

THE ARGUMENT FOR ROBUST COMPETITION SUPERVISION IN DEVELOPING AND TRANSITION COUNTRIES

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Abstract

The article discusses first the differences between market economic models, socialist or planned economies, and economies controlled by monopolies or cartels, to make the case for competition supervision. Subsequently it argues for a broad approach to competition supervision - beyond a narrow view of antitrust law. The second part of the paper discusses monopoly or dominant position and the criteria to measure them. It reviews the reasons for merger control as a preventive step against monopoly or dominant position. Finally it discusses the issues related to collusion in the form of cartels and how to detect them. The third part of the paper focuses on the best ways for developing and transition countries to introduce or reinforce comprehensive competition supervision: Functioning institutions and how they have to be empowered and structured; priorities to be set; how competition oversight has to be embedded in the legal system, including court review; and why effective enforcement is so important and how it can be promoted. In an annex** there are links to some 75 countries which have newly introduced competition laws in the past 25 years and their legislative materials. Finally, there are links to another 30 countries which have substantially revised their legislative bases in the same time frame.

Keywords: Robust Competition Supervision, Monopoly Regulation, Antitrust Law

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1. THE ECONOMICS OF COMPETITION

It has been said that there is no end to human greed. Pretty much everything else in the world, in particular those things that we consider positive and/or desirable, are in short supply. When something is in short supply, it means that there is not enough of it available to satisfy everyone who would like to have it. We may be able to produce more of one thing but only at the expense of another thing. For example, we may be able to satisfy more people who desire clean air by closing a factory that causes pollution or by forcing it to install expensive filter equipment. However, both of these measures, while increasing the supply of one thing, clean air, decrease the supply of one or more other things, in this case some or all of the jobs in the factory and some or all of the goods it is producing. One of the most important problems facing human societies, therefore, is the need to make decisions about how much to produce of everything and how to distri-

bute the limited production among the many who want to have a share of it. This is called the problem of allocation of limited resources.

Economists⁴² have long argued, and 20th century history has ultimately proven, that market econo-

⁴² Many lawyers - and at least some of my readers - very quickly get uncomfortable with any form of economic analysis, in particular if it includes charts, let alone numbers. All too often, the very reason why we went to law school in the first place is that it seemed the furthest from anything that could require mathematics. The reality is not quite like that, however. Whether in tax law, when we have to understand the financial implications of different ways of structuring a corporation or international business transaction, or in the calculation of damages in tort law, a good lawyer will always think about the economic implications of his or her advice for the client. This is all the more true in competition law, where economic analysis has become very important for the way regulatory authorities and courts will analyze conduct or

mies are more efficient than non-market economies at making these decisions.⁴³ In a non-market economy, decisions about allocation of scarce resources (capital, labor, goods, etc.) are either made by the state or by a small number of private actors. If these decisions are made by the state, we speak of a planned economy, sometimes also called a socialist or communist economy. If the decisions are made by a small number of private actors, they have to be in a position of monopoly or dominance or they have to collude in the form of cartels in order to have impact. By contrast, the allocation of scarce resources in a market economy is based on large numbers of decisions made by large numbers of buyers and sellers, who meet in the marketplace every day to negotiate deals, each of which individually does not significantly influence the overall economy.⁴⁴

practices of corporations potentially restricting competition; Cavanagh, 2013. As Morgan has pointed out, “whether or not one personally likes the implications toward which economic analysis points, a lawyer needs to understand the analysis in order to assess what the purpose and effect of a practice might be, whether the practice is likely to be challenged, and if so, how most courts today will react to it.” See Morgan, 2005, at p. 5. Fortunately, there are a number of relatively accessible books for lawyers seeking to understand economic analysis of law and more particularly competition law. These include Barnes and Stout, 1992; Walker and Bishop, 2010; Calvani and Siegfried, 1988; Gellhorn et al., 2004; Hildebrand, 2009; Hylton, 2010; as well as Sullivan and Harrison, 2014.

⁴³ The goal would be to come as close as possible to the so-called “Pareto-optimal allocation of goods and resources.” See Mueller, 2003, p. 3. A Pareto-optimum is achieved when all production factors, such as resources and other goods, know-how, labor, and capital, are allocated in such a way that any re-allocation making at least one person better off would also leave at least one person worse off. It should be noted, however, that Pareto-optimal allocation considers only the overall benefits to society. There may be many variations of Pareto-optimal allocation, each one benefitting society equally but individuals differently. For example, a certain level of employment at a factory may be the Pareto-optimum. Employing *more* workers would reduce the overall efficiency. However, employing *different* workers could well be the same from society’s point of view while making a huge difference for those who now have jobs and those who do no longer.

⁴⁴ Relatively small firms in competitive markets are also called *price takers* because they do not make the prices by restricting or increasing their output. Rather, the prices are made by the market, i.e. the aggregate of all buying and selling transactions by all buyers and sellers meeting in the marketplace. If one firm would reduce its output, it would not be able to sell less for more. Instead, it would just lose sales at the market price to another firm. Only if many firms would agree to lower their output and not to pick up customers turned away by their “competitors”, prices would go up. The latter, however, would be a cartel and not any more a competitive market. Very nearly every decent book on competition or antitrust law contains a discussion of price theory and competitive markets in its introductory chapters. For examples see note 1. Similar results can also be found in the public choice literature, for example in Stearns, 2003, at pp. 111-117.

The problem with all of these decisions – market economy or not – is that the decision-makers do not necessarily pursue the public good, that they have limited information, and that the parameters in the market place change all the time. Thus, from a point of view of economic efficiency, we can say that the problem is that a certain number of decisions will inevitably be *wrong*. Either those decisions will promote private benefit at the expense of public good, or they will try to promote the public good but fail to do so in the best possible way because of insufficient factual information or insufficient understanding of the optimal solution for the respective problem. Insufficient understanding may be an objective problem of predicting the future or a subjective problem of not understanding the present. For the purposes of this article, both types of decisions shall be defined as *mistakes*, namely those that promote short term and/or limited private gain over long term and/or larger public gain, and those that may pursue the best overall result but turn out to be inferior at doing that. Both types of mistakes cause overall loss to society.

In our globalizing world, national economies are no longer predominantly about the allocation of resources on the national level. They are also competing for resources on the global level, for example for profitable sales opportunities in foreign markets, for deals to buy natural or other resources abroad, and for decisions about foreign direct investment. At the same time, countries have become more interdependent, and decisions in one country may directly affect the availability and allocation of resources, hence ultimately the level of prosperity, in another country. This magnifies the impact of good or bad decisions and the importance of making as few mistakes as possible. To illustrate the point, compare the strategic decisions taken by Nissan and General Motors towards the next generation of electric automobile. While the Nissan Leaf runs entirely on electricity, which limits its range to the life of the battery, the Chevy Volt comes with a back-up engine running on gasoline so that it can operate beyond the life of its battery. However, the second engine in the Volt comes at the steep price of an additional \$8,000 on the sticker price. The next couple of years will show who made the better bet and either Nissan or General Motors will sell large numbers of automobiles not only in their respective domestic markets but potentially in many countries. Although it is possible that the one type of car may appeal to one type of user and the other to another and that both companies come out as winners, it is also possible that one of them will have sunk billions of dollars in development costs into a product that does not sell (enough) and does not recover this investment. Given the low prices of gasoline and the glut of crude oil in the market in recent months, it is equally possible that neither of the cars will ever recover its development cost. Needless to say, even large automobile manufacturers with deep pockets can only afford so many of these kinds of mistakes.

It is important to understand that the problem of wrong decision-making is inherent in all economic activities, whether in a market economy or a non-market economy. As long as decisions are taken by humans, we will encounter selfish pursuit of short term private benefit at the expense of society, and we will encounter problems of incompetence and of

predicting future developments. One may even argue that a state actor should be less incompetent, on average, than a private actor and that governments should come up with fewer wrong decisions than companies or private investors, simply because of the larger information base and other resources available to the government. However, this may be countered by the problem of ownership. While private actors and investors are using their own money and usually have to bear the consequences of their wrong decisions themselves, civil servants in the government are usually insulated from the consequences of their decisions and thus less motivated to do their best at avoiding mistakes.⁴⁵ Whether one believes that private individuals and investors are generally better than government officials at making the kind of decisions we are talking about, is a question of ideology.⁴⁶ However, what is beyond doubt and ideology is the fact that both types of actors will make mistakes. Furthermore, while the future has always been uncertain, change comes ever more quickly today, which requires that decisions are adjusted all the time to match the needs of a changing environment and prevent a good decision from becoming a mistake. The crucial question, therefore, is how different economic models deal with their mistakes and how they deal with the change that is imposed on them.

The worst model at correcting its mistakes is the economy dominated by a small number of private individuals via monopoly, dominance, or cartels. Such an economy actually *rewards* mistakes as defined above. In the absence of constraints, the private individuals can and usually will pursue their personal self-interest at the expense of public good and will prosper, while society as a whole has to pay the price. In the most extreme example of monopoly, the monopolist can and will charge super-competitive prices for its goods or services and become extremely rich. Each individual customer and society at large not only pay too much to satisfy their needs, but chances are that the absence of choice, hence competitive pressure, also results in inferior quality of the goods and services. Change, for example, in the form of technological progress, does not have to be accounted for by the monopolist, unless the very monopoly comes under

threat.⁴⁷ The situation is only marginally less extreme where an individual enterprise merely has a dominant position and not a full monopoly. The case where several enterprises could compete but rather collude in the form of a cartel may be the worst possible scenario because the monopolist at least benefits from economies of scale even if they are not passed on to customers. The bottom line is in each of these cases that everybody pays a higher price for lower quality, and the economic loss of the many far outweighs the economic gains of the few.

The planned or state controlled economy is only marginally less bad at correcting its mistakes. While this economy does not actually *reward* the decision-makers for their mistakes, unless there is also corruption, it fails to adequately *punish* the mistakes. To the extent bureaucrats may be held accountable for wrong decisions, this gives them an incentive to hide those decisions, for example by deferring to committees or by suppressing data. It also gives them an incentive to avoid taking decisions in the first place, which makes governmental structures rigid and inflexible in the face of new data and/or external change. Simply speaking, planned economies will be slow to adopt decisions and even slower to correct them once they turn out to be inferior. The Soviet Union was full of examples.

This brings us to the market economy and the question why large numbers of individually small sellers negotiating with large numbers of individually small buyers should be inherently better at understanding how best to allocate resources in the present environment and how best to deal with change in the future. One could even argue that the very fact that none of the buyers or sellers is individually large naturally limits their ability to research and process today's data and to hire the most competent experts at predicting future trends. However, this would completely misunderstand the power of the market. Much like a match between a grandmaster of chess and a supercomputer, the invincible power of the market relies on its ability simply to try out every possible alternative. We may go as far as saying that the market, compared to the experts, is not very smart at all and makes lots of inferior choices. However, while the expert has to rely on his or her expertise to come up with the best possible solution, one move at a time, the market relies on an infinite number of trial and error moves to find the best possible solution. While individual buying and selling decisions in an open market place may not look very smart at all, the aggregate result of all buying and selling decisions in that market has proven superior to any other form or method of allocating scarce resources today and accounting for change tomorrow.

Market economies have their own problems, however. Two of the most important shortcomings of the market are the failure to account for

⁴⁵ This is one important reason why larger companies that are run by salaried CEOs rather than owners tend to tie the compensation of their leaders to the overall performance of the company via annual bonuses and longer term stock options. For in-depth analysis see Jensen and Murphy, 1990.

⁴⁶ Until recently, the answer seemed pretty obvious. After all, the Soviet Union had proven unable to compete with the West and collapsed and even China had turned to market economy for its remarkable growth. However, the current financial crisis has somewhat discredited Western claims of superiority and indeed, those countries that have suffered less from the crisis seem to be the ones with more government intervention in markets. Nevertheless, there has yet to be a planned economy or an economy with heavy government intervention that reaches, let alone surpasses the level of general prosperity in the Western market economies of the EU and North America. In this context, it can also be instructive to compare different schools of antitrust analysis. See, for example, Posner, 1979.

⁴⁷ A good example was the supply of end-user telephone equipment in Germany in the 1970s and early 1980s. Since Siemens was the sole – and therefore monopoly – provider licensed by the state telephone company, Germans had to deal with large mouse-grey rotary dial phones at high prices while sleek and colorful dial tone phones were already available in many more competitive markets at much lower prices. For background reading see Morgan and Webber, 1986.

externalities and the trend towards *concentration*.⁴⁸ Both of them have to be accounted for by a country that seeks to improve its economic performance, and to promote sustainable growth, overall prosperity, and the gradual reduction of income disparities.

Externalities are sometimes also called “spill-over effects”. They occur when some of the costs or benefits of a decision or a deal affect natural or legal persons other than the decisionmaker(s) or the partners of the deal (Cole, 1991). For example, if a company is trying to reduce the cost of production by keeping the wages of the workers low, it may experience high turnover in the form of workers leaving for better paid positions elsewhere, as well as difficulty in recruiting skilled and motivated replacements. This would be an *internality*, as it affects the situation of the decision-maker itself. By contrast, if the same company reduces the cost of production by releasing waste water unfiltered into a nearby stream, this may have no impact on the decision-maker itself as long as there are no governmental or other sanctions. The pollution would be a *negative externality*, as it negatively affects the situation of the neighbors and other downstream users of the water.⁴⁹ As the example shows, the problem with externalities is the disconnect between those who take the decisions and those who suffer the consequences. In an unregulated market economy, there is an incentive for decision-makers to ignore negative externalities for private profit. This, in turn, creates a justification for government interference in the market. If there are negative externalities, corrective action should be taken in the form of financial disincentives (taxation) and/or regulation and enforcement. Conversely, positive externalities, i.e. benefits to third parties other than the decision-maker(s) or partners of a deal, can be a justification for government subsidies.⁵⁰

Concentration is the problem of individuals who prefer to cooperate rather than compete. The ideal market is one of perfect competition,⁵¹ characterized by an infinite number of small sellers constantly negotiating deals with an infinite number of small buyers (see figure 1), where transactions costs tend towards zero and full information transparency prevails.

In such a market,⁵² each individual producer/seller is in direct and open competition with every other producer/seller and additional sales will go to those who offer the highest quality product at the lowest price. Since transparency is a given, consumers can actually identify the highest quality and lowest price and since transactions costs are negligible, they can then go and contract with the supplier who offers that quality and price, regardless of distance.

Perfect competition is rarely found in reality, of course. The number of producers or sellers and the number of consumers or buyers is rarely infinite. More importantly, transparency is limited since products may not be entirely comparable and consumer time for price and quality research is limited.⁵³ Finally, transaction costs usually go up when transactions are done over a distance and involve credit financing and other complications. More realistically, therefore, is to speak of *workable* competition or *effective competition*⁵⁴ in markets where there are more than a few producers or sellers and more than a few consumers or buyers, where there is a reasonably good level of transparency, and where the transaction costs have little or no influence on purchasing decisions. The terms *workable* or *effective* competition signal that competition in these markets may not be perfect but it is generally working or effective enough to secure the general push for producers and sellers to offer the highest possible quality at the lowest possible price today and in the foreseeable future.

⁴⁸ Externalities as well as monopoly or market power are typically among the key market failures discussed in economics and public choice literature. See, for example, Cooter and Ulen, 2007, at pp. 43-45.

⁴⁹ Krugman and Wells, 2006, dedicate an entire chapter of their well-known textbook to negative externalities using the example of acid rain caused by coal burning power plants and other polluters, at pp. 455-474.

⁵⁰ An example of positive externalities could be the social benefits of education or the environmental benefits of the installation of solar panels by homeowners. For discussion see, for example, Krugman and Obstfeld, 2008, at pp. 267 et seq.

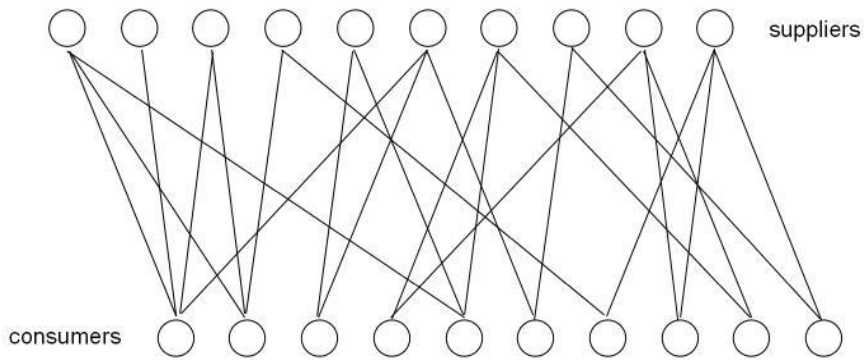
⁵¹ Bob Lane defines competition as “the struggle by firms to achieve superiority over other firms in the marketplace” and competition law as “the rules limiting the freedom by which they may do so”. See Lane, 2000, at p. 6.

⁵² Markets are defined in terms of products, including essentially all those products that are interchangeable from the consumer’s point of view, and in terms of geography, covering the largest possible territory that is sufficiently homogenous and not subject to significant barriers to trade or transaction costs. For example, the market for fresh bread is rarely larger than what can be reached within a 10 minute drive from the consumer’s home and may be as small as walking distance. Consequently, it may only include two or three bakers or shops which sell bread. Also having a fast food outlet in the area will not be a useful substitute for consumers trying to buy bread for their breakfast at home. By contrast, the market for large passenger airplanes is a global market and includes Boeing and Airbus as the only producers/sellers. Military transport aircraft and their producers are not in that market because the airlines cannot avoid high prices of Boeing or Airbus by purchasing transport aircraft. As we will see later, makers of military aircraft may nevertheless curb the market power of Boeing and Airbus to charge super-competitive prices because they can be potential entrants into the passenger aircraft market. For further discussion, see below.

⁵³ Indeed, there is an opinion that a certain level of misinformation of consumers is tolerable or even desirable, see Darby and Karni, 1973.

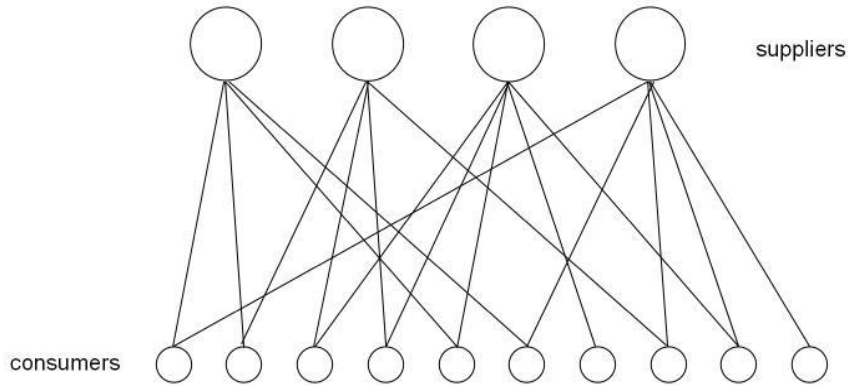
⁵⁴ For more detailed analysis see Areeda et al., 2004, pp. 15-32; Bishop and Walker, 2010, at pp. 15-50; and Fox et al., 2004, at pp. 56-76.

Figure 1. Structure of a Competitive Market



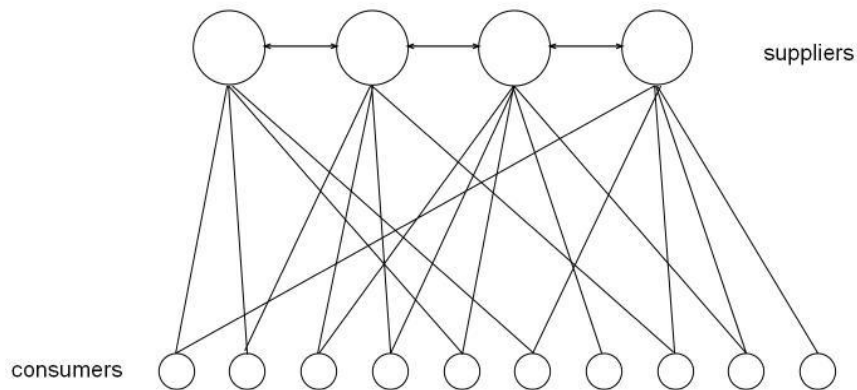
many small suppliers negotiate deals with many small consumers,
none of the suppliers or consumers have market power,
all of the suppliers and consumers have choices,
there is sufficient transparency and relatively low transaction costs

Figure 2. Structure of an Oligopolistic Market



many small consumers negotiate deals with a few large suppliers,
the consumers don't but the suppliers increasingly have market power,
suppliers have many and consumers still have some choices,
there is sufficient transparency and relatively low transaction costs

Figure 3. Structure of a Cartellistic Market



many small consumers negotiate deals with a few large suppliers,
the consumers don't but the suppliers together have market power,
since suppliers cooperate, consumers have no real choices,
transparency and transaction costs become irrelevant

While perfect or even just workable competition is the most beneficial situation for society as a whole, it is sub-optimal for the producers and sellers. The only way to grow in such a market is by working harder/longer/faster and/or better/smarter than the others. Since this is hard, some producers or sellers will seek to avoid the competitive pressures of the market place. First, they may seek to merge with competitors to reduce the number of producers or sellers and obtain a stronger position in a smaller crowd (see figure 2).

Once a process of consolidation begins, others come under pressure to follow suit lest their smaller size becomes a disadvantage in negotiating with suppliers or a real or perceived disadvantage regarding economies of scale.⁵⁵ In this way, a first mover can trigger an avalanche and, as a result, a structural shift from many competitors to an *oligopoly* of just a few competitors. Second, once the number of players in a market is no longer infinite,⁵⁶ the remaining companies may try to form a cartel to fix prices, limit output, or agree on some other form of anti-competitive conduct (see figure 3).

In an extreme case, a single company may become so dominant that it is essentially the only remaining significant player in a market and, hence, a *monopoly* (see figure 4).⁵⁷

Even a country that is blessed with near perfect or at least workable or effective competition in a given geographic and product market, therefore, has to undertake steps to ensure that this competition is not gradually undermined and disappearing. This is where competition law comes into the picture.⁵⁸ Unsurprisingly, economists can demonstrate that sustainable economic growth, overall prosperity, and gradual reduction of income disparities, are all supported by the adoption and implementation of robust competition⁵⁹ oversight. Even more impor-

tant, whenever a certain product and geographic market is not sufficiently competitive, let alone when a whole country is characterized by the existence of dominant firms or monopolies in many markets and/or heavy government intervention that is not justified as a measured reaction to correct externalities, there is much to be gained from the introduction of robust competition oversight. Furthermore, robust competition oversight should ideally be paired with measures to promote transparency in the market and measures to reduce transaction costs. All of these will be discussed in more detail below.

The economics of competition and competition law, as outlined very superficially above, are virtually universally accepted today. It is not surprising, therefore, that in the last 25 years, basically since the end of the cold war, at least 75 countries have introduced their version of competition oversight (Annex 1) and another 30 or so have substantially revised their older legislation (Annex 2).⁶⁰ However, the results have often been disappointing – in particular for the developing countries. Most of these countries do not have better market economies today than they had before the introduction of competition law and authorities. Prices have not come down from super-competitive levels, quality remains inferior to other parts of the world, and dominant firms, if anything, are larger and more powerful today than they were before. This begs the question what went wrong. After 20 years of watching countries and advising governments as they experiment with competition law, advising dozens of large and very large enterprises as they respond to these competition laws, and conducting or supervising many research projects done by me and my students in this area, I am trying to answer this question in the present publication.⁶¹

⁵⁵ For a recent example see Los Angeles Times, *Marriott's Plan to Buy Starwood for \$12.2 Billion Could Trigger More Hotel Mergers*, Business News, Friday, 11 March 2016.

⁵⁶ Cartels tend not to work well if the number of players in the respective market is too large. Either some firms will not participate in the cartel for fear of sanctions. Or some participants may begin to cheat, i.e. try to gain market share at the expense of other participants by undercutting the agreed upon prices or conditions. Smaller cartels can detect cheating firms and apply their own sanctions against them. Large cartels are rarely able to detect who is cheating. For more elaborate discussion see Dick, 1996.

⁵⁷ Since there are several paths to dominance or monopoly, including natural growth of the most innovative and competitive company, mergers, as well as natural monopolies, in particular in network-based industries such as railroads and utilities, size alone should not necessarily be condemned. This will be developed further below.

⁵⁸ The literature on antitrust- or competition law fills many shelves in our libraries. Books I have personally found particularly informative are, for example, Areeda et al., 2013; Elhauge and Geradin, 2011; Faull and Nikpay, 2014; Gavil et al., 2008; as well as Rose and Bailey, 2014.

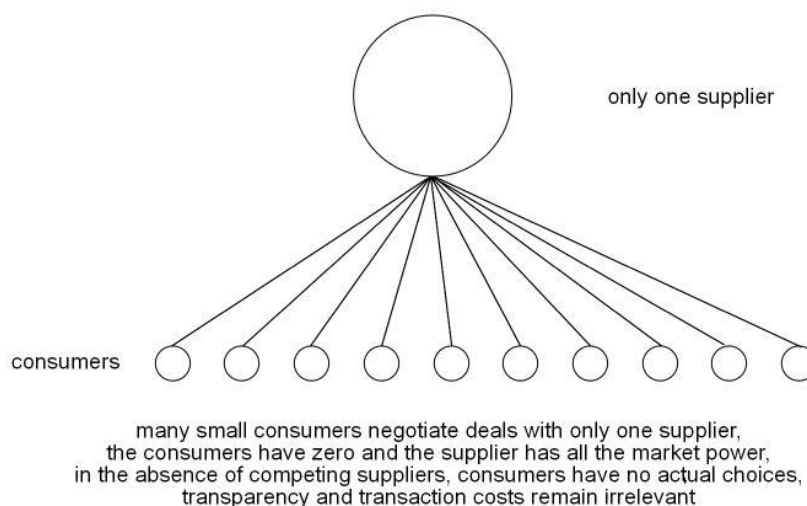
⁵⁹ Although in the United States of America, the subject is more commonly referred to as "antitrust law", I prefer to use the European terminology because "competition law" is wider, capturing not only the combat against trusts or cartels but also several other components of the fight against anti-

competitive practices implemented or attempted by private parties and even public authorities. The scope of analysis will be explained in part 2. of the article.

⁶⁰ For excellent introductions to the competition laws and supervisory mechanisms of Australia, Brazil, Canada, China, the EU, France, Germany, India, Ireland, Italy, Japan, Mexico, the Netherlands, Russia, South Africa, Spain, and the United Kingdom, see Fanelli et al., 2011. See also Maher Dabbah, 2010; Kronthaler, 2007; as well as Kronthaler and Stephan, 2007.

⁶¹ On a related issue see Emmert, 2003; some of the institutional problems are also addressed in Emmert, 2003a.

Figure 4. Structure of a Monopolistic Market



2. WHY COMPETITION LAW IS BETTER THAN ANTITRUST LAW

Although we can trace legal disputes over monopolies as far back as the early 17th century,⁶² and the first statute on the matter was probably the British Statute of Monopolies of 1632, which already prohibited monopolies with the exception of patents (Greenberg, 2010, at p. 1488), modern competition oversight was invented in the United States after the presidential elections in 1888. During this time, leading corporations in a variety of industries had started openly cooperating in the form of “trusts”, fixing prices and other terms of trade to the detriment of consumers and society at large. In response, Senator John Sherman introduced a bill declaring “[e]very contract, combination in the form of trust or otherwise, or conspiracy ... illegal” if it causes “restraint of trade or commerce among the several States, or with foreign nations”.⁶³ The legislative history demonstrates that the main purpose of going against the powerful trusts was the protection of consumer welfare.⁶⁴ Although §2 of the Sherman Act goes on to condemn monopolies, the “trust-busting”⁶⁵ purpose dominated the discussion

and the term “anti-trust law” stuck to this day. An alternative term for *trust*, although not strictly the same, is *cartel*. This is reflected in German law, which is commonly known as “Kartellrecht”,⁶⁶ with supervision entrusted to the “Bundeskartellamt” (Federal Cartel Office).⁶⁷

Since challenges to workable or effective competition arise not only from collusive practices of the major players in oligopolistic markets but also from other kinds of private interference and even some state interference with the forces of the market, both the terms antitrust law and cartel law are under-inclusive and to be avoided. In particular, in emerging markets and transitional economies, classic cartels are usually not the biggest problem since it is not very common that these markets have a number of relatively comparable enterprises that could compete but prefer to collude. More often than not, emerging and transitional markets are dominated by one or a few companies per industry. If this is indeed the case, measures against abuse of dominant position, respectively monopolization, are needed more urgently than anti-cartel measures. In general, it is preferable to use the term *competition law* and to develop this law in a comprehensive way that covers all major challenges to effective competition.

Although U.S. law regulates more than just trusts or cartels, it is not an easily accessible legal system for non-U.S. lawyers. The statutes are generally old and short and for their proper understanding it is necessary to study very many court decisions, which are by no means always easy to read or even consistent. By contrast, EU competition law was developed more recently (McGowan, 2010)

companies and combinations but merely regulate their conduct to prevent abusive practices.

⁶⁶ The official title of the German statute, however, is Gesetz gegen Wettbewerbsbeschränkungen (Act Against Restraints on Competition); see BGBl. 2009 I, at 3850 (the German version is available online at <http://www.gesetze-im-internet.de/bundesrecht/gwb/gesamt.pdf>); an English translation, although not entirely up to date, can be found at <http://www.iuscomp.org/gla/>).

⁶⁷ See The Bundeskartellamt, <http://www.bundeskartellamt.de/wEnglisch/index.php>.

⁶² See, for example, The Case of Monopolies, 77 ER 1260 (1603), as quoted in Morgan, 2005, at p. 1.

⁶³ See Sherman Antitrust Act, 15 U.S.C. §1. See also Collins, 2013.

⁶⁴ This is largely ignored by the Chicago School and even the Harvard School, both of whom work from the premise that antitrust law is first and foremost about promotion of economic efficiency, Posner, 1979. See also Pitofsky, 1979, and comments by Schwartz, 1979. An interesting discussion about the question whether antitrust should pursue any specific goals was conducted at a symposium at Fordham in 2013. See, *inter alia*, Stucke, 2013, Fox, 2013, as well as Hyman and Kovacic, 2013.

⁶⁵ The term was coined when President Roosevelt, from 1901/02, instructed his administration to make use of the Sherman Act to rein in powerful and abusive trusts like Rockefeller’s Standard Oil and Hill/Harriman/Morgan’s Northern Securities Co. (railroads). Roosevelt himself did not like the term because he did not want to destroy the

and is much more determined by statutory materials. Although the legislation in the EU is not exactly easy reading either, at least it is for the most part inherently consistent and one does not have to worry nearly as much whether a certain case has been overruled or should be distinguished.⁶⁸ More importantly, since 1980, antitrust enforcement in the U.S. has been going through a series of periods where it was largely dormant. During the Bush Administration from 2000-2008, the Justice Department did not bring a single monopolization case to court and merger applications were basically automatically approved, regardless of the potential for domination. The main exception was cartel enforcement. By contrast, the EU Commission, during much the same time, built a track record of vigorous and successful competition oversight and enforcement in all areas with a limited exception in state aids. Therefore, it is nowadays more fruitful for developing countries and emerging markets seeking to introduce robust competition oversight, to look to EU competition law for inspiration, rather than U.S. antitrust law.⁶⁹ Hence, the following discussion will be based heavily on EU law models⁷⁰ and draw only occasionally on US law.⁷¹

Analysis of threats to workable or effective competition on the one side, and EU law responses on the other, suggests that a country has to address not just monopolies and cartels but also a number of other issues. Therefore, the standards and definitions to be included in substantive competition law(s) of transitional and developing countries shall be outlined in some detail.

2.1. Monopoly or Dominant Position Resulting in Market Power

The first thing to remember in any discussion of monopoly is that size alone does not matter nearly as much as power, and that even power does not have to be a problem as long as it is not abused.⁷² Some definitions will be useful:

As the name suggests, *monopoly* is a market structure in which there is only one player on the producer/seller side (selling power) or on the user/purchaser side (purchasing power).⁷³ If there is one very large company in a market with one or more much smaller companies, it is better to speak

of a *dominant position* than of monopoly. Both of these scenarios require a definition of “the market” because it is not possible to know the number of companies sharing a market or to measure the power of a dominant firm in a market without first defining what the market is (Kauper, 1996; for an opposing view see Kaplow, 2010; Massey, 2010; as well as Crane, 2014). Markets have to be defined with regard to the *product* and the *geographic* scope.⁷⁴ The product market includes all sellers or buyers that are *in competition* with each other. Products are in competition when they can be exchanged. For example, small passenger cars are not identical to medium sized passenger cars but the one can be a *substitute* for the other from the buyer/consumer point of view. This is usually tested – in a hypothetical way – by assuming a significant and persistent price increase in only one of the two products and observing whether there is a measurable switch of consumers to the other product. In our example, if the price of medium sized passenger cars went up by 5-10%, would we see a significant number of potential buyers of medium sized cars switch to smaller passenger cars? Since the answer should be affirmative, small and medium sized passenger cars are in competition with each other and, therefore, in the same market. By contrast, luxury cars are not in the same market as small cars, since a price increase in the luxury car market would induce some buyers to switch to medium sized = medium priced cars but not all the way down to small = cheap cars. “The product” can be a good, like the cars in the previous example, but also a service, for example the distribution services of a supermarket chain or the work of a plumber. Therefore, “the product market” can also be food retailing or bathroom repairs and renovations and these markets would include all those who are offering the same or a substitutable service. “Consumers” don’t have to be end-users and are usually the direct contractual partners of the firm(s) under investigation. Therefore, the question whether different computer chips are part of one and the same market has to be answered from the point of view of the computer makers and any other firms who buy the chips to integrate them into their own products.

Once the product market has been determined, the geographic scope of that market also needs to be decided. In general, we include all those competitors into one geographic market who are operating under essentially homogeneous conditions, meaning in particular under comparable legal frameworks, economic and social structures, as well as consumer preferences and possible other factors. The test is again whether a potentially competing product is indeed a viable substitute from the buyer/consumer point of view. For example, if there is only one car maker in a given country, this company may have a monopoly. However, if it is sufficiently easy for car dealers and even average buyers to import cars from another car maker in a neighboring country, the

⁶⁸ For an overview of EU case law see, for example, Vogelaar, 2010.

⁶⁹ The EU model, given its supranational character, is of particular value for other regional economic integration systems like ASEAN, SADC, ECOWAS or CARICOM. On this issue see Drexler et al., 2012; as well as Papadopoulos, 2010, in particular chapter 5.

⁷⁰ For a compact overview of EU competition law, see Powell et al., 2011. See also Fox, 2009.

⁷¹ While difference in style are substantial, differences in substance may not be so great. See Bartalevich, 2013 and Bartalevich, 2014.

⁷² For useful comparative analysis see Schmidt, 2012.

⁷³ An example for purchasing power is a country or region where there is only one very large supermarket chain as the dominant food retailer. This chain would have a lot of power when negotiating with suppliers such as dairy producers. If your milk is not on the shelves of this supermarket chain, you are just not going to sell a lot.

⁷⁴ For guidance see COMMISSION NOTICE ON THE DEFINITION OF RELEVANT MARKET FOR THE PURPOSES OF COMMUNITY COMPETITION LAW, OJ 1997 C 372, pp. 5-13. See also Hawk and Huser, 1996, at pp. 123-168; and, more recently, Kokkoris and Shelanski, 2014, at pp. 199-220. For a critical analysis of the U.S. approach see ten Kate and Niels, 2009.

geographic market would encompass both countries and the market power of the local firm would be substantially reduced. Substitutability has to be examined in a comprehensive way, of course. If importing foreign cars is cheap and easy but they cannot be registered without major bureaucratic hurdles, they are generally not viable substitutes. Similarly, if the local cars come with right hand drive, as it is in the United Kingdom, imports from the European continent with left hand drive will not be viable substitutes for most drivers.

After the market has been determined in both product and geographic terms, the market power of the different firms in that market can be measured. Several criteria have to be considered.⁷⁵ First, we have to look at the respective market shares. A monopolist, by definition, has 100% market share. However, a firm may be considered dominant although it has only 40-50% of the market share, for example if all other firms in that market are tiny (50 firms with 1% market share each) or if the big firm has special advantages, such as essential intellectual property rights that it licenses - or does not license - to the competitors for a fee. As a rule of thumb, we can say that dominance is highly unlikely for a firm with a market share below 25%, it is possible but needs significant other factors with market shares between 25 and 50%, it is likely with market shares between 50 and 75%, and it is almost always a given with market shares over 75%.

The analysis of current market shares is a static analysis and does not account for dynamic markets. Therefore, it is usually necessary to look back at the evolution of market shares and also to make predictions about the future, in particular the existence of potential new entrants into the market. For example, a firm with 60-70% market share in a market where all other current competitors are small, say 10 firms with around 3% market share each, is clearly dominant. Whether it has actual market power, however, is a different question. Market power is defined as the ability to act independently, i.e. to disregard what the competitors are doing or may be doing in the foreseeable future.⁷⁶ In our example, the dominant firm would have market power if it could restrict its output and cause a shortage in supply that would drive up

prices without losing market share to the small competitors because they would be unable to increase their output enough to pick up the business. Alternatively, the big firm might decide to increase its prices and its market power would depend on the ability of at least some of its customers to switch to the smaller competitors for better deals. Dominant firms with market power are price makers, small firms without market power are price takers. If the dominant firm lowers its prices, the small firms have to follow suit or lose business and if they can't survive at the lower prices they will be squeezed out of the market. Conversely, if the dominant firm increases its prices, the small competitors might as well follow suit because they don't have the capacity anyway to pick up customers who want to avoid the new prices of the big firm. At the bottom line, market power is the ability to make super-competitive profits, i.e. to sell the same quality for higher prices than the competition or lower quality for the same price as the competition, and ultimately the ability to determine the profit margin of the smaller competitors and even their survival in the market. Analysis of past conduct of large firms, therefore, gives a good idea of their market power, in particular if they have been able to increase their prices without losing market share or if they have successfully squeezed smaller competitors out of the market already.

In addition to looking at past conduct as an indicator of market power, we need to look at possible future competition.⁷⁷ Potential competition is in most cases the single most powerful curb on the power of a dominant firm. Super-competitive profits are visible to potential competitors in the form of unusually high prices for competitive products or profitable sales of otherwise uncompetitive products. Markets where such super-competitive profits are possible over extended periods of time attract new market entrants. The question whether or not a new firm will enter a market and challenge the position of the currently dominant firm depends on two factors: Barriers to entry and the existence of potential competitors. *Barriers to entry* are either legal or economic. *Legal barriers* can be insurmountable, for example if the dominant firm has the key intellectual property right or if the government will not issue another license beyond the existing number. *Economic barriers* are usually surmountable, but if the cost of entry is high and the profitability of entry is uncertain, this may deter potential entrants from trying. The risk for the potential competitor will be determined by the amount of money at stake, the length of time it will take in unchanged market conditions to recover that amount, and the probability that market conditions will remain unchanged or at least not deteriorate significantly over that period of time.

For example, the dominant firm may be able to discourage potential entrants by lowering its prices from a super-competitive to a competitive level each time a potential entrant is showing interest by inquiring about a license or IP right or by entering

⁷⁵ Bellamy & Child, in their leading monograph on EU Competition Law, propose a three-step analysis: "(i) *market definition*: defining the relevant product market and the relevant geographic market ...; (ii) *market share analysis*: establishing the market share of the undertaking in question on the relevant market ...; (iii) *analysis of competitive constraints*: assessing the significance attributable to the market share of the undertaking in question and in particular whether it is likely to be eroded by actual or potential competitors" (emphasis in original). See Rose & Bailey, 2014, §9-009 at 920-936; see also Nenova, 2007, at p. 134.

⁷⁶ The European Court of Justice has defined "dominant position" as "a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition ... giving it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers." See ECJ, Judgment of 14 February 1978 in Case 27/76, United Brands Company and United Brands Continentaal B.V. v. Commission ("United Brands"), [1978] ECR 207, at para. 65.

⁷⁷ For a comprehensive analysis of factors contributing to or inhibiting market power see Rose and Bailey, 2014, §10-020 to §10-047 (see also 2010 supp. pp. 114 - 118). See also Massey, 2000; as well as the classic analysis of Landes and Posner, 1981.

into M&A negotiations with one or more of the small competitors already in the market. Volatility of prices is generally not encouraging large investments by potential competitors. In addition to the total cost of entry, a potential competitor will look at the so-called *sunk cost*, i.e. the amount that has to be written off and cannot be recovered if the market entry fails (Baumol and Willig, 1981). For example, if the entering firm is acquiring land or buildings for its operations, they can usually be sold if and when the firm leaves the market and the investment may be recoverable in full or at least in part. Conversely, if the entering firm has to spend a lot of time and money to train staff and develop know-how, the investment may not be recoverable at all in case of market exit.

Potential competitors are in particular those firms that already supply the same or a similar product in a different market and/or those firms that already work with the same customers as the dominant firm (Posner, 1975; Dasgupta and Stiglitz, 1988). For example, a passenger car manufacturer in country A can probably enter the market of country B relatively easily by setting up an assembly plant there if it seems that good money can be made in B because the current monopolist there has been charging high prices for relatively unsophisticated products. Similarly, a maker of military transport aircraft may be a potential entrant into the passenger aircraft market if it seems that good money can be made in that market for the foreseeable future.

Last but not least, the analysis of market power may also have to include special factors, for example legal advantages of the dominant firm such as licenses and intellectual property rights, special access of the dominant firm to input or raw materials due to its vertical integration, etc.

In parallel to the analysis of size and power of the firm under investigation, we need to ask the question how this firm became so big in the first place, whether the monopoly or dominance is economically or legally determined, and what, if anything, the competition authorities should do about it. Size, as measured in market share, can be desirable and undesirable from an economic point of view. There are markets in which it is simply not efficient to have more than one provider. They are often referred to as "natural monopolies". Those are in particular network dependent services with universal service obligations. Typical examples are the electricity, gas, and water supply networks. It does not make sense to have more than one country-wide network for these kinds of services, although some countries are successfully experimenting with a separation of the network from the providers so that several competing firms can feed their electricity into one and the same grid or several railway companies can run trains across the same tracks. Since the network or grid remains a monopoly, it is then either operated by the state or at least very closely supervised and regulated by the government. What remains difficult to resolve are networks or facilities with slots of different desirability. In the example where the government operates the one and only network of tracks and different companies can run their trains across them, who gets the slots during rush hour and who has to supply the late night service? The same is true for departure and landing slots at airports.

Efficient allocation requires distribution by auction or by another system that puts different prices on slots of different desirability.

In other markets it may be most efficient to have only one supplier but competition would be possible. For example, even in the United States only one supplier of larger passenger aircraft has survived (Boeing). Similarly, in Italy there is today only one manufacturer of mass-market passenger cars (Fiat). Former competitors were either forced out of the market or taken over because the market structure with multiple producers within the same country was not as efficient. However, competition is nowadays supplied from abroad, a development that was promoted by trade liberalization.

Another example where a company gradually acquired dominance in a given market was discussed by the US Supreme Court in *United Shoe*.⁷⁸ The firm under investigation was the largest supplier of shoe making machines with a market share between 75 and 85%. It held 3,915 patents and supplied machines of such superior quality that no competitor could match its offers. However, United Shoe also had a policy of never selling its machines but insisting on long-term leases, which created barriers to entry and other hurdles for actual and potential competitors and eliminated a second-hand market for the machines. The main question in a case such as this one is whether the competition authorities should interfere at all. On the one hand, United Shoe had acquired its dominant position by working hard over many years to provide superior technology and quality. On the other hand, even as a dominant firm, it still provided excellent machines and maintenance services to its customers while making only modest profits. Who or what is ultimately protected by competition law? The competitor(s)? The customer(s)? The market as such?

Developing and transition countries seeking to introduce or upgrade competition supervision have to figure out "their" way of assessing conduct *and* power and how and where to draw the lines.

One approach taken in U.S. antitrust law – but not the only one – can be summarized as follows: Any firm with an overwhelming share of the market "monopolizes" when it goes about its business and, thereby, causes a prima facie violation of §2 of the Sherman Act. However, the firm will not be prosecuted if "it owes its monopoly solely to superior skill, superior products, natural advantages, (including accessibility to raw materials and markets), economic or technological efficiency, (including scientific research), low margins of profit maintained permanently and without discrimination, or licenses conferred by, and used within, the limits of the law (including patents on one's own inventions, or franchises granted directly to the enterprise by a public authority)."⁷⁹ As can be easily seen, such an approach introduces an almost infinite

⁷⁸ See *United States v. United Shoe Machinery Corp.*, 110 F.Supp. 295 (D.Mass. 1953), *aff'd per curiam*, 347 U.S. 521 (1954).

⁷⁹ *Id.* at 342, Judge Wyzanski referring to Judge Hand in *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945).

number of variables and uncertainties.⁸⁰ Who can decide whether a firm grew “solely” based on “superior skill” or “superior products”? How do we know whether this firm is indeed the most economically and technologically efficient and that nobody else could do the job even better? What is the meaning of “low margins of profit” when profits can be manipulated by transfer pricing, flexible allocation of overheads and other costs, and similar forms of creative accounting?

The approach taken by the European Union may be more straightforward. Size alone is no crime and there is no need to ask how a company acquired a dominant position in the first place. The difference between a firm that has a dominant position versus one that does not is merely that the former “has a *special responsibility* not to allow its conduct to impair genuine undistorted competition”.⁸¹ What is prohibited by Article 102 TFEU (formerly Art. 82 ECT) is only the *abuse* of a *dominant position*. The EU, therefore, does not need to worry about firms that are not in a position of monopoly or dominance. If such firms should engage in abusive behavior, their business partners should be able to contract with competitors instead. Similarly, the EU does not have to worry about dominant firms as such, in particular about the way they became dominant, as long as they do not also engage in abusive conduct. Only when size and abuse come together, EU law draws the line and offers a number of remedies that will be discussed below.

Since we have already discussed the assessment of dominance above, what remains at this point in time is a brief discussion of the patterns of commercial conduct classified as abusive by EU law. The Treaty itself, in Article 102, contains a list of the main examples of abusive behavior, namely

(a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;

(b) limiting production, markets or technical development to the prejudice of consumers;

(c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.”

In practice, the determination whether a particular conduct is abusive or not, is not always easy. Several guiding factors can be identified.⁸²

⁸⁰ For a critical discussion of the vague and inconsistent definitions of ‘market power’ and ‘monopoly power’ provided by U.S. courts see Krattenmaker et al., 1987; as well as Kaplow, 2010, Massey, 2010, and Crane, 2014; See also Nelson and White, 2003.

⁸¹ See European Court of Justice, Judgment of 9 November 1983 in Case 322/81, NV Nederlandsche Banden-Industrie Michelin v Commission (“Michelin”), [1983] E.C.R. 3461, at para. 57, emphasis added.

⁸² For a good example from the U.S. see United States v. Microsoft Corp., United States Court of Appeals for the District of Columbia, No. 00-5212, Judgment of 28 June 2001. An instructive case in EU law would be Case C-62/86, AKZO

First, we must ask whether the conduct in question, for example the insistence of leasing of the shoe making machines combined with the refusal to sell such machines, is *likely to further reduce the competitiveness of the market*. As will be remembered, competition in the respective market is already not ideal, let alone perfect, because of the presence of the dominant firm. In such a situation, the interest of the government and society would be to promote more competition with measures to be discussed below, and certainly not to watch a further deterioration. While this does place a special responsibility on the dominant firm, it does not mean that the dominant firm should no longer vigorously compete for the highest possible quality at the lowest possible price. Our second question, therefore, must be whether the conduct in question is *proportionate to legitimate business interests*. Even a company in a dominant position can refuse to deal with a client who previously failed to pay for the goods or services in time or in full. However, it may not refuse to deal with a client if it has no other reason for such refusal than to hurt the client and/or reduce competition in the market. In general, measures subjectively intended and objectively suitable and necessary for the protection of one’s own legitimate business interests are allowed even to dominant firms, whereas measures that go beyond what is necessary or that pursue illegitimate goals, are not. In the present example, this may mean that the dominant firm has to contract even with the troublesome client, if the latter offers to pay in advance, unless payment was not the only problem in the past.⁸³ It also means that conduct,

Chemie BV v Commission of the European Communities, Judgment of 3 July 1991, ECR I-3359.

⁸³ Bellamy & Child discuss the following examples of abuse in some detail in their seminal book: 1) excessive pricing = unfairly high prices not justified by the quantity or quality of the goods or services; 2) predatory pricing = unfairly low prices designed to eliminate one or more competitors from a market and/or discourage new entrants; 3) price discrimination and price squeezing = different prices for similar transactions or customers which are not justified by objective and legitimate criteria, for example lower prices for those customers who do not deal with a particular competitor; 4) fidelity rebates and exclusive dealing = other encouragements for clients not to deal with competitors; 5) refusal to supply = our example; 6) abuse of intellectual property rights, for example the refusal to grant a license to a firm even though other competitors have received such a license and/or in situations where the respective market is undersupplied, without an objective justification for the refusal; 7) tying = the combination of goods or services that do not have to be combined, for example making the sale of photocopiers conditional upon the purchase of maintenance services; 8) other (abusive) contractual conditions, for example unfair restrictions on warranties, or prohibitions imposed in a license against “inventing around” the protected IP; 9) discrimination (other than price discrimination) = treating similar or even identical transactions differently in ways that are unfair and restrictive of competition; 10) limiting production, markets or technical development, for example the systematic and unnecessary undersupply of the market with the intention of raising prices; and 11) other abuses, for example intentional inefficiency, underutilization of capacity,

which may be fine for a company while it is small because clients can go to a competitor if they don't like the terms imposed on them, may become problematic if the same company grows to be dominant.

Against this background, countries wishing to introduce robust or improve existing competition supervision first and foremost have to adopt detailed statutory language that outlines the goal, protection of effective competition, and the primary tool, prohibition of abusive conduct by dominant firms. This must include clear and objective definitions and tools for the determination of the relevant market and the measurement of dominance and market power. Furthermore, abusive conduct has to be defined in detail and examples have to be provided. Ultimately, in-house counsel and external lawyers have to be able to determine for any medium sized or larger company a) whether the firm should consider itself dominant in a given market, and b) what kind of business conduct is consequently to be avoided. When in doubt, legislatures should seek inspiration from the statutory materials of the European Union, as well as their interpretation in the practice of the EU Commission and the European Court of Justice. If it were acceptable from a constitutional law and sovereignty point of view, explicit reference to EU competition law as the model to be followed, would provide useful guidance to practitioners, enforcement agencies, and courts, and greatly improve legal certainty.

As will be shown next, the other tools of competition oversight, in particular merger control, prohibition of cartels, and restrictions on public undertakings, are really just supporting policies either designed to prevent the creation of dominant enterprises in the first place, or to prevent other forms of accumulation of power, all with the ultimate goal of preventing abuse of power in the market.

2.2. Merger Control

Small firms generally do not have market power and if they should impose abusive terms in their contracts, their suppliers and clients presumably can just walk away and deal with a competitor instead. In this way, the market takes care of the abuser or, in other words, competition is effective in securing the highest possible quality at the lowest possible price for everyone. If firms start out small but grow large because of superior effort and quality, this kind of organic growth must not be discouraged, let alone penalized, because it would dampen competitive efforts in the first place. Thus, size alone is no crime and one should merely keep a closer eye on an increasingly powerful/dominant firm to make sure it does not get tempted to engage in abusive behavior as it gains the ability to do so without having to fear the competition any more. This was discussed in the previous section.

refusal to use available technology, or even the deliberate harassment of competitors with unwarranted litigation. See Rose and Bailey, 2014, §10-058 to §10-156 at 947-1030. Obviously, the items on the list are neither mutually exclusive, nor necessarily comprehensive of every possible form of abuse.

In this section, the focus will be on *the other* method of growing from small to big and eventually dominant, namely mergers and acquisitions. At the outset, we can say that M&A activity will not concern the competition authorities as long as the respective firms are relatively small in a relatively competitive market. However, if the market already tends towards an oligopoly, the perspectives change and further concentration becomes undesirable (Bos et al., 1992; Cook and Kerse, 2009; Hawk and Huser, 1996; Kokkoris and Shelanski, 2014; Navarro, 2005; Rose and Bailey, 2014; and Schwalbe and Zimmer, 2009). Also, there is a difference between vertical mergers, where two or more firms get together that were previously in a supplier-customer relationship and did not compete with each other,⁸⁴ and horizontal mergers, where firms get together that used to compete. Vertical mergers are less likely to reduce competition in a given market and trigger less concern on behalf of competition authorities.⁸⁵

An important tool in the assessment of the impact of a proposed horizontal merger is the Herfindahl-Hirschman Index of market concentration, which is used both in the EU and the US. The HHI is calculated by adding the squares of the market shares of all firms in a given market. For example, if a market has ten firms of 10% market share each, the HHI is $10 \times 10^2 = 1,000$. If there are only five firms of 20% market share each, the HHI is $5 \times 20^2 = 2,000$. If there is one firm of 50%, one of 30% and one of 20% market share, the HHI is $50^2 + 30^2 + 20^2 = 3,800$. Finally, a market with just one monopolist of 100% market share has an HHI of $100^2 = 10,000$. In general, markets with an HHI below 1,000 are considered to be unconcentrated, markets with an HHI between 1,000 and 1,800 are considered to be moderately concentrated, and markets with an HHI above 1,800 are considered to be highly concentrated.⁸⁶

When a merger between two firms is proposed, we can calculate the HHI before and after the merger to provide an assessment whether the merger will make a significant contribution toward a highly concentrated market. For example, if the market shares in a given market are 25%, 15%, and $12 \times 5\%$, the HHI is $25^2 + 15^2 + (12 \times 5^2) = 1,150$. If the biggest two firms were to merge, this would result in an HHI of $40^2 + (12 \times 5^2) = 1,900$, i.e. a highly concentrated market. By contrast, if the biggest firm would merge with one of the smaller firms, the HHI would be $30^2 + 15^2 + (11 \times 5^2) = 1,400$, a relatively modest increase in concentration. The result would be even clearer if

⁸⁴ Sometimes we also distinguish conglomerate mergers, where the firms were neither horizontal competitors nor vertical supplier-customers, for example if a financial services provider buys a diamond mine. Those are generally not problematic because the firms are not active in the same or at least connected markets and, therefore, cannot cause or strengthen the market dominance of one another. For detailed analysis see Goldberg, 1973, and Mueller, 1977.

⁸⁵ See European Commission, GUIDELINES ON THE ASSESSMENT OF NON-HORIZONTAL MERGERS UNDER THE COUNCIL REGULATION ON THE CONTROL OF CONCENTRATIONS BETWEEN UNDERTAKINGS, OJ 2008 C 265, p. 7, esp. paras. 23-27. See also Marco Colino, 2010.

⁸⁶ See Dep't of J. & Fed. Trade Comm'n, HORIZONTAL MERGER GUIDELINES 1.5 - 1.522 (rev. 1997).

the second firm were to merge with one of the smaller firms: $25^2 + 20^2 + (11 \times 5^2) = 1,300$.

The HHI is not the only measure, however, for the assessment of a suggested merger. Even firms with very large market share do not always have market power in the sense that they could be tempted to abuse their dominant position. In addition to market share, we must look at

1) the current structure of the respective market: The risk of abusive conduct by the merging firm(s) is smaller than their sheer size may suggest if the market is dominated by more than one large firm and there is a history of vigorous competition between them. In this respect, it is also of interest whether there is excess capacity in the market so that customers wanting to avoid abusive behavior by one firm will find others ready to satisfy their demand.

2) the potential future structure of the respective market, in particular the question of potential competition and whether there are significant barriers to entry in the given market. In general, abusive behavior, which is essentially the sale of average or below-average goods at above-average prices, will attract new competitors to enter the market because of the super-competitive profits that can apparently be made. As discussed above, the actual or even just the potential entry of new competitors curbs the market power of the dominant firm(s), unless there are insurmountable or at least very significant barriers to entry.

3) the structures of upstream and downstream markets: If the merging firm(s) are buying from powerful suppliers, they won't be able to impose abusive conduct on them. Similarly, if their customers are large and have purchasing power,⁸⁷ they will be able to resist potential abuse by the merging firm(s).

There are also potential positive effects of a merger that may have to be balanced against the undesirable move towards a more concentrated market. Positive effects may include *efficiency gains* due to economies of scale or the combination of complimentary technologic, financial, or other resources. It must be noted, however, that there has to be sufficient competitive pressure on the merging firm(s) to ensure that at least some of the efficiency gains will be passed on to consumers.⁸⁸ Last but not least, a merger that would normally result in a highly concentrated market and an overly dominant firm can nevertheless be permitted if one of the merger partners is a *failing firm*, i.e. a firm that would disappear as a competitor anyway.⁸⁹

⁸⁷ The EU Commission calls this "Countervailing Buyer Power", see European Commission, GUIDELINES ON THE ASSESSMENT OF HORIZONTAL MERGERS, OJ 2004 C 31, p. 3, paras. 64 et seq.

⁸⁸ Id. paras. 76-88.

⁸⁹ This was essentially the ratio for permitting the merger of Boeing and McDonnell Douglas in 1997. Although the merger involved the last two competitors in the U.S. in the market of large passenger aircraft and the combination of the no. 1 and no. 3 providers globally, it had become increasingly clear that McDonnell Douglas would not be able to survive on its own as a first tier commercial aircraft producer. Instead of preventing the merger and essentially forcing McDonnell Douglas out of the market, the competition authorities, at

2.3. Cartels and Other Forms of Collusion

If a firm does not actually have a dominant position in a given market and still tries to impose unfair conditions on its suppliers or consumers or any other form of abuse listed above, the market should take care of itself. Specifically, the frustrated suppliers or consumers will simply go to the competition to buy or sell goods or services of higher quality and/or lower prices. If the competition is effectively competing, that is. The market cannot take care of itself and rein in any attempts at abuse if the competition is no longer competing and instead colluding with the abusive firm. Therefore, Article 101 of the Treaty on the Functioning of the European Union prohibits cooperation between otherwise competing firms if it has as its "object or effect the prevention, restriction or distortion of competition ... and in particular those which:

(a) directly or indirectly fix purchase or selling prices or any other trading conditions;

(b) limit or control production, markets, technical development, or investment;

(c) share markets or sources of supply;

(d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts."

This is not the place to elaborate in detail about the various forms of abuse covered in this article. Some examples have already been given above, others can easily be found in case-law and literature. What is important, ultimately, is the understanding of the principle: We are always concerned with one and the same problem, namely any kind of abusive conduct in the market. If the market is highly concentrated, we have to control the conduct of the dominant firm(s). If the market is increasingly concentrated, we try to prevent mergers and thus the creation of dominant firms. If the market is not yet very concentrated, we just have to worry about collusion of otherwise competing firms because any one of them alone could not impose unfair conditions or other forms of abuse. Therefore, the new element to be dealt with in substantive law is the definition of prohibited forms of cooperation or collusion vs. other forms that are not (as) problematic.

As shown, the approach taken by the EU is to make all agreements between undertakings illegal if they have as their object or effect the prevention or restriction of competition. This is obviously very broad. If two or more competing firms agree to reduce their output to drive up prices or they just fix the prices straight away, they fall short of the

least in the EU, focused on reducing ancillary restraints on competition, in particular the practice of Boeing to enter into exclusive agreements with airlines for multi-annual periods of time. For details see Commission Decisions of 30 July 1997, Case No. IV/M.877 - Boeing/McDonnell Douglas, C(97) 2598 final, available online at http://ec.europa.eu/competition/mergers/cases/decisions/m877_19970730_600_en.pdf. For further analysis see also Clark and Ofek, 1994, as well as Mason and Weeds, 2002.

law, as they should. However, there are agreements between firms that reduce competition while also serving some legitimate commercial goals. For example, if BMW, Mercedes Benz or another luxury car manufacturer enters into a distribution agreement, the manufacturer typically grants the dealer exclusivity for a certain territory in exchange for commitments by the dealer to provide a high level of quality in sales and maintenance services, and to promote the brand in local and regional media. The territorial exclusivity is a restriction of competition since the manufacturer will turn away other interested dealers, even if they are qualified and willing to accept all obligations of the standard distributorship agreement. A further restriction may be a clause in the original agreement that prohibits the dealer from taking on other brands of automobiles. The restrictive agreement can nevertheless be overall beneficial. First, the dealer will not be willing to invest as much into a fancy showroom, expensive diagnosis and other tools, as well as training of mechanics, if return on such investments is uncertain because of an ever growing number of licensed dealers in the area. Second, the dealer will also not be willing to spend much money on advertising if the resulting sales have to be shared with free-riding dealers in the same territory. Essentially, the exclusive distributorship reduces intra-brand competition (between different BMW dealers), while at the same time increasing inter-brand competition (between the BMW dealer on the one hand and the competing Mercedes and Lexus dealers on the other). Other examples of agreements that reduce competition are exclusive licensing agreements, any kind of franchise or supply or distribution agreement with an element of exclusivity, and even agreements for joint research & development of expensive new technology. If all of those were always prohibited, we might end up with a situation where, for example, the development of fuel cells for use in cars could be abandoned or at least delayed by years because it might be too expensive for any one automobile manufacturer to develop on their own and cooperation between two or more would be illegal.

The EU and the U.S. have chosen different methods to accommodate agreements that have some anti-competitive but also some pro-competitive or otherwise beneficial effects. §1 of the Sherman Act simply states that “[e]very contract ... in restraint of trade or commerce ... is declared illegal.” In that respect it resembles the quoted passage of Article 101 TFEU and leaves the rest to the courts to resolve. Article 101 goes further than the statutory language of the Sherman Act, however, and explicitly provides that the prohibition of the first paragraph “may ... be declared inapplicable in the case of ... any agreement ... which contributes to improving the production or distribution of goods or to promoting technical or economic progress”. Last but not least, it provides three additional conditions for such declarations to be given, namely that consumers must receive a fair share of the benefit, no unnecessary restrictions on competition shall be imposed, and competition shall never be eliminated altogether.

In the EU, the exemptions are essentially granted by the Commission, that is the administra-

tion.⁹⁰ It may do so on a case by case basis but it has also adopted several legislative instruments, so called “Block Exemptions” to define entire categories of agreements that fall outside of the prohibition, as well as a number of conditions for that to happen.⁹¹ By contrast, in the U.S., a similar result is achieved via the case-law of the courts under the so-called “rule of reason” (Areeda, Kaplow and Edlin, 2004, at p. 113 et seq.). Needless to say, my recommendation for transitional and developing countries would be once again to follow the more clearly codified model of the EU, rather than the heavily case-based model of the U.S. (Stucke, 2009; Christiansen and Kerber, 2006).

2.4. Government Interference in the Market

In the three preceding sections, we analyzed how substantive competition law should prevent potentially abusive conduct by private actors in the market place. In this section, we have to shift our attention to potentially anti-competitive behavior by the state.

The government can influence firms and markets in a number of different ways: Primarily, the government charges different levels of fees for different kinds of economic activities via tax laws and licenses and the government adopts general legislation and administrative decisions to set the regulatory framework for all firms operating in its markets. Although legislative and regulatory decisions are often not economic decisions per se, they directly affect economic operators. Efficient allocation of resources requires on the one hand smart regulation by the government, for example with regard to the treatment of negative and positive externalities, and in general the promotion of efficient markets and technological progress. On the other hand, government regulation must be neutral and non-discriminatory to avoid interference with the forces of the market. For example, it simply does not make sense if a government buys the right to maintain trade protection for an inefficient domestic industry, say the textile industry in the U.S. or the agricultural sector in the EU, by offering special concessions to its trading partners in another sector of the economy. In the absence of a level playing field, an otherwise competitive industry may be pushed to extinction while an inefficient and

⁹⁰ The system was reformed and more responsibility was transferred from the Commission to the different undertakings with the adoption of COUNCIL REGULATION 1/2003 ON THE IMPLEMENTATION OF THE RULES ON COMPETITION LAID DOWN IN ARTICLES 81 AND 82 OF THE TREATY, OJ 2003 L 1.

⁹¹ For general block exemptions see COMMISSION REGULATION 330/2010 ON THE APPLICATION OF ARTICLE 101(3) TO CATEGORIES OF VERTICAL AGREEMENTS AND CONCERTED PRACTICES, OJ 2010 L 102, p. 1; COMMISSION REGULATION 1218/2010 ON THE APPLICATION OF ARTICLE 101(3) TO CATEGORIES OF SPECIALISATION AGREEMENTS, OJ 2010 L 335, p. 43; COMMISSION REGULATION 1217/2010 ON THE APPLICATION OF ARTICLE 101(3) TO CATEGORIES OF RESEARCH AND DEVELOPMENT AGREEMENTS, OJ 2010 L 335, p. 36); as well as COMMISSION REGULATION 772/2004 ON THE APPLICATION OF ARTICLE [101(3)] TO CATEGORIES OF TECHNOLOGY TRANSFER AGREEMENTS, OJ 2004 L 123, p. 11.

insufficiently competitive industry is artificially protected from having to downsize or exit from a market. General legislation and regulation should always be neutral and smart and any perceived or real need for special protection should be done via individual administrative decisions that are made public and provided with clear and transparent justifications for the exception to the rule.

Administrative decisions granting financial benefits or other special rights or privileges to specific firms or industries also come in many forms. Benefits may be in the form of direct financial transfers or subsidies. Similar effects can be achieved with tax breaks or via government procurement at higher-than-market prices. Or a government may allocate land or special rights or privileges, such as import- or operating licenses, without an open bidding procedure and at arbitrarily determined prices. The solution to all these problems is easy in theory and difficult in political reality. Again, efficient allocation of resources requires on the one hand smart decision-making, and on the other hand non-discriminatory decision-making. When state resources are given to private individuals or firms, whether in the format of direct financial contributions or in the form of rights and privileges of monetary value, they should be allocated efficiently. This usually requires a public tender procedure or a public auction. Direct negotiations with individual parties behind closed doors will invariably result in inefficient allocations and (accusations of) corruption.

Procedural and institutional guarantees are necessary to prevent circumvention of otherwise good laws. In particular in countries with a history of tribalism, ethnic strife, and/or corruption, the legitimacy and efficiency of institutions can be greatly enhanced via internationalization, either in the form of regular peer review by international experts or even in the form of international experts as appointed permanent members. For example, the Constitutional Court of Bosnia and Herzegovina, because of the recent ethnic warfare in this country, is still composed of six domestically elected judges plus three international judges who are appointed by the President of the European Court of Human Rights.⁹² As a result, if two of the ethnic groups would combine forces against the third, the two judges representing the third group, together with the three international judges, could put an end to this. Another example is the Lithuanian Centre for Quality Assessment in Higher Education.⁹³ Concerned with potential bias of national experts, it generally conducts the accreditation and re-accreditation procedures of all Lithuanian higher education institutions and degree programs with expert commissions composed of a majority of international experts. Similar structures could easily be created for competition authorities, procurement agencies, and similar institutions in transitional and developing countries! If such internationalized institutions and procedures are combined with a maximum level of transparency, i.e. widely

accessible and discussed reports and recommendations, as well as legal remedies in case of circumvention or non-compliance, many of the worst possible problems regarding state interference in the markets will already be taken care of.⁹⁴ Additional suggestions concerning effective enforcement will be discussed below.

3. WHY COMPETITION OVERSIGHT IS BETTER THAN COMPETITION LAW

Functioning institutions and procedures make the difference between laws that may well stay dead letter, and laws that will be effectively applied (Fox, 2010). Before they can benefit from internationalization, as outlined above, they must be suitably designed and equipped. Countries seeking to introduce robust competition oversight not only have to adopt the necessary substantive laws. Effective competition oversight is best accomplished via the creation of a single competition authority (Kovacic and Hyman, 2012; Sokol, 2010), versus several fragmented bureaus, with the necessary resources and a clear mandate

- to analyze markets in general and conduct studies of the current and the desirable or necessary level of competition;
- the power to investigate entire industries and/or individual firms, including the right to interrogate witnesses under oath and the right to search the premises and other facilities of companies and confiscate evidence;
- the ability to enforce its investigative powers if necessary, usually via lump sum or daily penalties for non-compliance or other forms of refusal to cooperate;
- the right to adopt decisions against one or more companies calling for behavioral and/or structural changes to rebuild workable or effective competition in a particular market;
- the right to adopt decisions to cease and desist anti-competitive conduct, to re-structure or divest a merger, and/or to effect other forms of lasting change;
- the ability to impose and enforce meaningful punitive decisions for past violations of competition rules;
- the right to enact interim or other urgent measures to prevent irreparable damage in case of ongoing violations of competition rules;
- the right to threaten significant penalties for any future violations of competition rules;

⁹⁴ Both OECD and UNCTAD offer support in this regard. See, for example, the UNCTAD Model Law on Competition, Geneva 2004. As all UN publications, this is available in Arabic, Chinese, English, French, Russian, and Spanish. Comparative analysis of the World Bank/OECD and UNCTAD model laws is provided by Lee, 2007.

Even more valuable may be the work of the International Competition Network (ICN), a cooperation program between a number of national competition authorities. The ICN provides a forum for exchange of experience and seeks to develop global best practice standards. See Hollman et al., 2012.

⁹² See Constitutional Court of Bosnia and Herzegovina, <http://www.ccbh.ba/eng/article.php?pid=1181&kat=503&pkat=509>.

⁹³ See Lithuanian Centre for Quality Assessment in Higher Education, <http://www.skvc.lt/en/?id=0>.

- and the authority to observe markets over extended periods of time and make repeated interventions if necessary.

In the exercise of its powers, the competition authority must be independent from political forces, which essentially means that there cannot be a supervisory function of the ministry of justice or the ministry of commerce or any other branch of the executive. Much like a central bank, the competition authority should be bound only by the law and accountable only to the courts. If necessary, this independence may have to be secured via the constitution (Jenny, 2012).

As indicated, the competition authority must dispose of suitable and sufficient human, physical and financial resources.⁹⁵ In particular, the institutional budget and the positions and salaries of the experts working for the competition authority, must be protected against politically motivated sanctions or cuts. One way of achieving this is to connect the budget and salaries to those of other state institutions, such as the courts or the different ministries via a rule that any institutional budget and individual salary changes, up or down, must be in line with the changes at the other institutions. If the competition authority is deemed to need additional resources and/or the ability to pay higher salaries than those at other government agencies,⁹⁶ one way of achieving this can be via a rule that allows the competition authority to keep a percentage of the fines it imposes for the enforcement of the competition rules. Transparency and judicial review mechanisms should be in place, however, to provide legitimacy and safeguards against potential abuse by the authority.

In addition to drafting help with actual substantive rules, technical assistance in the development of effective and efficient administrative structures is another prime example where more developed countries can make an impact in developing and transition economies without having to commit huge amounts of money or many years of involvement on the ground (Sokol and Stiegert, 2010; Geradin, 2004).

4. WHICH PRIORITIES TO SET IN A DEVELOPING OR TRANSITION ECONOMY

Both the EU and the U.S. needed decades to develop the sophisticated levels of competition oversight we find today. Transitional and developing countries can follow the same course and essentially develop substantive laws, procedural laws, suitable designs and powers for competition authorities, as well as institutional and procedural rules for specialized courts, on their own in a kind of trial-and-error fashion. Naturally, the process can be accelerated by involvement of international consultants. However, the mere fact that alternative rules and institutional designs are being discussed in the national political

⁹⁵ On this subject see, for example, Serebrisky, 2004. See also the discussion below, in part 4., of the experience in a number of developing countries in recent years.

⁹⁶ This was done, for example, at the Egyptian Competition Authority, to enable this public body to recruit and retain highly qualified lawyers and economists would not have come for regular Egyptian civil service salaries. For more information see <http://eca.org.eg/>.

process gives ample opportunity to different interest groups to throw spanners into the works. At the very least, they may be able to delay the creation of a robust system of competition oversight by a couple of years. Not infrequently, however, these political or economic players are able to introduce loopholes or structural weaknesses into the laws that permanently cripple the efforts of the newly created institutions.

The risk of delay, dilution, and debilitation can be much reduced if a transitional or developing country limits its discretionary decisions by opting to follow an existing and proven model. For example, if a country takes the strategic decision to use the EU system as its model, it can adopt a comprehensive set of substantive and procedural rules and will only have to determine how to apply the criterion of “may affect trade between Member States”,⁹⁷ as well as the length of different transition periods for the development of the competition authority, the judicial review mechanisms, and the application of the substantive laws to the different industries and sectors of the economy. To the extent some provisions of the transplanted legal system⁹⁸ turn out to be poorly suited for the transition and/or development context, fine-tuning will need to be done, as with every statutory or common law rule. A question that is too large to be dealt with here but definitely deserves further analysis is whether developing countries can and should adjust competition laws to specifically promote poverty reduction (Fox, 2006; and Fox, 1989).

5. HOW COMPETITION LAW MUST BE EMBEDDED IN A LEGAL SYSTEM

Competition law cannot thrive without context. We may distinguish the closer context of administrative law, of which competition law is a part, and the broader context of the legal system as a whole, including such areas as consumer protection (Kirkwood, 2013), environmental protection, and other areas dealing with externalities.

In the context of administrative law, robust competition oversight depends on an existing or at

⁹⁷ This clause is found both in Article 101 and 102 TFEU, and in the form of “[having] a Community dimension” also in COUNCIL REGULATION 139/2004 ON THE CONTROL OF CONCENTRATIONS BETWEEN UNDERTAKINGS, OJ 2004 L 24, p.1.

⁹⁸ I am well aware of the undying discussion in academic circles of the possibility and desirability of “legal transplants”. It would certainly be foolish to try to transplant specific rules or mechanisms from one legal system into another without any adjustments. However, like good surgeons will be able to select suitable organs for a transplant and prepare both the imported organ and the receiving organism for the operation to ensure success, a good expert team should be able to achieve a similar result in the legal field and potentially save a country from years and years of experimentation, let alone permanently dysfunctional mechanisms. For further discussion see, for example, Ajani, 1995; Berkowitz et al., 2003; Berkowitz et al., 2003a; Clarke, 2006; Dunning and Pop-Eleches, 2004; Garoupa and Ogun, 2006; Grajzl and Dimitrova-Grajzl, 2009; Graziadei, 2007; Kahn-Freund, 1974; Kingsley, 2004; Legrand, 1997; Mattei, 1994; Miller, 2003; Pistor et al., 2003; Schauer, 2000; Smits, 2003; Teubner, 2001; and Watson, 1993.

least evolving culture of good governance and rule of law.⁹⁹ Systemic problems of maladministration, institutional inefficiencies, and corruption, cannot be fixed by way of judicial review. The courts have neither the capacity, nor the expertise, or even the mandate, to do or re-do everything the administration should have done or should have done differently. Judicial review is suitable only to catch and correct the occasional slip and the most egregious problems (Tapia and Montt, 2012). It is essential, therefore, that all branches of the administration work together to develop a culture of law and government¹⁰⁰ that is focused on service to society, respect for human rights and fundamental freedoms (Andreangeli, 2008), pursuit of individual justice, and the assurance of transparency and personal integrity in matters large and small. Egypt is an example where a new, dynamic, well-intended and well-funded competition authority is being frustrated, and arguably failing, in the face of otherwise widespread administrative inefficiency and corruption.¹⁰¹ One specific problem in Egypt is the fact that enforcement of the decisions of the Egyptian Competition Authority (ECA) is entrusted to the normal prosecution service and judicial oversight is provided by the criminal courts. While the staff members of the ECA are specially trained lawyers and economists, the prosecutors and judges apply their normal standards regarding evidence, i.e. that the accused is innocent until proven guilty and proof needs to be “beyond a reasonable doubt”. There may also be a level of resentment among the regular and seasoned judges and prosecutors against the highly paid whiz kids at the ECA. As a result, more than a couple of cases that had been painstakingly put together by the ECA over many months fell apart at the enforcement stage either because the prosecutors were entirely unwilling to open a case or because the courts did not see a sufficient level of proof to impose the measures sought by the ECA. One consequence is a system that is at least partly dysfunctional. Another is a high level of frustration and attrition at the ECA. While Egypt may provide lessons of how *not* to introduce competition oversight,¹⁰² the reforms enacted in India since 2007 seem much more in line with the recommendations in this essay and, therefore, an example of how to get the job done

successfully.¹⁰³ Turkey seemed to be on the right path as well (Aydin, 2012). Latin American countries seem to be somewhere in the middle, with some good and some not so good examples.¹⁰⁴

In the broader context, countries can and should pursue a multi-pronged approach toward promotion of economic efficiency and growth. In particular, if a domestic market is small and the number of competitors in many industries is limited, the opening of borders via trade liberalization can noticeably enhance import competition and, thereby, reduce the market power of established industries. Other ways of enhancing competition include the promotion of transparency, for example via the creation and/or subsidization of consumer organizations and independent product testing agencies, requirements of clear disclosure of prices and fees, and other fair labeling rules. Transparency goes up and transaction costs go down if the government provides or supports fast internet service at reasonable prices and ensures lively competition in the market for parcel and package delivery and transport services.

If some markets turn out to be impervious to soft support measures and/or trade liberalization, the government can also resort to subsidies for infant industries or compulsory licenses to reduce the power of established industries, in particular if the latter have been abusing their power and the competition authority has not been able to improve the structure of the respective market with the normal tools at its disposal. Natural monopolies and undertakings providing services of general economic interest in a framework of general service obligation usually need to be tightly regulated and strictly supervised to ensure efficient allocation of resources for the benefit of high quality at low prices. Internationalization of institutional oversight may help if too many personal and institutional links on the domestic level pollute the relationship between the government and the governed in this context.

6. WHY EFFECTIVE ENFORCEMENT IS EVERYTHING

The best laws and the most admirable institutions remain useless if they lack the ability to adopt and enforce effective decisions. In the area of competition oversight, we find three options for the enforcement of the law. First, there is the administrative option prioritized by the EU. This requires a powerful and independent competition authority with meaningful investigative powers and

⁹⁹ The term “rule of law” has become at the same time more popular and ill-defined. For a systematic discussion of different definitions and the proposal of a better model see Emmert, 2008, especially pp. 551-569.

¹⁰⁰ The problem of legal culture, in particular the difference between common law countries emphasizing case-law and most other countries emphasizing statutory law, is discussed in Ma, 2012. The influence of the political system, the political ideology, and the approach to the rule of law on the adoption of competition laws – but not their application and enforcement – was compared for 183 countries in Parakkal, 2011.

¹⁰¹ See, for example, El Dean and Mohieldin, 2001; Ghoneim, 2002; and more recently Afifi, 2010. See also Geradin, 2004, for a critical assessment of competition enforcement by the Mediterranean Partners of the EU and an appeal for alignment of the competition laws in the region with those of the EU, as well as more technical assistance by the EU.

¹⁰² For more information on the Middle East see Dabbah, 2012.

¹⁰³ See, for example, Damtoft and Bhasin, 2011; Fox, 2006-2007; Mehta and Agarwal, 2006; Ramappa, 2013; as well as Singh, 2013. For a much more critical view see Bhattacharjea, 2008.

¹⁰⁴ The overly complicated institutional structure in Brazil is currently under review, see Calliari, 2011; as well as Ribeiro Todorov and Torres Filho, (2012). See also Mendes de Paula, 2007, with further references. Mexico is already a step ahead in the modernization process, see Castaneda, 2011, and Pérez Motta, 2007. See also Fox and Sokol, 2009; as well as Alvarez and Horna, 2008. Issue 1 of 2008 of the Chicago Kent Law Review contains a number of competition law related contributions to a symposium about law and economic development in Latin America.

the ability of imposing substantial penalties. As is well known, the EU Commission does indeed have these powers. It is authorized and equipped not only to analyze markets in a theoretical way but to go out on so-called “dawn raids” to investigate enterprises in the field. The Commission officials must be given access to premises and answers to questions. They can and regularly do search offices for documents and other evidence and they can confiscate computers, files, and other data storage media (Regulation 1/2003, Articles 17-22¹⁰⁵). To enforce its decisions and to penalize anti-competitive conduct, the Commission can impose periodic penalties of up to 5% of the average daily turnover of the enterprise, for example for every day until certain documents are surrendered, as well as fines of up to 10% of the total turnover of the enterprise in the previous year (Regulation 1/2003, Articles 23, 24). The highest fine against an individual enterprise adopted on this basis so far has been the fine of 1.45 billion US\$ against the computer chip manufacturer Intel,¹⁰⁶ arguably a sanction that even a large multinational corporation will not pay from petty cash and disregard.

The second option for the enforcement of competition law is the private or tort law option. Although it is possible in the EU for competitors, suppliers or customers to bring tort cases and collect compensation for proven damages from an enterprise that has violated competition rules, this route is rarely taken in practice, largely because of the difficulties in securing clear evidence of the violation and in calculating and proving the damage.¹⁰⁷ By contrast to the EU, the U.S. provide much broader powers for a plaintiff to collect evidence from competitors and other firms in the so-called pre-trial discovery procedure, and the U.S. provide the possibility of collecting treble damages, i.e. three times the amount of the proven damages. This makes private enforcement of antitrust law attractive in the U.S. (Cavanagh, 2010) and, indeed, the primary tool next to relatively weaker administrative instruments of the Federal Trade Commission (Gavil, Kovacic and Baker, 2008; Ginsburg, 2005).

Finally, there is the criminal law option of holding the management of a firm personally liable for anti-competitive conduct and imposing jail sentences against the worst offenders. This is widely considered particularly effective because the managers as employees may like to take the bonuses for earning super-competitive profits but they won't like to do time in jail for having made the extra money for their shareholders. By contrast, it is not clear how and why criminal sanctions against the companies themselves should be of use. Since legal persons do not go to jail, the sanctions will usually be financial penalties and those could be more easily imposed in administrative procedures where a lower

threshold for the required proof applies (Beaton-Wells, 2012).

While each of the three options for enforcement has its strengths and weaknesses, recent experience shows that private enforcement works best as a complementary tool when the necessary investigations have already been done and the evidence has been secured by a powerful and sophisticated competition authority. Criminal enforcement may be another complementary tool but most not be the only tool in the box because of the higher standards of proof it requires. Ultimately, a transitional or developing country should probably avail itself of all three methods of enforcement.¹⁰⁸ It must be clear beyond any doubt, however, that the key to success will be in the hands of a well-appointed competition authority.

7. CONCLUSIONS

Every country which currently does not enjoy robust and effective competition oversight of all sectors of the economy stands to gain from introducing or improving such a system. Successful introduction or reform requires i) sophisticated definitions and provisions in substantive law, ii) clear and fair administrative procedures, iii) a well-designed and well equipped competition authority (Trebilcock and Iacobucci, 2010), and iv) competent judicial review. The stool has four legs and will not do its job if one or more of these legs are missing or defective. The necessary legislative and administrative changes are complicated. Considerable resources have to be invested, in particular for the training of administrative and judicial staff. As a whole, the hurdles to be overcome may well seem daunting for transitional and developing countries (Gal, 2010). However, the prize is well worth the effort, namely the accelerated growth of the economy and the broader distribution of wealth.¹⁰⁹ Fortunately, there are models that can be followed and advice that can be purchased second hand, for example the European Union rules on competition supervision, including the enforcement via the EU Commission and judicial review via the European Court of Justice. Furthermore, help for legislative drafting, administrative and court reform, and training of competition experts can be obtained from a variety of governmental and non-governmental sources in the Western developed nations. The EU Commission, in particular, has a lot of experience in this regard, after having supported eleven Central- and Eastern European Countries (CEECs) in their preparation for EU membership, which included a focus on the development of functioning systems of competition supervision.¹¹⁰ In conclusion, we can say that a country that seriously wants to improve its economy by reinforcing its competition rules can certainly do so and obtain qualified support to get things right. The only question that remains is whether a country – or rather its political and business leaders – really want to develop an economy that works to provide the best possible goods and services to the largest possible number of users at the lowest possible

¹⁰⁵ See COUNCIL REGULATION 1/2003 ON THE IMPLEMENTATION OF THE RULES ON COMPETITION LAID DOWN IN ARTICLES [101] AND [102] OF THE TREATY, OJ 2003 L 1, p. 1, in particular Articles 17-22.

¹⁰⁶ See Case COMP/C-3/37.990 - Intel, Commission Decision (13 May 2009), OJ 2009 C 227, p. 13-17.

¹⁰⁷ For a somewhat more optimistic perspective see Friederiszick and Röller, 2010; as well as Basedow, et al., 2011.

¹⁰⁸ For further analysis see Baker, 2012.

¹⁰⁹ The best collection of essays on this point is probably by Sokol, Cheng and Lianos, 2013.

¹¹⁰ Doleys, 2012; See also above, note 53.

price, or whether they would rather continue their abuse of dominant positions, price fixing cartels, and other ways of exploiting their market power and ultimately their people.

Annex I - 75 Countries Which Introduced Competition Oversight for the First Time After 1990.

Annex II - 30 Countries Which Have Substantially Revised and Upgraded Competition Oversight Since 1990.

Both annexes are available for free download - like most of the authors publications - at https://www.researchgate.net/profile/Frank_Emmert_2.

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