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SOME REFLECTIONS ON THE EFFICIENCY AND EFFECTIVENESS OF MULTI-JURISDICTIONAL ANTITRUST ENFORCEMENT IN EUROPE

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One of the least questioned areas of government intervention is undoubtedly competition policy.¹ Going back to the Sherman Act in 1890 in the US and the European Economic Community Treaty nearly 50 years ago, competition policies have a long-standing tradition in economic life on both sides of the Atlantic. But in Europe recent decades have led to an even larger deployment of resources in the area of antitrust enforcement as a result of the devolution of some of the activity from the European Community to the level of the member states. In this period, the so-called “national competition authorities” (NCAs) were either started or have increased their effectiveness, whereas the above-mentioned devolution did not reduce the scope of the European competition authority. Overall, this has led to an increase in resources devoted to antitrust monitoring.

This brings up a different but related issue: even if the welfare-enhancing effects of optimal competition policies are understood and accepted, the question now is whether the resources allocated to these policies are deployed in an effective and efficient manner. Especially on the European scene, with its fragmented multi-jurisdictional enforcement, it is possible that several impediments to an optimal organization of competition policies exist. If that is the case, it is conceivable that real world competition policies in Europe do not deliver the welfare improvements that their blueprint design intended.

This contribution explores how effective and efficient some of the national competition authorities operate by reporting on recent research that has focused on particular aspects of this general question. Needless to say, given the absence of relevant

research findings some aspects that are possibly problematic for the effectiveness and efficiency of policy will not be elaborated in detail. Also the coverage of countries in which effectiveness and efficiency could be investigated has been limited. Instead, we focus on small open economies, in particular Belgium and The Netherlands, for a variety of reasons such as the closeness to actual policy-making as a member of the authority, the research done on these countries and recent availability of official audit reports on both the Belgian and Dutch antitrust authorities.

Multi-jurisdictional antitrust enforcement

The challenges to a multi-jurisdictional organization of competition policy are many, and outnumber the obvious advantages. In the area of merger review, it is immediately clear that a cross-border operation not handled by the EU has to be cleared by at least two competition authorities. This leads to:

- duplication of administrative costs, both for the companies involved and society as a whole;
- too strict enforcement of merger regulation and errors of type II.²

Both points deserve further explanation. It is not hard to see that preparing a file for two competition authorities requires more effort than for one. The additional red tape costs for the company are probably somewhat less than double when preparing the file for the second authority.³ But the administrative cost for government is not less, since it is simply not possible to rely on decisions taken by a foreign authority, given the difference in the objective function.⁴

In small open economies such as Belgium and the Netherlands, this has led to the criticism that it is not

¹ An opposing view is given in Crandell and Winston (2003). This viewpoint is contested in turn, by Connor (2004) and others.

² These include the disapproval of a merger that is welfare-enhancing, as opposed to errors of type I, which occur when a merger that reduces welfare is not blocked by the authority. This point was already raised by Evenett (2006).

³ One could say there are economies of scale in reducing additional authorities, given that a substantial element of costs is data gathering. See, however, Van Cayseele (1989) for an early contribution on subadditivity of cost functions for dealing with government agencies in the case of pharmaceutical companies registering prescription drugs.

⁴ Smets and Van Cayseele (1991) even show how to a large extent the objective functions are antagonistic when they constitute the traditional sum of producer and consumer surplus, and the merged entity repatriates profits, post-merger. Even when the NCAs look at consumer surplus (a less accepted criterion), the situation in both countries can be quite different, and each agency will need to engage in a full review of the submitted merger file.

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entirely clear what the contribution of the agency is. Furthermore, it is felt that this authority merely triggers government spending to enforce a goal that is perfectly executed by the market, given the openness of the economy. The next section will investigate this argument in detail, presenting empirical evidence on the matter.

The second point raised involves a too strict attitude vis-à-vis cross-border mergers. Since both jurisdictions need to clear the operation, the review process works like the Sah-Stiglitz hierarchy (see Van Cayseele (2004), especially in the context of bank merger approvals). The upshot is that when each of the agencies has its own objective function, the slightest incompatibility will imply a blocking of the operation. This is easy to see in the case of bank mergers when the merged entity acquires market power but also takes more precautions against liquidity shocks. When both the NCA and the Central Bank need to approve of merger, it will never pass, since the NCA (in the absence of pronounced efficiency gains that allow a decrease in the loan interest rates) will not applaud the consequences of increased market power, although the Central Bank is better off as a result of the increased precaution taken against liquidity shocks. A similar effect is in play when cross-border mergers are involved: it is sufficient that the operation cannot be tolerated by one single agency, because, for example, the loss of consumer surplus in that country is substantial, resulting in the operation being blocked even if it is welfare-improving in many other countries.

Less documented, if not entirely absent in the discussion on multi-jurisdictional antitrust enforcement is the fact that widely different regulations can create distortions in the pattern of industry evolution. The issue here is not the cost of cross-border mergers but the costs and possibilities of within-border mergers. It is well-known among industrial organisation and antitrust experts that the toughness of competition policy may have a strong impact on the long-run outcome of an industry. Taking a historical perspective, Bittlingmayer (1985) was the first to document how antitrust policy in itself could have been an explanation for a particular merger wave. Perhaps the best illustration in this respect was documented by John Sutton (1998) in what he has called “the fate of Ilford”.

A few decades ago, the market for photographic paper and film was dominated by a few players,

Agfa-Gevaert (Belgo-German), Kodak (US) and Ilford (US). Today, lagger Fuji has taken over first place, although all these companies are struggling to survive in a world where the process of making pictures has largely shifted from a chemical to an electronic one. But Ilford began to flounder much earlier, as British authorities opposed the possibility of growth via consolidation in the UK. The final result is a company which for more than three decades has no longer been active on the international scene and which has specialized in a particular niche. Agfa-Gevaert and Kodak did not face this particular constraint and succeeded in positioning themselves on the global market.

Therefore, the different enforcement of antitrust laws by different jurisdictions in the end implies a different evolution of industry. Below, we illustrate some differences in the various merger review processes. It is still too early to test empirically whether the documented differences have a role in explaining variations from industry to industry. But the differences are sometimes so remarkable that it is hard to believe that they have no consequences.

Competition policy in a small open economy

Critics of competition policy, and in particular merger review, have argued that the open character of the Belgian and Dutch economies is sufficient to ensure that a merger will not lead to the creation of market power. To use economics terminology, markets in small open economies are contestable. Imports (or the threat of imports) are a perfect substitute for competition policy.

Econometric analysis of price-cost margins indicates that the picture is less clear-cut. Konings, Van Cayseele and Warzynski (2001) estimate price-cost margins and explain them by investigating the effect of increased import penetration or competition policy enforcement. This is done using a panel data set of over 20 industries in Belgium and the Netherlands. The results show very mixed findings.

For Belgium, downward pressure on price-cost margins doesn't seem to come from competition policy at all, but import penetration is an effective disciplining device. For the Netherlands the exact opposite is true: imports hardly have an effect, whereas with the enforcement of the 1999 competition law, most industries have entered a period of decreased margins. How can this be explained?

There are several possible explanations. The first merely says that the Belgian anti-trust authority was not a very effective one. This might be a quite plausible explanation: at one point in time the Belgian authority even went on strike to point out the tremendous lack of manpower to deal with all cases properly. Other explanations are equally plausible, however. The starting position between the two countries could be different. In Belgium, competition policy replaced an elaborate system of price controls. As economists, we immediately question the effectiveness and efficiency of those controls and we do so for good reasons. But they could have had an effect, especially in a relative sense, as compared to the Netherlands where such price controls had been abolished much earlier. To some Dutch economists, the Netherlands in the previous low-competition era was called even “a cartel paradise”. So it could have indeed been the case that due to anti-competitive behaviour, the initial mark-ups were higher in the Netherlands, and especially the fear of getting caught and fined led Dutch industry into a period of more moderate margins.

This however still does not explain the different effect imports have. Here again we only can put forward plausible arguments, without the pretension of offering a final answer. One element that certainly plays an important role is the composition of the outputs that are aggregated in one and the same industry. Belgium tends to be more specialised in the manufacturing of bulk goods and semi-finished components (Drèze 1960). The Netherlands manufacture more finished goods, sold under their own brand names. In more modern terminology, Belgium is more into B2B and the Netherlands in B2C.

This implies that Belgian manufactured goods are sold on markets where the model of price competition in homogeneous goods (the Bertrand model) prevails. Dutch manufacturing then sells more in niches, where important elements of non-price competition also operate, or the market works along the lines of models of product differentiation.

Increased imports of these goods to Belgian territory then indeed imply that buyers located further inland in Europe have a choice: they can buy the commodity manufactured in Belgium, or the same good imported through Belgium.

This does not necessarily hold to the same degree for the Netherlands, given the differentiated nature of the

goods. The Netherlands, in addition, are more active in trading, where imports do not necessarily lead to more competition with their own manufactured output. On the contrary, the imported component could provide a welcome complement that makes the bundle, including both the domestically manufactured and imported goods, a more attractive one.

Regardless of the explanation for the findings, the facts remain. And these facts are that even for small open economies neither import substitution nor competition policy need to be effective in improving allocative efficiency. It all depends on which factor is (most) effective. In fact, they appear to be complements because our initial findings indicate that where import penetration works better, antitrust enforcement has less impact, and vice versa.

Are there really 50 different ways to implement competition policy

The previous section illustrates that one cannot immediately dismiss competition policy, not even for small open economies. But shouldn't these policies be similar at least to some extent?

It is common knowledge that even conceptually there are major differences regarding the approach followed in setting up an antitrust policy (Borrell 2005). Some countries rely on ex ante merger review, while others control ex post whether competition has been restrained. Some rely on administrative actions, others on the judiciary regime. Additionally, there is a discussion in Europe on whether one should rely exclusively on public enforcement or on public and private enforcement.

Not long ago, some economists maintained that within Europe the differences in antitrust policies were not that great, given that all the national regimes were copies of the articles in the EEC Treaty. They were clearly misguided. In a qualitative survey of the institutional features of antitrust policies in European member states (Belgium, Germany, Italy and the Netherlands), Van Cayseele, Sabbatini and Van Meerbeeck (2000) showed that even within systems that heavily rely on an administrative, exclusively public and ex ante system there are pronounced differences.

And even if the regimes are basically the same, the practical implementations might be very different.

To show this, De Loecker, Konings and Van Cayseele (2007) have focused on ex ante merger review in a number of European countries. The differences are striking, since to start with not all competition laws use the same criteria to determine whether a merger should be notified. In some countries, two criteria are used, for instance individual and combined domestic sales. Other countries introduce combined worldwide sales. Still other countries add criteria, such as market shares or total assets.

Furthermore, even when two countries use the same set of criteria, like individual domestic and combined worldwide sales, the thresholds vary substantially. Compared to France, the Netherlands has twice the level of domestic sales as a threshold. But it already triggers review at 75 percent of the level of worldwide sales. So the Netherlands favours larger players on the home market and is stricter in its handling of export champions, at least in comparison to France.

Perhaps the most astonishing fact for an industrial economist is that in all countries the criteria are the same for each and every industry. But industries vary widely in respect of the prevailing scale economies, volume of sales, etc. Hence, it becomes possible that in certain sectors, each and every company individually exceeds the threshold for merger review, but at the same time, there still are many players around given the size of the market. The implication nevertheless will be that every conceivable merger will need to be reviewed, no matter how unlikely it is to create market power. Conversely, it is easily conceivable that in another industry, where only 2 players are left, a merger creating a monopoly does not need to be reviewed by the authority because the individual companies do not exceed the sales thresholds.

The findings this leads to are surprising. Using an algorithm that tests how many mergers need to be reviewed, starting from all conceivable merger operations, wide differences appear across industries within one and the same country and between countries within one and the same industry. The latter finding is probably the most troublesome, recalling the “fate of Ilford” described above. To give but a few examples, in the manufacturing of chemicals and chemical products (NACE 24), in France in 1999, only 2.55 percent of all conceivable merger operations needed review by the competition authority. In the same year and industry, 19.23 percent of all conceivable operations in Belgium needed to be reviewed by the competition authority. And in the

Czech Republic, this was 24.95 percent. For the manufacturing of pulp, paper and paper products (NACE 21), in France only 0.79 percent of conceivable merger candidates needed to pass review. In Belgium it was 8.24 percent and in the Czech Republic 31.88 percent.

Of course, what matters in the end is how many mergers get blocked by the authority. So although in Belgium more operations needed to be reviewed than in France, it could well be that as many operations as in France are admitted. In terms of the rejection percentage, France would then look much “tougher”, since it grants permission for mergers for the same number of cases as Belgium, but in Belgium more operations need to be reviewed. But at the same time, companies in Belgium will less likely find a partner that allows for mergers without review, and hence will be more often confronted with the costs of filing. For a “large” operation, a recent study indicates that these costs might run into a figure of 100,000 euros for the companies involved. In addition to those, there are the costs of administration. Hence, widely differing thresholds, that do not take into account the size of the country and the presence of scale economics particular to each and every industry, will impose large differences in the transaction costs in the market for corporate control.

Conclusion

The previous sections show in part how multi-jurisdictional competition policies may create distortions. On all aspects, further research is necessary before conclusive policy advice can be given. That is of course always the case, and decision-makers often have to act before everything is known. Viewing it more positively, we are fortunate to know at least some aspects of the usefulness of competition policy in small open economies, on the nature of the distortions that can result, etc.

Unfortunately, there are issues just as important that are not only unresolved but where research has not even started. The highest research priority must be given to these issues.

One such example is to be found in the various leniency programs that have been adopted by nearly all of the NCAs. Two years after its inception, in Belgium 16 cartels had already applied for leniency. Undoubtedly some of these also operate on the

Dutch market, given the interwoven economic structure of Belgium and the Netherlands. What then happens when companies apply for leniency in one country but not in the other? Is the information they provide to the authorities secret, or will one authority pass it on to the other? At first sight, this might seem an entirely academic question, as companies who apply for leniency probably do so at the same time in all countries in which they operated, presuming information is exchanged between NCAs. But then, since the leniency programmes are different in terms of the reduction in fines, what is the overall impact on leniency of having many and different “tariff reductions”? For example, if in country A, the fine reduction is 100 percent for the first firm, while in country B this is only 40 percent, companies still need to calculate in a fine of 60 percent of the fine in country B. Clearly, if fining uses rules of thumb based on sales, and country B is relatively large compared to country A, this might still be a substantial amount. And hence the company might decide not to apply for leniency and leave the cartel unaffected. The harsh treatment in country B, together with information exchange between the NCAs, then renders country A’s leniency policy completely ineffective.

Judging from the 100 percent fine reduction, one could argue that country A relies a lot on its leniency policy to detect cartels, maybe because the NCA lacks the skills necessary to find out about price fixing practices, or because institutional factors favour the formation and stability of cartels.

By a similar argument, country B only grants 40 percent because it is well-equipped to fight cartels in the absence of cooperating conspirators. But by doing so, it interferes with its weaker colleague.

In summary, we started by noting that multi-jurisdictional competition policies make a lot of sense, even in the smaller open economies of the European economy. But the widespread differences in how these policies are implemented create pronounced distortions that probably affect the level playing field of competition in the EU. This apparently calls for more coordination among the member states, which is probably the case in the area of thresholds for merger review. But in the end, it may even be that coordinated behaviour, as with the exchange of information in leniency programmes, is not the best thing to do. This implies that for each and every aspect of competition policy, a precise answer can only be given after careful research has been con-

ducted. Given the increased level of resources allocated to competition policies, such benchmarking against both academic research and international best practice really has become a priority.

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