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Competition Policy and Regional Trade Agreements*

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DITC Working Paper

Competition Policy and Regional Trade Agreements (RTAs)

Regional trade negotiations have been taking place during the last 20 years at national, regional and international levels. The number of RTAs aiming, inter alia, at promoting cooperation on competition policy has also increased significantly in the same period. In particular, of the around 300 bilateral and regional trade agreements (RTAs) in force or in negotiation, over 100 include competition-policy related provisions. About 80% of the over 100 have been negotiated in the last decade and are part of a trend for ‘deeper’ RTAs which often include liberalize trade in services, investment, and other trade-related provisions.

What are the reasons for including competition law and policy provisions in RTAs involving developing countries?

It is widely accepted that the aim of competition law and policy in an RTA is to ensure that the benefits expected from trade liberalization of intra-regional trade are not nullified by restrictive business practices undertaken by private firms. Regional trade liberalization alone can have strong pro-competition effects but it may not by itself eliminate the propensity of firms to engage in anti-competitive practices. Trade liberalization can actually make collusive actions among intra-RTA firms even easier, at the expense of third-country firms, leading to more trade diversion. This argument suggests that, as in other instances, in RTAs anti-competitive private barriers can easily replace governmental barriers to trade. Thus, even if one believes that RTAs are beneficial, countries may not be able to derive full benefits without complementary competition-related provisions.

Developing countries, RTA members or not, are particularly vulnerable to intra-regional anticompetitive practices. They have generally smaller markets (both in terms of the quantity and range of products) that could be more easily abused by dominant companies from RTA partners. This is particularly true for in those developing countries without a competition law or without resources and expertise in prosecuting intra-regional anti-competitive practices, such as international cartels.

The inclusion of competition-related provisions (CRPs) in RTAs, particularly those signed by developing countries, is also justified by the fact that competition law plays a more important complementary role to trade liberalization than in developed countries. In less mature markets, as is the case of many developing and transition economies, given the inadequacy of business infrastructure (poor physical infrastructure, dysfunctional legal and regulatory frameworks, legacy of excessive state intervention and weak governance, and so on) there is a much greater proportion of ‘localized’ markets and ‘non-tradable’ products. Furthermore, developing country trade is constrained by more limited distribution channels and other public and private barriers that cannot be disciplined by import competition. Therefore, merely removing conventional trade barriers among RTA partners may not necessarily lead to increased trade, in the absence of complementary competition provisions (either as competition advocacy or enforcement actions).

What are the main types of such competition-related provisions?

What seems to emerge at this stage is that countries have been eager to ink an ever-increasing number of RTAs containing CRPs, with different levels of ambition and among countries at various levels of development. In this publication, RTA competition provisions were classified in several ways encompassing a wide spectrum of potential obligations. Such CRPs may refer to the adoption, or implementation of national competition laws. There may also be provisions for cooperation or coordination of activities by competition law enforcement bodies. At the deeper end of obligations, dispute resolution or consultation mechanisms could be provided for, or the creation of a supra-national authority that can apply competition law directly on private entities within the RTA (such as the EU, COMESA, and the Andean Community).

What has been the experience of competition agencies of developing countries with RTAs?

Despite the various countries' eagerness to sign RTAs with competition provisions, there is very little experience concerning their implementation and their effectiveness with regards to improving competition. Although RTAs, and more recently, agency-to-agency agreements (ATAs) have become a popular means of formalizing cooperation between competition authorities, the existing evidence does not always point to a "one size fits all" approach. Can we put in a positive way?? Sometimes RTA cooperation on competition rules may be useful but informal cooperation may be more effective as shown in many cases (i.e. ICN) and countries are keen to pursue this type of cooperation. Also, approaches used by developed countries to deal with competition issue at regional level may not be relevant for RTAs among developing countries. For instance, the EU modernization package may not be readily applicable in other regions such as the Andean Community, UEMOA, Mercosur, or Caricom.

Yet, one common trend that seems to emerge is that RTAs are a means of opening communication channels, and that these channels are subsequently expanded by competition authorities until a satisfactory level of cooperation has been achieved. Also, it is important to note that the "domino effect" of RTAs tends to spread competition legislation to new countries and that this increases the opportunities for cooperation and experience sharing among competition authorities.

How costly is it to implement CRPs contained in RTAs?

Cost-benefit considerations for competition provision obligations assumed within RTAs can be very complex. Both costs and benefits are hard to estimate. Costs will essentially depend on human resources and expertise that are needed to implement the various CRPs. Benefits stem from the ability to use CRPs in RTAs to curtail intra-RTA anticompetitive practices, such as international cartels. However, these potential benefits are difficult to estimate as the projected costs of anti-competitive practices and the probabilities of successfully addressing them are speculative. Nevertheless, if one uses the examples of international cartel costs (e.g. vitamins, heavy electrical equipment and graphite electrodes) benefits from the effective implementation of such CRPs could equal up to 1.2% of the combined GDP of affected countries.

But the benefits of signing onto a RTA's competition provisions may extend beyond detection and correction of anti-competitive practices. Companies operating within a region that apply RTA competition provisions may have less costs of compliance. For instance, a

RTA's M&A provisions might clarify costs and time required for an approval of a merger. Several RTAs are incorporating 'one-stop shop' approaches to merger analysis, for example the EU and COMESA. Such clarity and transparency may encourage mergers and acquisitions that improve efficiencies, better allocate resources and reduce consumer prices. The paradox however is that very few RTAs contain provisions relating to mergers, which is another issue for policy consideration and further research.

Are countries receiving any special and differential (S&D) treatment from a trading partner that is more developed?

At any rate, for developing countries, S&D treatment may help achieve a proper balance between costs and benefits. The UN Set recognized the need for S&D treatment in the area of competition policy as early as 1980 and UNCTAD has continued to endorse special measures for developing and LDCs at each subsequent Review Conference of the Set. The problems addressed by S&D provisions within competition clauses are the same as those that UNCTAD has flagged many times, particularly the need for policy space to ensure that parties at different levels of development benefit from non-reciprocated provisions in their favour. The appearance of S&D provisions within RTAs shows, at minimum, that weaker partners feel that there is a necessity for S&D treatment and that it is beneficial to them. A delay, exemption or technical and financial assistance in implementing a RTA's competition obligations would reduce the effective cost. Developed countries are offering technical assistance willingly in the framework of a RTA . It is hoped that with this technical assistance, developing countries without a domestic competition law may be able to establish the domestic legislation and related authorities more cost-effectively.

Policymaking requires coherence for effective implementation

As mentioned earlier, there is a clear link between trade policy and competition policy. Competition policy sets the parameters for the intensity of competition between producers within the national market including foreign investors, while trade policy sets the rules for competition from foreign-based suppliers, including those owned in the home country. Trade negotiations are seen as seeking to reduce the use of the anti-competitive instruments. However, certain trade instruments such as anti-dumping and safeguard measures, although designed to correct problems arising from alleged distortions in trading partners, can also have anti-competitive effects. new set of issues comes into play when regionalism leads to the establishment of a common market or economic union. When investment and labour issues are taken into account, regional trade and competition provisions may lead to conflicting objectives or adverse welfare effects.

Policy coherence becomes a key ingredient for an efficient and cost effective control of anti-competitive practices. To achieve their trade and competition objectives RTAs need frequent monitoring and benchmarking against other countries. In all cases in which the RTA needs to be rethought, a possible mechanism is the inclusion of an evolving or revision clause designed to give flexibility to the parties to jointly amend their RTA. Circumstances can change: new economic conditions, technologies, techniques or industrial organizations can be introduced. Such may require policy makers - both trade and competition - to reconsider the role and objectives of their competition provisions within their RTAs.

The way forward

UNCTAD work on the relationship between Competition and RTAs pointed to one clear conclusion: the available evidence shows that countries are eager to ink RTAs with CRPs but are far less eager to implement them. This weak implementation record can be partly explained by the fact that RTAs with CRPs is a relatively new phenomenon. The history of regional integration has shown that ‘deep integration’ rules, such as competition provisions, need time to fully materialize, particularly in RTAs involving developing countries. However, expeditious progress can only be expected if strengthening of implementation capacity in developing and transition RTA members is accompanied by reinforced commitment from developed countries to effectively address the main competition-policy concerns of their trading partners.

There are many important issues that still need to be tackled. For instance, anti-competitive practices in the infrastructure services (e.g. telecom, distribution services) may have negative spill-over effects on market access opportunities for developing countries in other sectors including trade in goods. Furthermore, as the evidence in this publication suggests, it would be interesting to assess why the more informal arrangements (bilateral or otherwise) cooperative arrangements are possibly more effective than textual obligations of RTA competition provisions.