent were only partially active and seven per cent were ineffective, as the intended objective was not satisfied.

59. With this type of approach, one would try to estimate the benefit of the competition regime by summing the positive outcomes of individual cases. However, this excludes the deterrent benefits from the possession of competition law, which can be quite sizeable. On the other hand, it also excludes the number of pro-competitive actions that were not undertaken out of fear of wrongful prosecution by means of the competition law. Hence, in jurisdictions where the application of the law is uneven and transparency of decision making with respect to competition is not clear, it can be very difficult to quantify the impact of competition by means of this "bottom-up" approach.

60. Similar difficulties arise when one tries to estimate the benefits of competition law enforcement at the country level. Again in this instance, it is difficult to isolate the impact of competition law and its enforcement. This is certainly extremely difficult to do at the level of the country competition authority, as many factors may affect the mark-up or level of manufacturing productivity, aside simply from the effectiveness of the competition regime. Nonetheless, there are interesting insights to be gained from the study of partial equilibriums, and suggestive evidence can be adduced from such studies of specific interventions to support its positive impact on economic growth, if not quantify it exactly.

61. It might be difficult to assess the effectiveness of certain competition authorities due to their recent establishment and the limited number of cases that have reached the execution stage. This is the case with Tunisia, for example, where the importance of objective evaluation of the work carried out by the authority was underscored. This objective evaluation should be linked to certain specific criteria such as, for example, the time-frame in which the cases are handled and the number of undertakings that have been brought into conformity following an intervention by the competition authority.

62. If a competition authority has been able to make recommendations or submit proposals to the Government concerning competition policy issues that have had a positive impact on the economy, this is also an indication of effectiveness. The competition authority in Tunisia has, for example, played a proactive role and paved the way for various reforms connected to competition legislation.

63. Another potential criterion for determining whether the authority is effective, or is at least perceived to be so, is to consider the attitude of important stakeholders. It is important to note in this respect that determining the relevant "stakeholders" (or at least determining what weights one assigns to their relevant interests) is to some extent determined by the stated goals of the legislation – if the competition legislation gives precedence to consumer interests then this group may be the primary stakeholder. If promoting or protecting small businesses is the purpose of the legislation, then this group is given priority, and so forth.

B. Review of selected empirical studies

1. Monopolization and abuse of dominance

64. A few studies on competition in developing and developed countries are cited in a 2002 UNCTAD working paper. One study using persistence of profits and another study using firm turnover (entry and exit) indicate that the level of competition in developing and transition economies is about the same as in developed economies. A review of manufacturers in developing countries "did not support the notion that LDC manufacturers are relatively stagnant and inefficient", again undermining the idea that competition is less intense in developing countries.

65. The 2007 Global Competitiveness Report pointed out that nations' prosperity increases with their productivity. The report contained indicators that were correlated with per capita gross domestic product (GDP). In summary, for low-income countries, mobile phones, high-quality electricity supply, Internet access, trade barriers, other infrastructure and local competition affect per capita GDP. For middle-income countries, these factors plus patents, the absence of market dominance by business groups, and the effectiveness of antitrust policy affect per capita GDP.

66. The Organization for Economic Cooperation and Development (OECD) has said, "Developing and transition economies may have structural weaknesses that make them particularly vulnerable to private anticompetitive conduct. The following factors, where they are found, are likely to have a negative impact on competitive pressure:

(a) Greater proportion of local markets insulated from trade liberalization measures;

(b) Limited access to essential inputs;

(c) More limited distribution channels;

(d) More dependence on import (basic industrial inputs) and/or exports (for growth);

(e) Greater incidence of administrative/institutional barriers to imports;

(f) Weak capital market."

67. Transition from State monopoly to competition may generate further scope for exclusionary abuses of dominance. Also according to OECD, "A former monopolist being challenged by new entrants may have 'inherited' advantages from the former position, like a strong financial position, control of certain network facilities, connections and political support, or established relations to suppliers and customers. Such a dominant firm or 'incumbent operator' may find many ways to make life difficult for new entrants and in the end exclude competitors effectively. In many countries that have liberalized markets, the competition law enforcer finds itself inundated by endless cases of alleged abuse of dominance resulting from the imbalance between a former monopolist and new entrants." The Indian competition law, article 19 (4)(g) indicates awareness of this issue, a factor that may be considered in determining whether an enterprise that enjoys a dominant position is "monopoly or dominant position whether acquired as a result of any statute or by virtue of being a Government company or a public sector undertaking or otherwise".

68. Dutz argues that competition authorities in developing and transition countries should focus their anti-abuse of dominance efforts on abuses that foreclose access to services that are essential to business. The idea is to reduce barriers to new entrepreneurs and SMEs. Examples of local essential inputs are "real estate, banking, transport, distribution warehouses, communications and professional business services".

69. Fox states that, "Anti-competitive practices are rife in areas of physical and business necessity, such as milk, soft drinks, beer, chicken, sugar, cotton, paper, aluminium, steel, chemicals (for fertilizer), telecommunications including mobile services, cement and other construction materials, transportation including trucking, shipping, and port access, industrial gases, banking, insurance, coal and electricity. Many of the practices are local, many are facilitated by the Government, and many others are offshore, resulting in inbound restraints." She argues that intervention against entry-blocking or discriminatory conduct by State-owned or State-privileged enterprises may have more benefits and fewer costs than anti-abuse intervention in developed countries.

2. Hardcore cartels

70. A striking feature of these cases is that many are clustered within a few economic sectors. For example, it seems that cement cartels exist almost everywhere. It is a rare country that has an anti-cartel programme and has not prosecuted one or more cement cartels. More generally, construction materials and construction services seem to be fertile ground for cartel operators.

71. The reasons for the high incidence of cartel activity in these sectors are fairly obvious. Construction materials, especially cement, are homogeneous products. Producers are differentiated almost entirely by price. This homogeneity makes it easier for sellers to agree on the terms of a cartel agreement. Importantly, these products and services are often sold by means of bids or tenders to government or public bodies. These buyers are particularly vulnerable to bid rigging activity, as is discussed further below.

72. There have been a relatively large number of cartel cases and investigations in the petroleum sector, in particular that of petrol (gasoline). There may be several reasons for the high incidence of petrol cases. Petrol is an important consumer product – for many, a necessity. Also, petrol prices have generally risen in the past few years, and while this is doubtless mostly because of increasing demand, the suspicion exists that cartels are at least partly responsible. Perhaps most important, current retail petrol prices are readily visible. This could facilitate an agreement among petrol sellers. It also could alert both consumers and competition officials to the possible existence of a cartel.

73. But here a word of caution is in order. It is axiomatic that mere simultaneous movement of prices, especially for a homogeneous product such as petrol, is not by itself sufficient to prove an unlawful agreement. Such price activity could be equally consistent with active competition. In almost all countries, there must be more evidence than just parallel pricing to support a cartel prosecution. Indeed, in some countries, investigations of possible price fixing in petrol have failed because such additional evidence was lacking

74. Food products also seem to be disproportionately represented in the cases described in this report. Again, a combination of factors may be responsible. Like petrol, food is an important consumer product. It can be a homogeneous product, especially at the producer/processor level. Price information may be more readily available to both sellers and buyers in this sector. Other sectors that appear frequently in cartel cases include transportation services and professional services.

75. But the most frequently occurring common feature in the cases above is bid rigging on sales to government agencies. Government purchasing agents may not recognize suspicious bidding activity, and procedures that they use may lack safeguards against bid rigging. In some cases, there is even the danger that procurement procedures might be subject to corruption. The openness of public procurement can also facilitate the formation and monitoring of cartel agreements.

III. Lessons for the future: how to improve competition policy formulation and enforcement in developing countries and other countries

76. Ways to improve competition policy formulation and enforcement include:

(a) **Develop a tailor-made competition law and policy and its enforcement framework.** Developing countries are beset by a number of barriers to competition. There is an urgent need for an effective competition law and policy in these countries. However, owing to various market characteristics and legal and enforcement difficulties, it is much harder to implement competition law and policy in developing countries than in developed countries. Some of these factors include large informal sectors, problems relating to small size and large barriers to entry, difficulties in instilling a competition culture, and capacity and political economy constraints. It is therefore important for each country to tailor its competition law and its implementation within these constraints;

(b) **Work to develop a competition culture.** The themes developed above suggest several ways in which competition law enforcement can be strengthened. First is the development of a “competition culture” – an understanding by the public of the benefits of competition and broad-based support for a strong competition policy. The process is ongoing; it requires communication with all parts of society – consumers, businesspeople, trade unions, educators, the legal community, government and regulatory officials, and judges – about the benefits of competitive markets to them and to their country’s economy;

(c) **Encourage complaint submission.** Educated consumers and businesspeople will be more alert to possible anti-competitive activity and more willing to report it. As was noted above, complaints to the competition agency have been, and in developing countries are likely to continue to be, the most common source of information about previously unknown cartels. It must ensure that the identity of complainants is protected as confidential information to the fullest extent possible;

(d) **Begin to establish a leniency programme.** The word “begin” is important. One cannot expect the mere creation of a leniency programme to produce immediate results for the agency. The competition agency must first establish credibility – that it will discover

and successfully prosecute cartels, and that it will severely punish those that are prosecuted. When this credibility is established, properly structured leniency programme will succeed;

(e) **Focus initial investigative efforts on sectors where cartel conduct is most likely.** There is now strong evidence that, while cartels can occur in any economic sector, they are more likely to occur in some sectors than in others, especially in the case of developing countries. The new competition agency should focus its efforts on those sectors. One area in which sector studies could be fruitful, however, is public procurement. A study of bidding behaviour in situations where bid rigging is suspected might identify patterns suggesting customer allocation or bid rotation. Such studies should be conducted with the assistance of a knowledgeable procurement official who can interpret the data correctly;

(f) **Begin to impose strong sanctions against cartel conduct.** An indispensable element of a successful anti-cartel programme is an aggressive sanctioning policy. Sanctions can take several forms, including administrative fines against businesses and natural persons; criminal sanctions, including fines and imprisonment; and recovery of compensatory damages by victims of a cartel. Administrative fines against businesses are the most common. Pecuniary sanctions should be severe enough to eliminate a cartel's gains. Consequently, there is a growing awareness of the need to also assess sanctions against culpable individuals in cartel cases. If they face personal sanctions, whether imprisonment (in a minority of countries) or large fines, they have additional reasons not to participate in cartel activity;

(g) **Educate the public about the harm caused by cartels.** Countries new to competition law enforcement probably cannot immediately begin to impose strong sanctions in their first cases. Some business operators will have been unaware that their conduct was unlawful, or formation of the cartel may have predated the enactment of the first competition law. Courts may be unwilling to approve strong sanctions when they are unfamiliar with competition policy or competition cases. Building support for strong sanctions in cartel cases requires a programme of education regarding the harm that cartels cause;

(h) **Engage in international cooperation in the enforcement of competition law effort.** The international competition community is working on means of achieving greater cooperation in fighting these secret, multinational agreements. But the effort goes well beyond that. International organizations, including UNCTAD and OECD, have long been active in studying and reporting on hardcore cartels. Also, for the past seven years, representatives of the competition agencies have met annually to discuss anti-cartel enforcement techniques. The International Competition Network has embarked on a programme to address the challenges to anti-cartel enforcement posed by international and domestic cartels. Developing countries will be limited, if only by resource constraints, in their ability to participate in these international forums. But almost the entire work product generated in these forums is publicly available, usually on the Internet. These resources are a rich source of information for the less experienced competition agency;

(i) **Work to develop a relationship with the courts that will hear appeals of cartel cases.** It is inevitable that, as a competition agency becomes more active in prosecuting cartels and other violations of the competition law, some of its cases will be appealed. Experience across countries indicates that it is almost as inevitable that the agency will suffer setbacks in some of these appeals. Competition cases are unique in many ways, and judges will not have had experience with them. Initially, they will tend to avoid deciding cases on their merits; instead, they will concentrate on procedural issues, with which they are more familiar, and reverse some cases on that basis. In particular, in cartel cases, they may be reluctant to uphold large fines assessed by the competition agency;

(j) **Conduct peer reviews.** UNCTAD's Voluntary Peer Review on Competition Policy is dedicated to enhancing the quality and effectiveness of the competition policy enforcement framework in developing countries and economies in transition. It involves the scrutiny of competition policy as embodied in the competition law and reflects on the effectiveness of institutions and institutional arrangements in enforcing competition law. By agreeing to show its work to others, a country/institution that volunteers for a Competition Peer Review engages in a self-assessment that helps pinpoint strengths and weaknesses in an environment that allows for non-adversarial external participation. The inclusive nature of the consultations boosts the confidence of other stakeholders in the reviewed institution and signals an outward rather than inward orientation.