Introduction

This publication includes the documentation presented at the eighth Global Forum on Competition held in Paris in February 2009.

Overview

The programme of the Forum included four main sessions on Competition Policy, Industrial Policy and National Champions, Competition Policy and the Informal Economy, the Challenges Faced by Young Competition Authorities, and the Role of Competition Authorities in the Response to Economic Crisis (Food Prices and Supply, Energy Prices, Market Crises).

Related Topics

- Competition Policy, Industrial Policy and National Champions (2009)
- Competition Policy and the Informal Economy (2009)
- The Interface between Competition and Consumer Policies (2008)
- Competition Policy and Concessions (2007)
- Concessions (2006)
- Peer Review of Chinese Taipei (2006)
OECD

GLOBAL FORUM
ON COMPETITION

Eighth Meeting
19 - 20 FEBRUARY 2009

COUNTRY CONTRIBUTIONS
SESSIONS 1 AND 2
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**COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL CHAMPIONS**

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#### SESSION II

**COMPETITION POLICY AND THE INFORMAL ECONOMY**

Call for Contributions
Appel à contributions

**Written Contributions**

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Presentations by

Siddhartha Mitra
Rita Ramalho
SESSION I

COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL CHAMPIONS
CALL FOR CONTRIBUTIONS
Dear GFC Participant,

The OECD Global Forum on Competition will hold a roundtable on 19 February, 2009, to discuss the relationship between competition policy, industrial policy and national champions. You are invited to make a written submission by 10 January at the latest.

An often-articulated goal of competition policy is the protection of competition, not competitors. Policies that support this concept are thought to promote consumer welfare, choice and efficiency. Industrial policy that creates or favours national champions may purport to have the same goals, yet it often conflicts with competition policy.

Policy proposals, laws and regulations supporting national champions are often associated with a firm or industry that is considered strategically important to the nation or which may be experiencing some financial pressure. Governments may directly support the growth of an emerging or established industry or firm based on the view that success in these markets requires critical mass that will not be gained through normal market processes, or that there are key markets in which a nation must have a viable player.

Intensive coordination between companies that would otherwise be competitors, mergers that create market power, selective purchasing or selling policies, the creation of barriers to entry and import restrictions and market distortions caused by state aids or subsidies are examples of ways in which industrial policy may restrict competition and harm consumers. Competition agencies, may also have concerns about the influence that special interest groups may be able to bring to bear on governments to promote and protect certain firms or sectors from competition at the expense of consumers.

Such apparent conflicts between competition and industrial policy may be less significant if they result from efforts to correct market failures, foster economic development or incorporate wider strategic considerations. Market failures, for example, can lead to under or over investment in individual markets, and governments may be able to improve market performance by correcting such failures. In these situations, industrial policy may be consistent with enhancing long-term consumer welfare and efficiency and may therefore be thought to sit comfortably with competition policy.

The effectiveness and value of the roundtable will be greatly strengthened by written contributions from participants based on their own experiences. It would be particularly helpful if written contributions include case studies.

To help you to prepare your contribution, a number of issues and questions are attached that you should feel free to respond to and discuss in your submission. This is not intended to be a restrictive or comprehensive list. Participants are encouraged to raise and address other issues based on their own experience. A suggested bibliography is attached, as well.
Please advise the Secretariat by 15 December at the latest if you will be making a written contribution. Written contributions are due by 10 January at the latest. Failure to meet that deadline could result in a contribution not being taken into account in the scenario to be prepared for the roundtable. Late contributions may also not be distributed to participants over the internet at www.oecd.org/competition/globalforum in a timely fashion in advance of the meeting.

All communications regarding documentation for this roundtable should be sent to jennah.huxley@oecd.org, Tel. 33 1 45 24 85 55; Fax 33 1 45 24 96 95, with a copy to helene.chadzynska@oecd.org (GFC Programme Manager); Ken Danger, Senior Economist, would be pleased to answer any substantive questions you may have about the roundtable. His phone number and e-mail address are: 33 1 45 24 82 50 and ken.danger@oecd.org.
Questions for Consideration

History and Evaluation

1. To what extent does the industrial policy in your country target firms on the basis of their nationality (e.g., by granting state aids/subsidies to national firms only, or by controlling their ownership)? If so, how is nationality defined?

2. What economic conditions have been associated with government industrial policy and support for national champions in your nation and region? Has this changed over time as economic development advanced?

3. Are there major success stories of industrial policy or national champions that are prominent in policy discussions? Are there any perceived major failures of industrial or national champion policies? How do you define “success” and “failure” in this context? Are successful national champion stories supported by best practice competition policy standards?

4. Does your competition agency use benchmarks to assess the economic costs and benefits of government interventions that promote industrial policy or national champions? Have you communicated benchmarks to other economic policy makers? Is there any dependable analytical approach that allows you to distinguish industrial policy from competition policy? Do you engage in competition advocacy in this policy area?

5. Have merger review laws ever been suspended in your country? If so, why? Were concerns expressed either explicitly or implicitly about the way in which merger efficiencies are typically examined or in the way in which failing firms are analysed?

6. Have any of your decisions ever been overridden on grounds of industrial policy? Are there any recent examples? What reasons were given? To what extent had the competition agency already considered the market characteristics or considerations that were the basis for the override? What have been the consequences of the override for consumers and competition policy?

7. Does your government implement some policies directly dedicated to innovation? If so, could you specify the sectors that benefit from these policies as well as the instruments used to foster innovation?

8. Did measures adopted in your country to deal with the recent economic crisis raise competition concerns? If so, could you describe the measures and the concerns? Have these competition concerns been taken into account, and, if so, how? In particular, have initial proposals been amended in order to comply with competition law? Have some of these measures been exempted from competition policy scrutiny?
Means and Goals

1. Please specify whether any of the following are instruments of industrial policy in your country:
   - Government procurement
   - Exemptions from antitrust laws
   - Regulatory barriers to competition
   - Access to credit
   - Arranged mergers and acquisitions
   - Control of acquisitions of national companies by foreign investors
   - Other?

2. To what extent are industrial policies in your country motivated or rationalised as regional or national economic development initiatives? Has this explanation been used more sparingly over time as your economy expanded?

3. To what extent are industrial policies motivated or rationalised as an effort to help domestic firms withstand the exercise of market power by foreign firms? How does this rationale square with rules against market distortions caused by state aids? How has your competition agency analysed these circumstances?

4. Are industrial policies motivated or rationalised as a means to correct market failures in your country? If so, what types of market failures have been involved? How do you compare industrial policy or national champions with other policy approaches for correcting these market failures (such as taxes or subsidies on consumption of the product)?

5. Do you think that one nation engaging in industrial policy or supporting national champions attracts retaliation from other nations? To what extent are projected gains from industrial policy and national champions dependent on other nations not pursuing these policies, too? Do industrial policy and national champions constitute a “prisoners’ dilemma” situation?
SELECTED REFERENCES:


APPEL À CONTRIBUTIONS
À TOUS LES PARTICIPANTS AU FORUM MONDIAL

Objet : politique de la concurrence, politique industrielle et champions nationaux

Forum mondial sur la concurrence (19-20 février 2009)

Session I

Madame, Monsieur,

Le Forum mondial de l’OCDE sur la concurrence tiendra une table ronde le 19 février 2009 pour examiner les liens entre politique de la concurrence, politique industrielle et champions nationaux. Nous vous prions de bien vouloir transmettre une contribution écrite d’ici au 10 janvier au plus tard.

L’un des objectifs les plus fréquemment cités de la politique de la concurrence concerne la protection de la concurrence en elle-même et non celle des concurrents. On estime que les politiques qui respectent ce principe œuvrent en faveur du consommateur, de la liberté de choix et de l’efficience. Si la politique industrielle qui engendre ou favorise les champions nationaux peut prétendre aux mêmes objectifs, elle est souvent en contradiction avec la politique de la concurrence.

Les propositions de mesures, lois et réglementations en faveur des champions nationaux sont souvent associées à une entreprise ou à un secteur considéré comme stratégique pour l’économie nationale ou confronté à des pressions d’ordre financier. L’État peut soutenir directement la croissance d’une entreprise ou d’un secteur émergent ou établi en s’appuyant sur la théorie selon laquelle pour réussir sur le marché concerné, il est nécessaire d’atteindre une taille critique qui ne pourra être obtenue par le biais des mécanismes de marché traditionnels ou qu’il existe des marchés sensibles qui requièrent au moins un acteur national viable.

Coopération étroite entre des entreprises qui devraient normalement se faire concurrence, fusions renforçant le pouvoir de marché, politiques sélectives d’achat ou de vente, instauration de barrières à l’entrée et de restrictions à l’importation, distorsions de marché suscitées par des aides ou des subventions de l’État : autant d’exemples par lesquels la politique industrielle peut limiter la concurrence et nuire aux consommateurs. Les autorités de la concurrence peuvent également s’interroger sur l’influence que peuvent exercer certains groupes de défense d’intérêts catégoriels sur les gouvernements en vue de soutenir et de protéger certaines entreprises ou certains secteurs de la concurrence, au détriment des consommateurs.

Il est possible de limiter les conflits apparents entre politique de la concurrence et politique industrielle en menant des efforts pour pallier les défaillances du marché, encourager le développement économique ou prendre en compte des considérations stratégiques plus larges. Par exemple, les défaillances de marché peuvent se traduire par un déficit ou un excédent d’investissement sur certains marchés : les pouvoirs publics peuvent donc améliorer les performances du marché en corrigeant ces défaillances. Dans de tels cas, la politique industrielle peut se concilier avec l’amélioration du bien-être du consommateur à long terme et l’on peut considérer qu’elle est en harmonie avec la politique de la concurrence.

La qualité et l’utilité de la table ronde se trouveront grandement renforcées par des contributions écrites des participants, fondées sur leurs propres expériences. Il serait particulièrement utile d’inclure des études de cas dans chaque contribution.
Afin de vous aider à préparer votre contribution, vous trouverez ci-joint un certain nombre de questions auxquelles vous pourrez répondre librement et que vous pourrez développer. Cette liste n’a pas pour objet d’être restrictive ni exhaustive. Les participants sont invités à évoquer et à traiter également d’autres questions, en fonction de leur propre expérience. Vous trouverez aussi ci-joint une proposition de bibliographie.

Si vous envisagez de présenter une contribution écrite, vous êtes prié d’en aviser le Secrétariat d’ici le 15 décembre au plus tard. Les contributions écrites devront parvenir avant le 10 janvier. Si cette date limite est dépassée, votre contribution risque de ne pas être prise en compte dans la préparation de la table ronde. Les contributions qui seront transmises en retard pourraient également ne pas être diffusées aux participants sur le site www.oecd.org/competition/globalforum en temps voulu avant la réunion.

Toutes les contributions pour cette table ronde doivent être envoyées à jennah.huxley@oecd.org, tél. 33 1 45 24 85 55, fax 33 1 45 24 96 95, avec copie à helene.chadzynska@oecd.org (Responsable du programme sur le Forum mondial sur la concurrence). Ken Danger, Économiste principal, se fera un plaisir de répondre aux questions de fond que vous pourriez avoir à poser à propos de la table ronde. Son numéro de téléphone et son adresse électronique sont les suivants : 33 1 45 24 82 50, ken.danger@oecd.org.
Questions à examiner

Historique et évaluation

1. Dans quelle mesure la politique industrielle mise en œuvre dans votre pays cible-t-elle les entreprises en fonction de leur nationalité (par exemple en accordant des aides/subventions de l’État aux entreprises nationales uniquement ou en contrôlant leur actionnariat) ? Dans ce cas, comment est définie la nationalité de l’entreprise ?

2. Quelles sont les conditions économiques associées à la politique industrielle et au soutien des champions nationaux par l’État dans votre pays et dans votre région ? Ces conditions ont-elles évolué parallèlement au développement économique ?


4. L’autorité de la concurrence de votre pays utilise-t-elle des critères de référence pour évaluer les coûts et les bénéfices économiques des interventions de l’État visant à soutenir la politique industrielle ou les champions nationaux ? Avez-vous communiqué des critères de référence à d’autres responsables de la formulation de la politique économique ? Existe-t-il une méthode d’analyse fiable pour faire la distinction entre politique industrielle et politique de la concurrence dans votre pays ? Participez-vous à la défense des principes de la concurrence dans ce domaine ?

5. La législation sur le contrôle des fusions a-t-elle déjà été abrogée dans votre pays ? Si oui, pourquoi ? A-t-on exprimé des inquiétudes, de manière implicite ou explicite, sur la manière dont les avantages de la fusion sont examinés ou dont les entreprises en difficulté sont analysées ?

6. L’une de vos décisions a-t-elle déjà été annulée pour des motifs liés à la politique industrielle ? Pouvez-vous fournir un exemple récent ? Quelles sont les raisons qui ont été données ? Dans quelle mesure l’autorité de la concurrence avait-elle déjà examiné les caractéristiques ou les considérations de marché invoquées pour justifier cette annulation ? Quelles ont été les conséquences de cette annulation pour les consommateurs et la politique de la concurrence ?

7. Votre gouvernement a-t-il mis en œuvre des politiques directement dédiées à l’innovation ? Si oui, pouvez-vous spécifier les secteurs bénéficiant de ces politiques et les instruments utilisés pour encourager l’innovation ?

**Moyens et objectifs**

1. Veuillez indiquer si l’un des instruments ci-dessous est utilisé dans le cadre de la politique industrielle dans votre pays :
   - Marchés publics
   - Exemptions vis-à-vis du droit de la concurrence
   - Barrières réglementaires à la concurrence
   - Accès au crédit
   - Fusions et acquisitions concertées
   - Contrôle du rachat des entreprises nationales par des investisseurs étrangers
   - Autre ?

2. Dans quelle mesure les politiques industrielles mises en œuvre dans votre pays sont-elles considérées comme des initiatives de développement économique régionales ou nationales ? Le recours à cette explication a-t-il diminué au fur et à mesure de l’expansion de votre économie ?

3. Dans quelle mesure les politiques industrielles sont-elles considérées comme un effort visant à aider les entreprises nationales à faire face à la puissance des entreprises étrangères sur le marché ? Comment justifier cette stratégie par rapport à la réglementation visant à lutter contre les distorsions de marché causées par les aides de l’État ? Quelle est l’analyse de l’autorité de la concurrence de votre pays ?

4. Les politiques industrielles sont-elles considérées comme un moyen de pallier les défaillances de marché dans votre pays ? Si oui, quels sont les types de défaillances de marché concernés ? Selon vous, la politique industrielle ou le soutien aux champions nationaux sont-ils plus efficaces que d’autres mesures (comme les taxes ou les aides sur un produit) pour corriger ces défaillances ?

5. De votre point de vue, est-ce qu’un pays qui mène une politique industrielle active ou soutient ses champions nationaux s’expose à des mesures de représailles de la part d’autres pays ? Dans quelle mesure les bénéfices d’une politique industrielle active ou d’un soutien aux champions nationaux dépendent-ils de l’absence de mesures de représailles de la part d’autres pays ? La politique industrielle active et le soutien aux champions nationaux correspondent-ils à des situations caractéristiques du « dilemme du prisonnier » ?
BIBLIOGRAPHIE


THE RELATIONSHIP BETWEEN COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL CHAMPIONS

-- Brazil --

1. Introduction

1. The interaction between industrial and competition policies in Brazil is recent and derives from the change of perspective that has occurred in the nineties within the eternal dispute between interventionists and liberals. Indeed, although the main objective of competition policy is not to help companies to increase their competitive power, it can foster competition working in convergence with the industrial policy.

2. Said connection between competition and industrial policies is feasible and based on the institutional and legal convergence, as much as on the economic literature. Therefore should not be taken as a tension between policies, as it is many times alleged. This discussion is again been stimulated due to the financial crisis as much as the debate on the national champions and on the industrial policies based on vertical intervention.

3. In Brazil, industrial policy has been being implemented for many years while competition policy is relatively young.

4. Apart from their respective specific objectives, industrial and competition policies have the common goal of enhancing dynamic competitive advantages in markets increasingly integrated. Notwithstanding, the Brazilian experience shows that competition plays an important role to industrial policy although it may not be a sufficient mechanism to achieve all its goals. This interaction depends on facing competition as a dynamic process towards a highly competitive environment. The Brazilian Government is working on a policy model that fosters the convergence between industrial policy and competition policies, as per described in this paper.

2. The historical context

5. From the end of the Second World War to the beginning of eighties, Brazil started an industrialisation process based on import substitution and the alliance between national and foreign private capital. For the first time, industrialisation entered the political and economical agenda in Brazil. New political actors came to the scene, as industrial and labor associations, and the economic policy reflected this new political perspective. The nationalist development and the state interventionism prevailed, amalgamating political forces to economical objectives of the industrialising project.

6. These interventionist policies created state owned companies in order to foster economic activities considered essential to the national development. These companies turned into national champions as Petrobras (the Brazilian oil producer with refineries, production and exploitation areas, pipelines, and terminals), CSN (the Brazilian Steel Company), Vale do Rio Doce (the Brazilian mining company) among other champions that were always promoted as being necessary for strengthening the national sovereignty and security.

7. In 1988 a new Constitution was launched “founded on the appreciation of the value of human work and on free enterprise, (and) is intended to ensure everyone a life with dignity, in accordance with the
dictates of social justice” as much as established that the “free exercise of any economic activity is ensured to everyone, regardless of authorization from government agencies, except in the cases set forth by law.”

8. Therefore, the end of the eighties and the nineties symbolized a change from direct interventionist policies towards indirect intervention based on regulation, what represented a transformation to the development standards in Brazil.

9. This transformation happened not only on the industrial policy orientation, but also on all the public policies. Through this perspective, social policies were redrafted, inflation was controlled, economy was opened, companies were privatised and governmental agencies were created in order to regulate some sectors (telecommunications, electricity, petroleum, etc).

10. The “Collor Plan”\(^2\), a collection of economic reforms which combined fiscal and trade liberalisation with radical inflation stabilisation measures carried out between 1990 and 1992, was launched among other programs, as the privatisation one, the "National Privatization Program" (“PND”), and the industrial and foreign trade reform program, the “Industrial and Foreign Trade Policy” (“PICE”), which aimed to stimulate the entry of foreign companies; meanwhile, innovation was motivated by commercial opening through non-tariff barrier reduction, targeting oligopolised sectors of the economy.

11. Later on, still with the selective protection of certain key industries and the fail of the stabilisation strategy and the presidential impeachment, inflation and fiscal problems appeared again. A new plan was launched in 1994, the “Real Plan”, and represented a milestone to the economic development standards in Brazil, that was influenced by the guidelines established on the Washington Consensus. The Real Plan proposed a new fiscal strategy, a monetary reform and continued to envision the economy opening, managing to decrease inflation.

12. Among with the aforementioned changes promoted in 1994, Law #8.884/94 was enacted and changed the Administrative Council for Economic Defense (CADE) into an independent agency\(^3\), regulated other antitrust measures, and aimed to create a competition culture between producers and consumers in which competition rules are mandatory to guarantee the existence of the free market. These objectives, however, were just consolidated in the last decade.

13. The industrial policy has grown stronger as of 2002, during President Lula’s government, with the policies called “Industrial, Technological and Foreign Trade Policy” (PITCE), and “Policy for Productive Development” (PDP), aiming to strengthen and expand the Brazilian industrial sector trough an improvement on companies innovative capacity in a long term strategy.

14. Furthermore, the Brazilian National Agency for Industrial Development (“ABDI”) was created in 2004 in order to execute the projects of said development policy, which acts jointly with the Finance Ministry and the Brazilian Development Bank (BNDES).

15. The PDP aims to continue the advances promoted by the PITCE, amplifying its objectives and consolidating the ongoing actions and the capacity of implementing and evaluating the industrial policies, through a long term strategy, as per described above. Said Plan was developed under the leadership of the Brazilian Ministry of Development, Industry and Foreign Trade and has four horizontal macro targets: (i)

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2. The Color Plan was officially called New Brazil Plan, but it became closely associated with the former President, Fernando Collor de Mello himself, and therefore was names “Collor Plan”
3. CADE was created in 1962, but the Council had marginal economic impact.
expansion of fixed investment; (ii) raising private expenditure in research and development (R&D); (iii) expansion of exports; (iv) making Small and Micro Enterprises (SMEs) more dynamic. These targets were divided in three different levels: (i) systemic actions, which have the focus on generating positives externalities for the whole productive structure; (ii) strategic highlights, consisting on public policy goals chosen due to their importance to the long-term productive development of Brazil; and (iii) structural programmes for productive systems, oriented towards strategic targets based on the diversity of the domestic productive structure.

16. The instruments of the PDP are divided in four categories, which expressively comprise antitrust regulation: (i) incentives (fiscal incentives, credit, venture capital, and economic subvention); (ii) state’s buying power (public procurement and state-owned companies’ procurement); (iii) technical support (certification, export/trade promotion, intellectual property, human resources and business capacity building); and (iv) regulation (technical, economic and antitrust).

17. The PDP is a horizontal policy, meaning that it is aimed at promoting incentives for the increase of economic competitiveness. An example worth mentioning of this horizontality is the inclusion in the macro targets of the PDP of incentives for the promotion of SMEs, which represent around 20% of the Brazilian GDP. This example also shows that industrial policy converges with competition policy, to the extent it provides conditions for the increase of competition and participation of SMEs in international markets and, consequently, within the internal market as well.

18. Competition principles are intrinsic to the whole industrial policy. Notwithstanding, the Brazilian Government can recognize some sectors such as the information technology, biofuels, infrastructure and capital goods sectors as essential for the systemic competitiveness, should they generate horizontal effects to the economy as a whole. Furthermore, even when there is such recognition, policies are designed on a horizontal way, so that no companies are privileged to the detriment of other companies of the same sector. Indeed, financial support lines and programs offered by the Brazilian Development Bank (BNDES) are available to all the companies of a respective sector.

19. Nowadays, both competition and industrial policies are mature and representative in the political agenda, which aims to enhance dynamic competitive advantages in markets increasingly integrated. However, the convergence of said policies is something new to the agenda.

3. **Convergence between industrial and competition policies**

20. Nowadays, post-merger control in Brazil is mandatory, and there are no exemptions in the Brazilian Competition Law or other sectorial laws. Thus, there is antitrust enforcement even when mergers occur in the regulated sectors.

21. Notwithstanding, article 54 of the Law 8.884 contains a special provision that permits mergers that satisfy attributes enumerated in its Paragraph 2 to be approved, provided that the transaction is “taken in the public interest or otherwise required to the benefit of the Brazilian economy” and that “no damages are caused to end-consumers or end-users”:

> "Article 54. Any acts that may limit or otherwise restrain open competition, or that result in the control of relevant markets for certain products or services, shall be submitted to CADE for review."

4 The role of the Central Bank while analyzing mergers in the financial sector is being discussed at the moment, according to what is going to be explained below.
Paragraph 1. CADE may authorize any acts referred to in the main section of this article, provided that they meet the following requirements:

I - they shall be cumulatively or alternatively intended to:

(a) increase productivity;

(b) improve the quality of a product or service; or

(c) cause an increased efficiency, as well as foster the technological or economic development;

II - the resulting benefits shall be ratably allocated among their participants, on the one part, and consumers or end-users, on the other;

III - they shall not drive competition out of a substantial portion of the relevant market for a product or service; and

IV - only the acts strictly required to attain an envisaged objective shall be performed for that purpose.

Paragraph 2. Any action under this article may be considered lawful if at least three of the requirements listed in the above items are met, whenever any such action is taken in the public interest or otherwise required to the benefit of the Brazilian economy, provided no damages are caused to end-consumers or end-users. (...)

22. To date, however, no decisions have ever been issued on grounds of this provision.

23. There are other discussions in regards to competences of the Brazilian Competition Policy System (BCPS)\(^5\) and other agencies in certain regulated sectors. The regulatory policies – especially those focused on infrastructure sectors, in which market failures occur – should be connected to a wider and more modern industrial policy. In this perspective, in which there is a regulatory agency responsible for the technical and economical regulation, cooperation strategies between CADE and said agencies have been implemented regarding conducts and merger control. These sectorial bodies can issue non-binding opinions concerning the impacts of competition processes to industry.

24. Relating to the financial sector matters, the Bill # 5.877/05 establishes, among other provisions, the role of the Central Bank while analysing mergers in the financial sector. According to said Bill, the Central Bank would be responsible for evaluating if the merger is justifiable in order to avoid systemic risks. In case of no systemic risk involved, CADE would be responsible for reviewing the merger according to the competition rules in force.

25. In the same tone, negotiations between CADE and BNDES are being undertaken aiming to strengthen the relationship between the two authorities. Among the objectives of the negotiations are the establishment of technical cooperation, the exchange of information, and the development of sectorial studies. Furthermore, CADE and Ministry of Development, Industry and Foreign Trade (MDIC) are also presently engaged in developing a cooperation agreement designed to facilitate sharing of industrial sector information between the two agencies.

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5 The Brazilian Competition Policy System (BCPS) is composed of three agencies -- namely, the Secretariat for Economic Monitoring of the Ministry of Finance (SEAE), the Secretariat of Economic Law of the Ministry of Justice (SDE), and the Administrative Council for Economic Defense (CADE).
26. Brazil's antitrust law provides that any transaction that may limit or otherwise restrain competition must be notified. As mentioned above, there are no exemptions to antitrust review under the Brazilian law. However, CADE could take into consideration if the transaction being analyzed is being supported by an industrial policy. In this case, the support by other governmental agencies to the transaction could be a strong indication for CADE’s review, as long as it is identified that the aims of the industrial policy that supports the merger are subsumed to one of the provisions of the article 54 above mentioned. This is a feasible convergence between industrial and competition policies, should both policies target the increase of productivity, the improvement of quality and the increase of efficiency as well as fostering economical and technological development.

27. Even though to date no decisions on merger reviews have ever been justified on the grounds of this convergence, the polemic discussion regarding national champions was brought to discussion in AmBev case.

28. In said case, (Merger Review nº 08012.005846/1999-12) two of the largest Brazilian beverage companies merged, creating American Beverage Co (AmBev), which turned to be the biggest beverage company in Latin America. Part of the case for the AmBev merger was that it would create a “national champion” capable of competing internationally, even though the debate was limited to private interests and there was not public effort or public policy involved.

29. The transaction was approved with the imposition of some remedies. However, CADE could not impose, as a restriction, the prohibition of selling the company to an international company, what happened four years after the transaction was approved, when the firm was taken over by Belgian beer giant Interbrew in the deal that created Inbev. CADE does not have the power to prohibit an international company to buy a Brazilian company if the deal is in accordance with the Brazilian rules.

30. More recently, two large telecommunication companies in Brazil announced their merger. Again, it has been alleged that the merge would create a national telecommunications champion. CADE, however, has not issued any opinion in said ongoing Merger Review yet.

4. Conclusions

31. The convergence between industrial policy and competition policy is feasible. Industrial policy should be designed in a pro-competitive way and the competition policy should amplify its competitive process, recognising that cooperative actions are mandatory to the power of antitrust policy.

32. The relationship between competition and industrial policies is recent. However, Brazil has nowadays mature institutions that have been working hard on said convergence, and the negotiations between CADE, the Brazilian Development Bank and the Ministry of Development, Industry and Foreign Trade are an indication of these efforts put towards the development of a qualitative transformation of the economy.

33. The Brazilian state continues to act as a regulator and therefore no types of companies are exempted of antitrust rules. Notwithstanding, the Brazilian Competition Policy System, when applying the antitrust policy can take into consideration the existence of public policies towards a certain industry.
CONTRIBUTION BY CANADA
THE ROLE OF COMPETITION POLICY IN THE CONTEXT
OF A NATIONAL INDUSTRIAL POLICY

--Canada--

1. This paper provides an overview of Canada’s competition and industrial policies as they could be said to relate to the debate on national champions. In particular, we consider the Canadian merger review analytical framework, and its interface with the public debate regarding domestic mergers. We also describe some of Canada’s current industrial policies with respect to investment in certain Canadian businesses. Specifically, we discuss the current rules governing ownership restrictions in the airline and telecommunication industries.

National Champions

2. As elsewhere, Canadians want to see their companies achieve success on the world stage and become global leaders. The term “national champion” can have many meanings. For some, it can mean globally renowned companies that are efficient and globally diversified and inspire national pride. To others, it means the creation of domestic monopolies at the expense of domestic consumers and businesses. Competition drives innovation, investment and, ultimately, the production of road-tested companies ready to compete in a rough and tumble world. This was management expert Michael Porter’s observation many years ago and it remains valid today: “creating a dominant domestic competitor rarely results in international competitive advantage. Companies that do not face significant competition at home are less likely to succeed internationally.”

3. Furthermore, as the Competition Bureau (the “Bureau”) has observed:

Domestic monopolies or near-monopolies, meanwhile, harm not only the Canadian economy, but also individual businesses and consumers in Canada, who may be forced to pay higher prices for the goods and services of companies not facing domestic competition.

The OECD’s Assessment of Certain Industrial Policies and Ownership Restrictions in Canada

4. As in most countries, there is, in Canada, legislation that restricts ownership or investment in certain industries. In some cases, legislation places direct restrictions on foreign ownership to ensure that such businesses do not fall under the control of non-Canadians. In other cases, the restrictions limit the degree to which any investor may hold more than a prescribed percentage of the business in question.

5. In 2006 and 2007, the OECD undertook both country-specific studies and country-comparative studies assessing the openness of various economies to foreign direct investment. Among the conclusions of these studies was an opinion that the economic consequences of Canada’s sector-specific policies

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1 See, for example, M. Porter, The Competitive Advantage of Nations (MacMillan Press, 1990) at 662.
restricting foreign investment have had significant negative implications for the productivity of the industry and the economic performance of the economy as a whole.

6. The OECD, in its studies, recognises the importance of FDI as a source for importing new technologies, management practices and sector specific know-how between countries. This, in turn, intensifies domestic competitive pressures by spurring domestic rivals to adopt best practices and state-of-the-art technologies. One conclusion of the OECD’s study is that Canada could have increased its annual productivity growth rate between 1995-2003 by three quarters of one percent annually had it amended its regulations that restrained competition to conform to the least restrictive regulations of other OECD countries. With respect to FDI restrictions, according to the OECD, reducing them to the level that is the least restrictive of competition (of all jurisdictions studied) would increase employment and provide a strong impulse to labour productivity growth.

Canada’s Study of Competition and Foreign Direct Investment Policies

7. In response to the challenges Canada faces with respect to improving its overall competitive performance, in June, 2007 the federal government appointed a task force of leading business experts, the Competition Policy Review Panel, with the mandate to review Canada's competition policies and its framework for foreign investment policy and to make recommendations to the Government of Canada for making Canada more competitive in an increasingly global marketplace. As part of its work, the Panel considered whether Canada’s policies regarding merger review act as an impediment to the emergence of so-called Canadian national champions. As part of its public consultation process, third parties were invited to make submissions regarding this and a number of other issues affecting Canada’s competitive performance internationally.

8. In their submissions, some parties raised specific concerns regarding the manner in which Canada applies the merger provisions in the case of domestic mergers, taking the view that the Bureau is impeding the growth of Canadian companies.

9. In its final report, the Panel fully endorsed the benefits of competition and competitive markets and rejected government policies that legislate or otherwise protect Canadian control:

While we have many global success stories, Canada has also witnessed the loss of some of our most iconic firms. Our Panel was formed at a time when the debate over the hollowing out of Canada was at its peak. Indeed, we ourselves share the feelings of disappointment and loss when a notable Canadian firm is acquired by a foreign company.

In our consultation paper, we asked Canadians whether domestic control and ownership was important to Canada’s economic prospects and our ability to create opportunity for Canadians.

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Ibid, OECD’s FDI Regulatory Restrictiveness Index: Revision and Extension to More Economies, p. 147
Ibid, OECD’s FDI Regulatory Restrictiveness Index: Revision and Extension to More Economies p. 150
See, for example, From Common Sense to Bold Ambition, Moving Canada Forward on the Global Stage, Canadian Council of Chief Executives, Submission to the Competition Policy Review Panel, January 2008, p. 17. “Even as the process of consolidation has accelerated globally, the application of Canadian competition policy has appeared to reflect a bias against domestic mergers and acquisitions. The inevitable result has been a series of foreign takeovers.”
For our part, we believe that competitive, Canadian-based firms are important. We are steadfast in our belief that Canadian ownership of our firms is valuable. But we do not believe that the best way to ensure Canadian control is by legislating it or imposing other protections.

We believe that the best way to ensure we create and sustain new Canadian champions is by ensuring that our policies, laws and regulations are the right ones to facilitate growth. Given the right conditions, the dynamism, talent and ambition of Canadians will rise to the fore. We will have more Canadian firms competing globally. And winning globally.8

With regards to the Competition Act specifically, the Panel observed that it “is recognised internationally as both modern and flexible and, in the Panel’s view, it does not constitute an impediment to Canada’s overall competitiveness.”9 Addressing the specific issue of merger review, the Panel noted:

Merger review is a key activity conducted by the Competition Bureau that has a substantial impact on the competitiveness and scale of Canadian industry. Most transactions are reviewed on a timely basis as posing no competition concerns and very few transactions require merger remedies. Overall, the Panel is satisfied that substantive merger provisions are generally modern, compatible with the laws of our major trading partners and appropriate for the Canadian economy.10

Included in the Panel’s recommendations were a number directed towards improving certain outmoded or ineffective provisions of the Competition Act. In the Fall of 2008, the Government of Canada announced its intention to proceed with legislation to modernise Canada’s competition and investment laws and implement many of the recommendations of the Competition Policy Review Panel. In legislation tabled in the House of Commons on February 6, 2009, the Government introduced a package of amendments to both the Competition Act and the Investment Canada Act.11

The Interface between Competition Policy and National Industrial Policy

As noted above, during the Panel’s review, much of the debate about the ability of Canadian companies to emerge and succeed internationally centred on alleged deficiencies in Canada’s merger review regime. Of course, the Canadian Competition Act does not impede the emergence of national champions through superior competitive performance. With respect to merger transactions in Canada, the Bureau has a statutory obligation to review proposed merger transactions to ensure that the merger does not result in a substantial lessening or prevention of competition.

Like the antitrust merger review regimes of its major trading partners, Canada’s regime does not take the nationality of the merging parties into account. Rather, it examines whether Canadian consumers and businesses will continue to benefit from a competitive market if the merger is completed. This includes asking such questions as “Where can Canadian consumers or businesses turn in order to buy competing products?” and “Will Canadian consumers and businesses continue to benefit from a

8 Id Supranote 6, Compete to Win, p. 104.
9 Id Supranote 6, p. 53
10 Id Supranote 6, pp. 55-56
competitive market following the merger?” This is in contrast to the view that the merging companies often bring to the table, which naturally focuses on their immediate business interests; namely, how the merger will help the company develop and expand the markets for their products. That can include the enhancement of an ability to exercise market power - what the Bureau must ensure is not substantial.

14. As a result of the approach required by statute, a more thorough review will typically be necessary whenever a merger involves two parties, either foreign or domestic, that supply the same Canadian market(s), particularly if the market(s) are highly concentrated and difficult for new competitors to enter. The reality is that, because financial investors or foreign competitors entering Canadian markets may raise no competition issues (owing to the fact they do not participate in the target’s market(s) pre-merger), they can often benefit from an expedited review. The same is true for Canadian firms competing for an acquisition with foreign firms who may be more concentrated in the particular local markets affected. Finally, where the markets are continental or worldwide, rarely do any proposed mergers between even two very significant Canadian players raise concerns.

15. In the submissions to the Panel, there were two principal criticisms regarding the Bureau’s merger review process with respect to the issue of the emergence of national champions. The first was that geographic markets are defined too narrowly, given the global nature of the marketplace. The second was that the Bureau does not understand the need of merging parties to achieve the size necessary to compete internationally. In response, it is important to understand the Bureau’s role as set out in the Competition Act; namely, to ensure that Canadian businesses and consumers are able to benefit from a competitive marketplace, whether they buy from local, national or international companies.

i) The Relevant Geographic Markets Criticism:

Turning to the first criticism; namely that the Bureau puts some parties (particularly domestically-based merging parties) at a disadvantage because of its approach to defining geographic markets.

In this regard, the Bureau is diligent in approaching the issue of geographic market definition from a disciplined analytical perspective. To suggest the Bureau is insensitive to the fact many markets are broader than Canada ignores the facts. There are many examples where a merger has been cleared based on a geographic market that is broader than Canada, including mergers in the mining, steel, upstream oil and gas, and certain chemical industries. For example, in its review of Mittal Steel’s acquisition of Arcelor SA, the Bureau concluded that the market is larger than Canada – in that case, North American in scope. It is a question of evidence from the market in the specific case as to where, from an antitrust perspective, the contours of the geographic market should be drawn.

Similarly, as part of its assessment, Canada always accounts for the role of foreign competitors. For example, in the Bureau’s analysis of the Maytag/Whirlpool merger, foreign competition was an important and offsetting factor that would limit the ability of manufacturers to increase prices for Canadian consumers in an anticompetitive way. What the critics ignore is that, while a merger may involve firms that operate globally, it may raise concerns in local markets within Canada. For example, local upstream markets may raise issues notwithstanding the downstream market may be continental or even worldwide. A recent example where markets were local – in the sense of provincial - was the acquisition of ICI by Akzo Nobel. In that case, both the merging firms supplied paint and other products in various jurisdictions worldwide. However, owing to, among other things, strong local preferences and barriers resulting from loyalty programs, the Bureau was concerned that the merger would substantially lessen competition in Quebec, where the parties were two of the leading suppliers of paint. The remedy was confined to preserving
competition in Quebec by requiring the merging parties to divest of certain brands sold in Quebec.

ii) Scale Necessary to Compete – The Efficiency Criticism:

With respect to the second criticism, that the Bureau does not understand the need for parties to achieve the scale necessary to compete in the global marketplace, there are two principal responses. First, preferring local Canadian companies by allowing them to consolidate irrespective of the effect on Canadian consumers is contrary to the Bureau’s mandate; in any event, the evidence is clear that companies not forced to compete at home do not thrive in global markets. Second, the Canadian Competition Act has an explicit statutory exception for transactions that are likely to generate gains in efficiency. In 1986, Parliament enacted an efficiency exception in section 96 of the Act. Pursuant to this exception, a merger that would likely result in a substantial prevention or lessening of competition will be allowed if the merger is likely to bring about gains in efficiency that will be greater than and offset the anti-competitive effects. As such, Canada’s merger provisions account for the positive effects of efficiencies arising out of such mergers. In this regard, Canada currently has one of the most receptive regimes internationally for the consideration of efficiency claims in merger review. Consequently, even in the small number of cases where it is found that the merger will lessen competition substantially, it is always open to the parties to argue that an anti-competitive transaction should be cleared in light of the efficiencies it will bring to the Canadian economy.

It is worth noting in this regard that the number of mergers that the Bureau challenges is very small. Moreover, the reasons the Bureau does not challenge the vast majority of mergers is owing to factors other than the efficiencies exception. Specifically, the Bureau concludes, following a rigorous and economic analysis, that no substantial lessening or prevention of competition is likely to result from the merger. This can be owing to, among other considerations, the fact that sufficient competition will remain in affected markets following the merger, or that low barriers to entry allow for sufficient potential competition, either of which will prevent the exercise of market power. Accordingly, while there is an explicit statutory efficiencies provision, to date few firms have needed to take advantage of this provision.

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12 The test used by the Bureau is whether a substantial lessening or prevention of competition will result from the merger. This refers to the ability of the merged parties to exercise market power, which is generally viewed as the ability to profitably raise price or otherwise restrict competition without fear of competitive reaction. The test extends beyond pricing and can include such non-monetary aspects of competition as restricting output, quality, variety, service, advertising, innovation and other dimensions of competition.

13 In general, the categories of efficiencies that will be considered include technical (productive) efficiency (the creation of a given volume of output at the lowest possible resource cost); and dynamic efficiency (the optimal introduction of new products and production processes over time).

14 The Superior Propane case in 2003 (Canada (The Commissioner of Competition) v. Superior Propane Inc., [2003] 3 F.C. 529 (C.A.), aff’d (2002), 18 C.P.R. (4th) 417 (Comp. Trib.) (redetermination decision following [2001] 3 F.C. 185 (C.A.), rev’d (2000), 7 C.P.R. (4th) 385 (Comp. Trib.))) is the only case in which the Competition Tribunal and the courts have applied the efficiencies exception in the Competition Act. The efficiencies exception was first invoked in Canada (Director of Investigation and Research) v. Hillsdown Holdings (Canada) Ltd. (1992). In this case, the exception was moot, since the Competition Tribunal found that the merger did not substantially lessen or prevent competition. The exception has also been mentioned (but not applied) in four other Tribunal cases, namely: Canada (Director of Investigation and Research) v. Air Canada (1988)(the Tribunal observed that section 96 had to be interpreted in light of section 1.1); Canada (Director of Investigation and Research) v. Imperial Oil Limited (1989) (the Tribunal commented on the quantum of claimed efficiency gains); Director of Investigation and Research v.
16. In its submission to the Competition Policy Review Panel, the Bureau recommended that Canada’s position regarding the interface between merger review and the evolution of national champions be as follows:

- The efficiencies exception in the Competition Act provides a mechanism through which firms can grow to an efficient scale, even at the expense of competition in Canada. This approach requires that firms that are proposing an otherwise harmful merger bring forward credible and convincing evidence of the anticipated efficiency gains, rather than relying solely on arguments.

- Although the existing Canadian approach to balancing efficiencies against anti-competitive harm may be complex in some cases, it is based on principled and objective criteria that allow firms to grow to scale by achieving the efficiencies necessary to compete at home and abroad. It is applied through an independent, transparent legal process before the Competition Tribunal.

- In contrast, the introduction of a broad-based public interest test as part of any merger review process risks the possibility that decisions will not be made with proper regard to evidence or sound economic principles. The complexity inherent in public interest analysis can run the risk of greater delay and could even prevent potentially pro-competitive transactions. Moreover, where benefits are concentrated and costs are diffuse, it is possible for narrow groups that stand to benefit from public interest reviews to enrich themselves at the expense of others.

- The challenge for any government is to adopt policies that will enhance the economic benefits flowing from an open economy and the benefits of deregulation, while resisting the call from some to retreat to protectionism for certain industries at the expense of other domestic businesses and individual consumers. Adopting policies that favour protectionism increase the opportunity and ability of firms in protected industries to exercise market power by raising or maintaining prices above competitive levels. The implication of such policies is to sacrifice the global competitiveness of any other domestic industry that rely upon the products or services produced by the so-called national champion.

- Where public interest merger reviews are deemed necessary, they should be based on clearly identified public interest criteria, conducted by an independent body in a transparent manner, based on fact and evidence (as opposed to argument and private interest). Furthermore, the weighing of this evidence should be based on a standard that requires public benefits to clearly outweigh any potential harm to competition that may result from the proposed transaction.

**Specific Sectoral Restrictions in Canada**

17. The Bureau frequently considers the issue of investment restrictions in various sectors of Canada’s economy, either as a feature of its enforcement activities under the Act or in its role as an advocate of competition policy before various legislative and regulatory bodies.

18. When undertaking any competitive effects analysis under the Act, among the factors the Bureau considers is the presence of barriers to entry into a market for prospective competitors. Barriers can take

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many forms, ranging from regulatory restrictions, including sectoral restrictions, to sunk costs that cannot be recovered. As was noted in the Competition Policy Review Panel’s final report, sectoral investment regimes and ownership restrictions constitute barriers to entry to many markets in Canada.\footnote{See, for example, the Panel’s comments noted above, supranote 8.}

**Airlines**

19. The Canada Transportation Act\footnote{S.C. 1996, c. 10} provides that each Canadian airline must be at least 75% owned or otherwise controlled by Canadians, and that only a Canadian may obtain a licence to operate. "Canadian" is defined as:

   a Canadian citizen or a permanent resident within the meaning of subsection 2(1) of the Immigration and Refugee Protection Act, a government in Canada or an agent of such a government or a corporation or other entity that is incorporated or formed under the laws of Canada or a province, that is controlled in fact by Canadians and of which at least seventy-five per cent, or such lesser percentage as the Governor in Council may by regulation specify, of the voting interests are owned and controlled by Canadians.\footnote{Id., s. 55(1).}

20. In addition, the Air Canada Public Participation Act\footnote{R.S.C. 1985, c. C-35 (4th Supp.).} requires that Air Canada’s articles of continuance:

   contain provisions imposing constraints on the issue, transfer and ownership, including joint ownership, of voting shares of the Corporation to prevent non-residents from holding, beneficially owning or controlling, directly or indirectly, otherwise than by way of security only, in the aggregate voting shares to which are attached more than 25%, or any higher percentage that the Governor in Council may by regulation specify, of the votes that may ordinarily be cast to elect directors of the Corporation, other than votes that may be so cast by or on behalf of the Minister.\footnote{Idem, s. 6(1)(b).}

21. In Canada, the presence of foreign ownership restrictions was a significant factor in the restructuring of the Canadian airline industry in 1999. As a result of these restrictions, Air Canada emerged as the only viable acquirer of Canadian Airlines and became the largest domestic carrier in the immediate period following the merger, although it subsequently sought bankruptcy protection to restructure its operations. Nonetheless, the restrictions have not prevented the emergence of WestJet as a second national carrier.

22. As the Bureau noted in its submission to the Competition Policy Review Panel, it supports a number of measures that would result in the reduction or elimination of foreign ownership restrictions on Canadian air carriers\footnote{Submission to the Competition Policy Review Panel by the Commissioner of Competition, January 11, 2008, p.13. http://www.ic.gc.ca/eic/site/cprp-gepmc.nsf/vwapj/commissioner_competition_bureau.pdf/$FILE/commissioner_competition_bureau.pdf}. There does not appear to be any compelling economic reason why the air transportation sector should continue to have such restrictions. The Bureau recognises that the elimination of all ownership restrictions may not be feasible under current bilateral air agreements that require

\footnote{\textsuperscript{15} See, for example, the Panel’s comments noted above, supranote 8.\textsuperscript{16} S.C. 1996, c. 10\textsuperscript{17} Id., s. 55(1).\textsuperscript{18} R.S.C. 1985, c. C-35 (4th Supp.).\textsuperscript{19} Idem, s. 6(1)(b).\textsuperscript{20} Submission to the Competition Policy Review Panel by the Commissioner of Competition, January 11, 2008, p.13. http://www.ic.gc.ca/eic/site/cprp-gepmc.nsf/vwapj/commissioner_competition_bureau.pdf/$FILE/commissioner_competition_bureau.pdf}
domestic air carriers to be substantially owned and controlled by their government or home country nationals. Accordingly, as a first step, the Bureau supports increasing the limit on foreign ownership of voting shares in Canadian air carriers from the current 25 percent to 49.9 percent. The airline industry is capital-intensive. New entrants, as well as established players, would benefit from the greater access to foreign capital through liberalised ownership rules.

23. In respect of domestic routes, the Bureau has also voiced its support for permitting the entry of wholly foreign owned carriers that only serve routes within Canada. Such an approach has been successfully adopted in Australia. Pursuant to such a policy, foreign carriers could draw upon their knowledge and expertise to establish new operations in Canada. Such “Canada-only carriers” could also generate greater feed traffic beyond the major international gateways thereby allowing international carriers to serve a greater number of routes to and from Canada.

24. The Bureau also supports cabotage. Cabotage refers to the right of a foreign carrier to operate within the domestic borders of another country. Canada, like most countries, does not permit cabotage. This prohibits, for example, a carrier such as Air France serving the Paris-Toronto route, from picking up additional passengers in Toronto and continuing a flight service to Vancouver. Permitting foreign air carriers to provide services between points in Canada has the potential to further promote competition on routes within Canada.

25. As part of its review, the Competition Policy Review Panel commented on the issues surrounding ownership restrictions in the airline industry and recommended that the Minister of Transport increase the limit on foreign ownership to 49% of voting equity, on a reciprocal basis, through bilateral negotiations with other countries. The Panel also recommended that the Minister indicate whether he would be willing to accept foreign-owned Canadian-incorporated domestic air carriers by December, 2009. The Panel urged the Minister to complete an Open Skies agreement with the European Union as soon as possible. In that regard, Canada recently concluded negotiations with the European Union (EU) on a comprehensive air transport agreement that will open access to all 27 Member States for Canadian carriers and all points in Canada for EU carriers. We anticipate that consumers and air dependant industries will benefit from the additional flexibility provided by this new agreement.

**Telecommunications**

26. Canada continues to have foreign ownership restrictions on domestic telecommunications undertakings. In that sector, non-Canadians cannot directly own more than 20% of a Canadian telecommunications carrier and not more than 33.3% of a holding company that owns a Canadian carrier. As a result, the combined limit on foreign direct and indirect investment in a Canadian telecommunications carrier is capped at 46.7%. The Telecommunications Act provides that only a Canadian carrier that is a Canadian-owned and controlled corporation incorporated or continued under the laws of Canada or a province may own or operate a transmission facility to provide telecommunications services to the public. A corporation is Canadian-owned and controlled if: (i) not less than 80% of the members of its board of directors are individual Canadians; (ii) Canadians beneficially own, directly or indirectly, in the aggregate and otherwise than by way of security, not less than 80% of the corporation’s issued and outstanding voting shares; and (iii) the corporation is not otherwise controlled by persons that are not

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21 Id Supranote 6, Recommendations 7, 8 & 9, p. 42
23 Id., s. 16(1).
Canadians. A Canadian is defined in the Canadian Telecommunications Common Carrier Ownership and Control Regulations as follows:

- a Canadian citizen or permanent resident;
- a corporation without share capital where a majority of its directors or officers are appointed or designated by a federal or provincial government;
- a corporation in which Canadians beneficially own and control, in the aggregate and otherwise than by way of security, not less than two-thirds of the issued and outstanding voting shares, and which is not otherwise controlled by non-Canadians;
- a trust in which Canadians have not less than two-thirds of the beneficial interest and of which a majority of the trustees are Canadian; and
- a partnership in which Canadian partners beneficially own and control not less than two third of the beneficial interest and which is not otherwise controlled by non-Canadians.

In 2006, an expert panel struck by the government to study Canada’s telecommunications policies and regulatory framework, the Telecommunications Policy Review Panel (the TPRP), recommended that restrictions on foreign investment in telecommunications service providers be liberalised. This position was supported by many of the parties that participated in the TPRP’s review. Similarly, the OECD has urged Canada to eliminate foreign ownership restrictions in telecommunications and has argued the negative effects of foreign investment restrictions on the cost of capital and on competition more generally.

In the Bureau’s view, foreign ownership restrictions on facilities-based telecommunications carriers are no longer necessary to harmonise Canadian policy with that of our global trading partners. By limiting potential entry in the telecommunications markets, Canada’s foreign investment restrictions reduce the competitive discipline that the threat of entry can provide. Moreover, these restrictions slow the realisation of the benefits to open competition for consumers and business supplied by these markets. Telecom is a key enabler in many other sectors of the economy and, as such, its impact on innovation and competitiveness is seen nationwide.

With respect to companies that previously only distributed broadcast signals but can now take advantage of technical advances to enter into competition with facilities-based telecommunications carriers, it is the Bureau’s view that the foreign investment levels for these corporations should be consistent with those applicable to the telecommunications carriers. Regardless of technology, all carriers should enjoy the same access to capital and be bound by the same ownership rules. This approach will

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24 Id., s. 16(3).
25 SOR/94-667.
26 Id., s. 2.
28 Id. supranote 6, p. 8.
ensure that broadcasting distribution undertakings are not placed at an unfair competitive disadvantage vis-à-vis telecommunications companies, given that both compete in high-speed access and telephony.

30. The Competition Policy Review Panel adopted the earlier recommendation from the TPRP noted above, namely, that the federal government should adopt a two-phased approach to foreign participation in the telecommunications and broadcast industry. In the first phase, according to the Panel recommendation, the Minister of Industry should amend the Telecommunications Act to allow foreign companies to establish a new telecommunications business in Canada or to acquire an existing telecommunications company with a market share of up to 10 percent of the telecommunications market in Canada. In the second phase, following a review of broadcasting and cultural policies including foreign investment, telecommunications and broadcasting foreign investment restrictions should be liberalised in a manner that is competitively neutral for telecommunications and broadcasting companies.29

Conclusion

31. Champion companies should emerge as the result of their superior competitive performance and market forces. There are significant risks of picking and promoting particular firms by exempting firms or industries from general competition laws or allowing firms to merge based on “public interest” criteria other than competitive effects and economic efficiency. Moreover, protecting domestic firms from foreign competition or other preferential treatment is harmful to the productivity of the domestic economy and the competitiveness of Canadian industries that, in many cases, depend on these firms for essential inputs into their businesses. In that regard, the Government of Canada has stated that “[i]n Canada, we must ensure that we have strong and effective regulations to protect people and enhance our quality of life, while minimising regulations that are unnecessary or that put Canada at a significant competitive disadvantage.”30

29 Id. supranote 6, Recommendation 11 at p. 49.

CONTRIBUTION BY CHINA
THE REGULATION ON RESTRICTIVE COMPETITIVE BEHAVIOUR
BY PUBLIC ENTERPRISES

--China--

By: Song Yue

Intensifying supervision of public enterprises and guiding them to act in a law-abiding way is an important task for competition authorities of every country. Plenty of public enterprises such as water supply, electricity supply, gas supply, heat supply, postal service, telecoms, railways, civil aviation, urban transportation and cabled TV have direct bearing on people’s life. These industries, most of which are regulatory ones and possess natural monopoly features, lack sufficient competition, thus easily resulting in high-price, low-quality products and services. These situations have caused dissatisfaction among consumers, gradually becoming a hot issue.

Chinese government attaches great importance on the supervision of public enterprises, encouraging them to compete efficiently. Recently we have made some progress in the reform of the monopoly industries by separating government functions and enterprises management, introducing competition into the industry, improving government’s supervision and promoting enterprise restructuring, etc. For instance, in the past ten years we have been working hard on the reform in the telecommunication industry. Through the separation of enterprise management from the government, the whole industry restructured several times and we currently have three telecommunication companies. Each of them can carry out the local fixed-line phone business in each other’s regions as well as provide mutual preferential service to each other, such as equal access. The competition is being shaped step by step, thus problems such as high price, low quality service have been solved to some extent. Besides, a lot of private investment is coming into industries like civil aviation and oil supply and consumers have more options other than public enterprises.

Meanwhile, through legislation Chinese government have been intensifying the supervision in this area. The Anti-Unfair Competition Law of 1993 has included specific regulations prohibiting restrictive competitive behaviours of public enterprises and other operators possessing an exclusive position in accordance with the Law. According to Article 6 of the Law, the public enterprises and other operators with an exclusive position in accordance with Law shall not force others to buy the goods of operators designated by them so as to exclude other operators from competing fairly. Besides, laws like “Price Law of China”, “Telecommunications Regulations of China” have set strict regulations on restrictive competitive behaviour of public enterprises.

SAIC is the competent authority directly under the State Council, taking charge of market supervision and enforcing “Anti-Unfair Competition Law”, supervising restrictive behaviour. According to statistics, Administrations for Industry and Commerce (AIC), from 1999 to the first half of 2008, almost 7000 cases of restrictive behaviour of public enterprises have been dealt with, covering a dozen industries such as water supply, electricity supply, insurance, telecoms, commercial banks, tobacco, oil, salt supply etc. Their restrictive behaviours include coercive transactions, coercive service supply, differentiated treatments, tie-in with unreasonable trading conditions, and abuse of the dominant position to collect unjustified fees.

In guiding public enterprises to follow fair competition principle, we work closely with industry institutions and give respective due role to full play to strengthen effective supervision in regulatory industries. We coordinate with the postal service, telecoms, railways and civil aviation industry

1 Antimonopoly and Anti-Unfair Competition Enforcement Bureau, SAIC, China
institutions, particularly intensifying communication on the drafting of competition policy and industrial policy, and discuss how to prevent unfair competitive behaviour and restrictive behaviour in these special industries. We are working shoulder to shoulder and perform duties within respective jurisdictions in regulating and supervising public enterprises’ behaviour to guarantee the legitimate rights and interests of consumers. It has been proved by practice that to supervise public enterprises, the coordination and cooperation between competition authorities and industrial institutions is of utter importance.

Since 1 August 2008, Chinese Antimonopoly Law (AML) has taken effect. SAIC is one of the main competition enforcement authorities, in accordance with law and the entrustment of the State Council. We take charge of Monopoly Agreement, Abuse of a Dominant Market Position, Abuse of Administrative Power to Eliminate or Restrict Competition (price monopoly behaviour excluded). Article 7 of the Law has clearly stated that business of monopolised industry shall act in a law-abiding, honest, credit-worthy and self-disciplined way, and shall subject themselves to public scrutiny. The public enterprises shall not abuse their dominant or exclusive position to harm consumers’ interests. SAIC, as the main AML enforcement authority, will further supervise public enterprises in accordance with the Law, enhance consumers’ welfare and construct a highly-efficient and orderly competition pattern.
CONTRIBUTION BY EUROPEAN COMMISSION
INDUSTRIAL POLICY, COMPETITION POLICY AND NATIONAL CHAMPIONS

-- European Commission --

1. The Commission’s general stance on industrial policy and "national champions"

1. It should be emphasised at the outset that in the view of the European Commission, industrial policy and competition policy are not in conflict with each other. Rather, particularly as a strong industry depends on an open market with free competition, competition policy should form part of industrial policy. Accordingly, this rather anachronistic term should more suitably be substituted by "competitiveness policy" as the overall notion. This view has been frequently stated by the Commission, notably in its 2004 Communication "A pro-active Competition Policy for a Competitive Europe".

2. The term "national champions" is often used to refer to domestic companies that are strong players in international markets and that are in various ways supported by their governments. They often contribute to national pride and their success is seen as a benchmark of the state of the national economy.

3. It has to be underlined that the Commission is not against "national champions" per se, as long as their status is achieved in accordance with EC law on competition, mergers and State aid. National champions resulting from the play of competition in an open and competitive market do not raise issues.

4. However, it should also be noted that the Commission does not see a special need to foster "national champions". Every nation can be a winner in the single market, with which the concept of merely "national" champions is somewhat in tension. In contrast, a recent call for the creation of "European Champions" is more in keeping with the spirit of the internal market. But even regarding "European Champions", the Commission does not see any need to foster them in an interventionist way. Moreover, the concept of any kind of "champion" cannot be invoked, explicitly or implicitly, as a justification for setting aside the rules on anti-trust, mergers and State aid.

5. The Commission holds that a competitive market, guaranteed by EC law, is the best instrument to bolster the economy and industry in Europe. It is the central driver for economic growth, and only firms that can stand competition at home (and in Europe) can compete with the entire world. Thus, vigorous

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1 P.A. Geroski, Competition Policy and National Champions, p. 6 et seq.
2 N. Kroes, Industrial Policy and Competition Law & Policy, Speech/06/499, p. 2; N. Kroes, Competitiveness, Speech/08/207, p. 2; also Lars Sorgard, The Economics of National Champions, p. 63.
3 See N. Kroes, Industrial Policy and Competition Law & Policy, Speech/06/499, p. 4 et seq.
5 See J. Hayward in J.E. Shalom (ed.), Industrial Enterprise and European Integration, p. 10 et seq. on the different notions and M. Motta, Competition Policy, p. 10 et seq. on the history.
7 N. Kroes, Competitiveness, Speech/08/207, p. 2.
8 D. Strauss-Kahn, Round Table: Sustainable Project for Europe: Final Report of the Group of Policy Advisors, 2004; the creation of European Champions has also been an argument of the French Government in the past, see J. Hayward in J.E. Shalom (ed.), Industrial Enterprise and European Integration, p. 7.
9 N. Kroes, Building a Competitive Europe, Speech/05/78, p. 4.
competition based on a pro-active competition policy, that intends to improve the regulatory framework for competition as well as the efficiency of enforcement practices, is the best industrial policy. EC law does not form an obstacle to creating firms with sufficient dimension to compete in the global marketplace, as long as competition is guaranteed.

6. However, competition is not an end in itself but a means to an end, and in that respect it is connected to the Lisbon Agenda (a ten-year strategy for improving the competitiveness of the EU economy, launched in Lisbon in 2000). Economic growth should be based on innovation, lead to new knowledge-based jobs, guarantee sustainability, protect the environment and thereby contribute to social welfare and ensure long-term prosperity in Europe. One should bear in mind that also the Lisbon Agenda is a European Agenda, exceeding national borders.

2. Exemptions from competition law for National Champions?

2.1 The "critical mass" or "scale economy"-argument

7. One common argument invoked in favour of national champions is the "critical mass" or "scale economy"-argument, stating that EC competition law as it is applied by the Commission may prevent companies from reaching the "critical mass" necessary to persist in markets that require undertaking with a special scale to be competitive. Especially, to compete in the global market might require a critical mass, according to the supporters of that view.

8. This argument is not convincing: Firstly, if the business idea is actually sustainable and persuasive, investors with rational expectations and interest in future compensation will be found so that the necessary size will be reached even without government support and State aid. Secondly, the merger rules do not preclude companies from growing to a "critical mass", whether organically or by merger and acquisition, as long as this does not lead to a distortion of competition to the disadvantage of consumers, or to a denial of market access. Thus, the Commission acknowledges that a minimal scale might be desirable, especially in high-tech sectors, but this does not remove the rationale for ensuring competition even in those sectors. Thirdly, defining the relevant market in merger cases with respect to their scale (meaning de facto a more lenient approach in the case of smaller local or national markets) would lead to an unacceptable discrimination against consumers in smaller economies.

2.2 "Market failure" and "learning effects"-argument

9. There might be situations in which under the given technology a profitable production is not possible for private producers. This leads to a market failure that a government can address in order to produce a total welfare benefit that exceeds the government's cost. Comparable problems might arise concerning the development of new technology and inventions in general. In some areas (e.g. the aviation sector) the costs and risks are so high and incalculable that private investors may be unwilling to incur them irrespective of the opportunities. Further, one might conceivably envisage government support for national firms during their "learning phase" until they know how to be profitable in highly innovative sectors. But even in those cases, no support should be granted if funds could be achieved from the free

10 See COM (2004) 293 final in this respect.
11 N. Kroes, Building a Competitive Europe, Speech/05/78, p. 4.
12 N. Kroes, Competitiveness, Speech/08/207, p. 4 et seq.
13 N. Kroes, Building a Competitive Europe, Speech/05/78, p. 3; N. Kroes, Industrial Policy and Competition Law & Policy, Speech/06/499, p. 7.
market because of expectations of profit in the long-term. In any case, there is a fundamental distinction between a government address market failures and fostering the creation of national champions.

10. EC law provides for mechanisms to address market failures via state aids, e.g. the Community Framework for State aid for Research and Development and Innovation (2006 OJ C 323/1)\(^{15}\); the Community guidelines on state aid to promote risk capital investments in small and medium-sized enterprises (2006 OJ C 194/2)\(^{16}\) or the Community guidelines on State aid for rescuing and restructuring firms in difficulty (2004 OJ C 244/2)\(^{17}\).

11. In short, one could say that the Commission accepts "intelligently-targeted support" to fill gaps left by genuine market failures if the support is granted to enhance active competition.\(^{18}\) The outcome of a national champion does not raise concerns under these circumstances; however, the aim of creation of a national champion does not serve as a justification in itself for state aid or other state intervention.

3. **Case-law regarding interventions by Member States**

12. In the context of "national champions", an EU member State could be incited to intervene in one of three ways which are pertinent for EU competition law:

   a) It may grant state aid in some form to the undertaking in question. In this case article 87 of the Treaty applies. Unless covered by a block exemption, the aid must be notified to the Commission and may not be paid as long as the Commission has not approved it. Any state aid illegally paid out must be reimbursed to the State in question by the beneficiary company.

   As an example of the Commission's determined enforcement practice one might refer to the case "Électricité de France (EdF)". The Commission did not accept the State guarantee that France accorded EdF for several years\(^ {19}\) and decided in 2003 that EdF had to reimburse more than €1,2

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\(^{15}\) See p. 20 under 7.3.1.: "Existence of a market failure: As indicated in Chapter 1, State aid may be necessary to increase R&D&I in the economy only to the extent that the market, on its own, fails to deliver an optimal outcome. It is established that certain market failures hamper the overall level of R&D&I in the Community. However, not all undertakings and sectors in the economy are confronted to these market failures to the same extent. Consequently, as regards measures subject to a detailed assessment, the Member State should provide adequate information whether the aid refers to a general market failure regarding R&D&I in the Community, or to a specific market failure."

\(^{16}\) See p. 5 concerning the balancing test asking inter alia: "(2) Is the aid well designed to deliver the objective of common interest, that is does the proposed aid address the market failure or other objective?".

\(^{17}\) See para. 19: "Article 87(2) and (3) of the Treaty provide for the possibility that aid falling within the scope of Article 87(1) will be regarded as compatible with the common market. Apart from cases of aid envisaged by Article 87(2), in particular aid to make good the damage caused by natural disasters or exceptional occurrences, which are not covered here, the only basis on which aid for firms in difficulty can be deemed compatible is Article 87(3)(c). Under that provision the Commission has the power to authorise «aid to facilitate the development of certain economic activities (...) where such aid does not adversely affect trading conditions to an extent contrary to the common interest.» In particular, this could be the case where the aid is necessary to correct disparities caused by market failures or to ensure economic and social cohesion."

\(^{18}\) N. Kroes, Building a Competitive Europe, Speech/05/78, p. 8.

\(^{19}\) See press release IP/03/477.
b) It may encourage or foster a merger between two domestic companies which has a Community dimension and therefore falls within the scope of the EU merger regulation. In this case the Commission, under the merger Regulation, assesses only the effect on competition, without taking into account other factors, and where the merger poses problems for competition, it can require remedies or prohibit the merger, regardless of whether it is supported by a Member State.

Accordingly, the Commission was unable to authorise a merger of Scania and Volvo irrespective of the support of the Swedish government for the merger. The merger of Gaz de France (GdF) and Suez, supported by the French government, could be approved only after various remedies had been accepted to avoid distortions of competition in France and Belgium.

c) It may oppose a takeover of a domestic company by a foreign company, where there is a Community dimension and the EU merger regulation is applicable. In this case, the only legal instrument permitting a member State to intervene is article 21.4 of the merger Regulation, which allows intervention on strictly limited grounds: public security, plurality of the media and prudential rules, and other public interests only if they are communicated to the Commission by the Member State concerned and shall be recognised by the Commission. Thus, the Real Decreto-Ley 4/2006 of 24th February 2006, an emergency law enacted by the Spanish government to prevent the takeover of national energy firm Endesa by the German firm E.ON., was annulled by the European Court of Justice, on application by the Commission, as being in violation of 21.4 of the merger Regulation. Already in 1999 in the Champalimaud case

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20 See inter alia press releases IP/02/1853, IP/05/1139, IP/06/425, IP/06/531, IP/06/1424.
21 COMP/M.1672 Volvo/Scania and the accompanying press release IP/00/257.
22 See press release IP/06/1558.
23 Full text of article 21.4 of the merger Regulation:

Notwithstanding paragraphs 2 and 3, Member States may take appropriate measures to protect legitimate interests other than those taken into consideration by this Regulation and compatible with the general principles and other provisions of Community law.

Public security, plurality of the media and prudential rules shall be regarded as legitimate interests within the meaning of the first subparagraph.

Notwithstanding paragraphs 2 and 3, Member States may take appropriate measures to protect legitimate interests other than those taken into consideration by this Regulation and compatible with the general principles and other provisions of Community law.

Public security, plurality of the media and prudential rules shall be regarded as legitimate interests within the meaning of the first subparagraph.

Any other public interest must be communicated to the Commission by the Member State concerned and shall be recognised by the Commission after an assessment of its compatibility with the general principles and other provisions of Community law before the measures referred to above may be taken. The Commission shall inform the Member State concerned of its decision within 25 working days of that communication.

the Commission had rejected the attempt of Portugal to block a bid of Banco Santander Central Hispano (BSCH) for the Champalimaud financial group as incompatible with article 21 of the merger Regulation.25

13. These examples may suffice to prove that national champions do not enjoy a privileged or special status and that the Commission is determined to enforce the competition rules for all undertakings in the EU.

4. Conclusions

- The Commission holds that industrial policy and competition policy are not in contrast to each other but that industriapolicy has to comprise competition policy and therefore should be called competitiveness policy.

- The Commission believes in open markets and free competition as the best means to brace Europe's economy for the global market and to maintain and enhance social welfare in Europe. There is no need for national champions as all Member States and their economies are winners of the single market.

- However, there is no per se objection to national champions as long as their status is achieved in compliance with EC law and as a result of an open and competitive market.

- The idea of national champions itself can in no case justify the incompliance with EC-law or suffice for an exemption from it.

- Exemptions might lead to national champions but the wish for national champions does not suffice for an exemption.

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25 See press releases IP/99/774 and IP/00/296. However, the Court of Justice did not rule on that case, as the Portuguese state withdrew the measures in question.
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THE RELATIONSHIP BETWEEN COMPETITION POLICY, INDUSTRIAL POLICY
AND NATIONAL CHAMPIONS

--France1--

1. Until about the early 1990s, industrial policy could still be defined as an instrument of economic policy wielded by government with the aim of promoting certain sectors of activity for reasons of national independence, technological autonomy or regional balance. De facto, for over 15 years now the French government's main priority on the industrial front has been to encourage innovation rather than any particular sector, even if that has meant promoting the most promising generic technologies, especially the knowledge-based society and ICT, health and biotechnology, materials and nanotechnologies.

2. Likewise, industrial policy can no longer be simply defined as all vertical policies as opposed to cross-cutting policies, such as competition policy. Innovation policies are broadly cross-cutting, as are policies relating to intellectual property, business-oriented higher education, entrepreneurship, the small business environment, design, the adaptation of the productive system to geopolitical changes in world demand, sustainable development and the green industries needed to reduce greenhouses gases, business tax breaks, etc.

3. Vertical policies are not therefore structural policies designed to influence industrial rationalisation and concentration and concerned merely to coordinate the different players within the same sector, as in the 1970s. To give an example, industries as "traditional" as steelmaking advance not by "coordinating the different players within the same sector" but through a combination of the gradual percolation of technologies from outside the industry, such as ICT, and the spread of new technologies in ferrous materials in other industries (special steels in car making, building, the railways, shipbuilding, etc.) in partnership with them.

4. Industrial policy objectives may sometimes involve forming or developing large groups supported by the state. These are national, or in some cases European champions, as we shall see in Section I. But when concentration in a given industry is relatively high, the question arises of the link between increased value resulting from size and concentration and the drawbacks resulting from less competition. This is compounded by the now constant issue of relevant markets on a global scale and the regional strategies of various major players, typically the US, the EU and China.

5. It is important not to give in to the temptation of economic nationalism, but there is no reason to be dogmatic either. When there is a limited number of operators, especially at European level, and the same applies in the United States or China, with laws that favour those operators, sometimes in a discriminatory fashion in relation to WTO rules (as is patently the case with TRIMs in China, for example), it is essential to have a genuine capacity for negotiation in order to reduce the main distortions of competition at the level where they occur. In very many cases, that now means at global level. It may involve concentrations on a continental scale or, in some cases involving a defence element in particular, on a smaller scale. The issue then is to ensure that the framing of industrial policy and competition policy is sufficiently neutral fashion for them to be implemented in a complementary way to ensure greater competitiveness and overall efficiency. This will be the subject of Section II.

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1 This paper is inspired by the competition workshops organised by DGCCRF (the French competition watchdog) on 20 April 2005 on the subject of national champions and competition law.
1. What is a champion?

1.1. How the idea of champions developed in France

6. France has a long-standing tradition of central support for industry that dates back at least as far as the royal manufactories, private enterprises under royal control granted privileges in return. An industrial policy is entirely consistent with the existence of private enterprise, as the industrial revolutions in Europe, North America and Asia have shown. The wave of nationalisations during the 1930s in reaction to the Great Depression and then in the post-war period (1945-60) can also be regarded as reflecting government's desire to create big national firms under the aegis and direct control of the state alongside a larger private sector. It was thus supply-side policies, not Keynesian demand-oriented policies, that endowed France with large-scale networks for post-war reconstruction.

7. The French tradition from the start of the 19th century until the early 1960s – and beyond, if the political narrative is to be believed – has consistently been to take the side of Davids against Goliaths, as in the retail sector. Laws were passed in the 19th century to defend small shopkeepers against "chain stores" and were stepped up under the Popular Front (1936-38) against "dollar stores".

8. The policy of "national champions" has had two main strands.

- The "de Gaulle" strand
  This is the strand of the great industrial and technological projects of the 1960s and 70, almost all in the hands of a public firm or group, which resulted in the creation of Concorde during the presidency of Charles de Gaulle, then of Airbus under Georges Pompidou and the telecommunications plan under Valéry Giscard d'Estaing.

- The "New Society" strand during the Pompidou presidency
  This strand involved State support for concentrations in the private sector, which either attracted benevolent attention (especially in the form of tax sweeteners) or sprang from a desire not to hinder firms' growth, even after the adoption of merger control legislation (Act 77-806 of 19 July 1977).

9. The Conseil d'État initially lent its weight to the idea that it can be in the general interest to concentrate state support on a single firm. In a judgment of 29 June 1951, Syndicat de la raffinerie de soufre française (Rec. p.377), it held that the administration can grant preferential terms to a single firm "when it deems it to be in the national interest to favour the expansion of a given firm”.

10. In another even more significant case, involving two French companies competing with each other to sell equipment for sugar refineries on San Domingo, the French government deliberately thwarted the efforts of one firm and favoured the other so that it could be competitive against rival foreign firms: "The investigation shows that competition between the two French groups in the face of offers from third countries was likely to be detrimental to French interests; the measures about which the plaintiff complains were therefore justified by the general interest” (CE 13 July 1963, Aureille, RDP 1964 p.205).

11. The case law also meant, for example, that no obstacle was placed in the way of the development of the Elf brand, deliberately encouraged by the French government. A decree had been issued restricting the expansion of oil firms already operating in France, stating that no new petrol station could be created within 40 kilometres of another petrol station of the same brand. An appeal by Shell was dismissed on the grounds that a law dating back to 1928, which governed the importation of oil products and the requirement to constitute reserves, allowed the regulatory authority to regulate all aspects of such firms' business (CE 19 June 1964, Sté des pétroles Shell Berre et autres, Rec.334; RDP 1964 p. 1019 concl. Mme
Commentators on the judgment were not slow to point out that this conclusion gave a certain comfort to the industrial policy of the day.

1.2. Current practices and rules relating to the protection of national interests

Some practices and rules favour the defence of national interests, but nowadays competition policy served by industrial policy has largely given way to industrial policy channelled by competition law. However, that does not mean that industrial policy and competition policy are in conflict: industry prospers through and draws strength from competition, and in Schumpeterian theory industrial policy as a whole includes competition issues. In fact, industrial policy may be said to be one of the main motive forces behind the very existence of competition (see e.g. the 2000 CAE report on industrial policies in Europe, Lorenzi, Cohen et al.).

1.2.1. The defence of national interests channelled by Community competition law

The control exercised by the European Community concerns compliance with the principles of non-discrimination and proportionality; it does not rule out all protection of certain legitimate national interests. In fact, some provisions of Community law allow for the defence of such interests.

14. In France, Article L. 153-1 I of the Monetary and Financial Code states that "Prior authorisation by the minister of the economy is required for any foreign investment in an activity in France which, even on an occasional basis, involves the exercise of public authority or falls within one of the following domains: a) Activities liable to be detrimental to public order, public safety or the interests of national defence; b) Research into and the production and marketing of weapons, munitions and explosives".

15. A decree of 31 December 2005, codified at Articles R.153-1 to R.153-5 and adopted on the basis of that article, gives a list of strategic sectors to be protected from foreign investment. The list includes seven sectors if the investment stems from an EU country (private security, communications interception equipment, data security, dual-use goods and technologies, etc.) and eleven sectors if the investment stems from a third country (cryptology, research into and production of weapons and explosives, studies and procurement for the defence ministry, etc.).

16. The minister of the economy can therefore seek certain guarantees from foreign investors wishing to acquire French companies in these so-called sensitive sectors, such as assurances about the long-term future of the activities and of industrial capacity.

17. Publication of this decree (no. 2005-1739) on 30 December 2005 led the European Commission to question whether it was consistent with the principles of the free movement of capital and the freedom of establishment. It therefore sent France a request for information on 20 January 2006, a letter of formal notice on 4 April 2006 and a reasoned opinion on 12 October 2006 to which the French government responded on 11 December 2006, indicating that the review could result in the investment not being blocked by asking the investor for "assurances limited solely to the establishment concerned". No case has been brought before the European Court of Justice on the grounds of the decree. However, the issue has still not been formally settled.

18. The French decree is not the only one of its kind, since other economic powers have similar rules:

- In Germany, certain types of foreign investment are restricted under the Foreign Trade Act of 6 May 2004 and its implementing regulations of July 2004 and September 2006. On 20 August 2008, the federal government adopted a bill extending these restrictions, under the pressure of concerns relating to the possible actions of certain sovereign wealth funds (those of China and oil
states in particular) in a context of falling stock prices and competitive asymmetry arising from those countries' business law.

- The United States have the Exon Florio Act, passed in 1988, amended by the Foreign Investment and National Security Act of 2007. An implementing regulation under the Defense Production Act of 1950 and the Foreign Investment and National Security Act was issued on 14 November 2008. Under the Webb-Pomerene Act of 1918, supplemented by the Export Trading Company Act of 1982, associations of American firms engaged in exporting\(^2\) are exempted from US antitrust laws, especially the ban on cartels, provided they do not hinder the exports of their American competitors and do not lead to price changes or practices that restrict competition on the American market. The purpose of the legislation is therefore to favour American exporters.

- Japan has a 1949 Foreign Trade Act, amended in 1992 and 1998. A ministerial order of 7 September 2007 supplements the legislation and the list of sectors for which prior authorisation is required.

- China, above all, has 67 "strategic" sectors in which foreign investment is restricted (in particular to minority shareholdings) and 34 in which it is prohibited. It tightened up the rules on 1 August 2008 in a discretionary manner.

1.2.2. Community rules allowing the defence of certain legitimate interests under European Commission oversight

   a) Article 21 of the Merger Control Regulation

19. The enforcement of European rules is sometimes accused of stymying any political strategy in the industrial sphere because it entails exercising strict control over the granting of state aid or ensuring that mergers, even when they enable the formation of a "national champion", do not lead to the creation of a dominant position. In fact, the contradiction is not as frequent as all that and the number of cases where the Commission prohibits a merger is still very small.

20. Under Article 21 of Regulation no. 139/2004 of 20 January 2004 on the control of concentrations between undertakings, the Commission has sole jurisdiction to take decisions relating to mergers with a Community dimension.

21. However, Article 21.4 states:

   "Member States may take appropriate measures to protect legitimate interests other than those taken into consideration by this Regulation and compatible with the general principles and other provisions of Community law.

   Public security, plurality of the media and prudential rules shall be regarded as legitimate interests within the meaning of the first subparagraph.

   Any other public interest must be communicated to the Commission by the Member State concerned and shall be recognised by the Commission after an assessment of its compatibility with the general principles and other provisions of Community law before the measures referred to above may be taken. The Commission shall inform the Member State concerned of its decision within 25 working days of that communication."

\(^2\) The Export Trading Company Act of 1982 relaxed the provisions of the Webb-Pomerene Act: exemption is no longer available only to associations exclusively engaged in exporting; however, the exemption applies only to exporting. In addition, exporting activities include not only goods but also services and technology transfers.

This provision was also contained in the previous regulation, no. 4064/89 of 21 December 1989.

22. The notion of public security referred to in Article 21 is relatively broad, insofar as it includes not only national defence and internal security but also the secure sourcing of a product or service of vital importance for a country's existence (CJEC, 10 July 1984, Campus Oil Limited et al. v. Minister for Industry and Energy et al.):

"Petroleum products, because of their exceptional importance as an energy source in the modern economy, are of fundamental importance for a country's existence since not only its economy but above all its institutions, its essential public services and even the survival of its inhabitants depend upon them. An interruption of supplies of petroleum products, with the resultant dangers for the country's existence, could therefore seriously affect the public security that Article 36 (new Article 30) of the Treaty allows States to protect."

23. Nonetheless, "public security may be relied on only if there is a genuine and sufficiently serious threat to a fundamental interest of society" (European Commission, E.ON v Endesa, Case M. 4197, §61).

24. If the interests of public security or plurality of the media or prudential rules are invoked, the Commission checks not only that there is a threat to a legitimate public interest but also that the country in question complies with the principles of proportionality and non-discrimination and chooses the objectively least restrictive measure to achieve the desired aim. If that is not the case, it may refer the matter to the European Court of Justice on the grounds of Article 226 of the EC Treaty, having first issued preliminary conclusions.

25. The Commission takes a strict line on disproportionate government measures designed to prevent cross-border mergers, especially as a European industrial policy is gaining ground, with the idea of "European champions".

b) Article 87 of the EC Treaty and State aid

26. Community policy on State aid is also designed to prevent distortions of competition in the single market. Governments may be responsible for restricting competition when they grant State aid to economic operators.

27. Under Article 87 of the EC Treaty "any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market".

28. Any advantage granted by a state or using state resources is deemed to constitute state aid when:

- it confers an economic advantage on the beneficiary;
- it is granted selectively to certain undertakings or for the production of certain goods;
- it could distort competition;
- it affects trade between Member States.

29. Only aid notified to the European Commission and expressly authorised by the European Union can be exempt from this ban.
30. State aid is governed by three Community regulations and the Commission assesses the measures notified to it according to guidelines which, while they have no regulatory force, inform Member States of the Commission's assessment criteria for each category of aid.

c) *From national to European champions?*

31. In practice, over-strict enforcement of Community competition rules may prevent the emergence of "European champions" while indirectly favouring the creation of non-European rivals (cf. withdrawal of the Pechiney/Alcan merger on account of the assurances demanded by the Commission, which was followed by the Alcan/Pechiney merger to the detriment of a major European firm).

32. However, the European Commission tends to understand the importance of not setting industrial strategy and common market rules against each other in the context of a globalised economy.

33. At a competition policy meeting between Japan and the European Union at Tokyo on 7 March 2006, Competition Commissioner Neelie Kroes declared: "National champions are outdated […] The borders are gone. It is all about European champions, and global champions."

34. In another speech the same year, she said that cross-border mergers within the EU were "more likely to create strong European groups able to win on global markets and at the same time provide better choice and value to European industrial and domestic consumers" (Challenges to the Integration of the European Market: Protectionism and Effective Competition Policy, 12 June 2006).

35. Viviane Reding, Commissioner for Information Society and Media said at the Rencontres du Cercle des Européens-L'Express on 7 March 2008 that "making Europe successful is a matter of building not national champions but European champions, which alone offer the capacity for development to cope with the challenges of a global economy".

36. This line of reasoning is not far removed from that of national champions, insofar as it sees itself as a defence against global competition. In her speech, talking about the need for European champions, Viviane Reding went on to say that the common market is both "a bulwark against globalisation and a driving force so that European firms can assert themselves as world leaders".

37. The logic of national or European champions is not in contradiction with competition policy. Both are instruments of public policy that can be made to work in concert to promote greater competitiveness. The issue today is how to link them better.

2. **The complementary nature of industrial and competition policy**

2.1. **The importance of industry**

38. Industry is the main locus of technological innovation and productivity gains. It can also play a strategic role in terms of independence and competitiveness.

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2.1.1. The French example

The Beffa report, *For a New Industrial Policy*, summarises the essential role industry plays in economic growth.

"Even if the share of services in the economy is growing, a solid manufacturing base is necessary for a virtuous trade balance and for growth. There is still considerable demand for manufactured goods in developed countries because it ensures their core standard of living. If the goods are not produced domestically, they have to be bought from other countries. What services can be exported to pay for manufactured goods bought abroad? In one scenario envisaged by some commentators, France could become a predominantly agricultural and tourist economy, buying its goods from other countries that specialise in manufacturing. This shift in specialisation towards low value-added sectors would make France poorer and weaken its position in international trade.

Moreover, the opposition between services and manufacturing is becoming increasingly meaningless. Growth in services is driven mainly by business services, which are growing much faster than private services (INSEE Première no. 972, June 2004). Growth in manufacturing and growth in services should therefore be regarded as complementary and not as substitutable.

More generally, manufacturing is still one of the main drivers of the economy in terms of added value and jobs. It exerts a powerful stimulus on the entire economy, especially through intermediate consumption: manufacturing consumes €0.7 of intermediate products for every €1 of output, compared with €0.4 for services (DATAR, 2004). So the importance of manufacturing should be assessed in terms that correspond to the extent of its true economic impact. Manufacturing represented 41% of French GDP and 51% of market-sector jobs in 1998. Thus, the fall in direct manufacturing employment is meaningful only if account is also taken of the almost doubling of temporary employment in manufacturing in the 1990s and the extensive outsourcing of a certain number of functions to the service sector. In addition, manufacturing has a highly structural effect on the spread of technological innovations to the economy as a whole, and as a result on its overall productivity."\(^5\)

2.1.2. At European level

Industry is a decisive factor in the European economy. Manufacturing accounts for 20% of total EU output, 75% of exports and over 80% of private-sector spending on research and development (R&D).

Productivity growth is almost twice as high in manufacturing as in the rest of the economy. Employing nearly 50 million people in the European Union, industry also acts as a driving force through its link with services, which are widely used by the manufacturing sector. Growth in services is also stimulated by industrial innovation.\(^6\)

Following the European Council meeting in Lisbon in March 2000, which set itself the goal of making the European Union "the most competitive and dynamic knowledge-based economy in the world" by 2010, the European Commission laid the foundations for a Community industrial policy because of the manufacturing industry's importance in the European economy. The policy guidelines are contained in a set

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\(^5\) Beffa report to the President of the Republic, *For a New Industrial Policy*, La Documentation Française, 2005.

of texts that include the Innovation and Competitiveness Framework Programme,\textsuperscript{7} the Communication on Manufacturing,\textsuperscript{8} the Communication on Implementing the Community Lisbon Programme on Research and Innovation\textsuperscript{9} and the Seventh Research Framework Programme.\textsuperscript{10}

2.2. The economic analysis of industrial champions: industrial policy as a factor of competitiveness

43. The Harvard school and the Chicago school are the two dominant schools of thought in industrial economy. According to the Harvard school, the structure of the market determines how firms behave, which in turn determines their performance.

44. The Chicago school turns it the other way round: firms' performance determines how they behave, which in turn determines the structure of the market. Different chains of causality naturally give rise to radically different terms of public intervention.

45. According to the Chicago school, once it is possible to enter and invest in a market where there are no barriers to entry, competition authorities should not seek to regulate the market. Because it is firms' performance that structures the market, there is no point trying to influence the structure.

46. Conversely, from the Harvard school standpoint, influencing the structure of the market may be the optimum course of action. Industrial policy, and a policy of national champions in particular, may be relevant if the idea is accepted that minimum size on certain markets leads to a certain degree of efficiency in terms of production costs and innovation. The aim in that case is to favour better performance through two main factors, namely productivity and innovation. However, this only pertains at a certain level of competition.

2.2.1. Productivity

47. The first argument in favour of industrial policy is that globalisation increases market size. It thus encourages the formation of large firms in order to benefit from greater economies of scale.

48. However, there is little empirical proof of a positive correlation between concentration and higher productivity. In contrast, in a paper published in 1996 Nickell studied the link between various indicators of competition and factor productivity growth and concluded that greater competition led to an acceleration of overall factor productivity, which slowed with higher levels of concentration and higher profits.

2.2.2. Innovation

49. Innovation is a driver of growth. Defenders of industrial policy argue that a national champion can in some cases be used to stimulate innovation.

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\textsuperscript{8} Communication from the Commission: Implementing the Community Lisbon Programme: A policy framework to strengthen EU manufacturing - towards a more integrated approach for industrial policy, COM (2005) 474.


50. The issue dates back to Schumpeter. According to the Harvard school paradigm, a large firm will innovate more because it can, because it has the resources to take risks.

51. The Beffa report\textsuperscript{11} recommends a return to national programmes, each one being coordinated by a leader or national champion. Behind this defence of innovation lies the idea that research and development by large firms trickles down to the rest of the economy, as has been the case in the telecoms sector in France.

52. Schumpeter argues that R&D is an activity in which there are returns of scale. In addition, innovation will be more easily spread in a large firm. Furthermore, less competition on the product market will favour the creation of rents, which will in turn encourage other firms to enter the market by innovating. Consequently, the leading firm will be encouraged to innovate more in order to preserve its position.

53. This argument can be backed up by a "race to innovate" argument. Where there is a race to innovate between a monopoly and a competitor, the former will keep its monopoly power if it is the first to innovate. If the potential rival is the first to innovate, the market becomes a duopoly. The monopoly therefore has more to lose by not innovating than its rival.

54. Another argument is based on risk diversification. R&D is a risky business. A large firm with a range of activities will spread the risk of failure among all its activities. The state can also play this risk-spreading role in the framework of major programmes.

55. The last argument concerns funding. Since financial markets are imperfect, firms need to finance their R&D spending partly from their own resources. Large firms, which have more such resources, are therefore more capable of innovating than smaller firms.

56. Conversely, there is a replacement effect theory according to which innovation is a process of "creative destruction". Each innovation will create a negative externality for the owner of the destroyed innovation. A monopoly that innovates is therefore obliged to destroy its previous innovation. Consequently, it will be less inclined to innovate unless the competitive nature of the market encourages it to do so.

57. However, the creative destruction process will favour skilled employment generated by the innovation.

58. In conclusion, the existence of a national champion can enhance both the incentive to innovate and productivity provided that a certain degree of competition exists on the market. Ultimately, however, everything depends on the size of the market.

59. Industrial policy and competition policy thus go hand in hand in making the economy more efficient and more competitive.

2.3. The complementary nature of industrial and competition policy

60. For the supporters of economic nationalism, industrial policy makes up for the adverse effects of a competition policy that favours opening up frontiers and capital ownership. In particular, they start from the assumption that the nationality of a firm's owners and the place where it has its headquarters influence

\textsuperscript{11} Op. cit.
the location of its activities and, above all, the protection of national jobs. Economic nationalists see proof of this theory in the few examples that bear it out.  

61. Yet there is no proof that changes in the ownership of firms systematically affect the location of their activities and no proof that, even if such effects exist, they are due to the fact that the new owner is foreign. It is true that foreign firms are "less susceptible to pressure from unions, the media, politicians and even governments", but any job cuts they may make could simply be rational in economic terms. In a global economy, the strategic choice of where to locate production depends to a great extent on the availability of skilled labour. The European Union must face the challenge of growing competition, in particular from emerging countries. Current trends carry a risk of disindustrialisation in Europe, reflected in the relocation of a significant number of production centres to third countries.

62. Industrial policy and competition policy are not mutually exclusive: on the contrary, insofar as their goal is greater competitiveness and a healthy economic situation, they are complementary in the long term. Action in the name of industrial policy can be lastingly meaningful and effective only if the firms that benefit are exposed to genuine competition in a context of fair and sound international trade.

63. Moreover, competition policy is not in contradiction with the industrial policies implemented at national and/or European level. It does not prohibit the formation of industrial champions. It could merely entail the prohibition of mergers that irretrievably distort competition.

64. Mario Monti, then European Competition Commissioner, said at a hearing of the Senate Economic Affairs Committee on 8 June 2004 that European competition rules, far from hindering the emergence of industrial champions, in fact encouraged them, partly because of the size of the European market and partly because of the one-stop shop and the uniformity of Community competition rules. He pointed out that very few mergers were ever rejected, allowing for the formation of large groups that were competitive on a global scale.

65. The report A European Strategy for Globalisation of the "Europe and Globalisation" mission chaired by Laurent Cohen-Tanugi, published in April 2008 for the French presidency of the Council of the European Union, said that the Commission "had prevented only about thirty European mergers and acquisitions in the last twenty years (out of over 3,000 notified transactions), allowing for […] the creation of a large number of European and national champions".  

66. Competition can therefore go hand in hand with an effective industrial policy. Greater competition in the telecoms sector, for example, has led to the emergence of European champions like Ericsson and Siemens. "Competition policy should not be seen as serving solely to defend competition but rather as a means of achieving economic efficiency."

67. Recognising the goals of industrial policy does not necessarily imply lowering the sights and the resources of competition policy, contrary to the ideas of certain economists who assert that the notion of industrial champion is in complete contradiction with the atomicity criterion of the pure and perfect

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12 Closure of plants in France when Alcan acquired Pechiney.

13 Augustin Landier and David Thesmar, "Quel patriotisme économique au XXIe siècle?" in Problèmes Economiques, La Documentation Française, 5 July 2006 (no. 2.903), p.29.


15 D. Encaoua and R. Guesnerie, Politiques de concurrence, Report by the Conseil d’Analyse Economique, 2006 (no. 60), La Documentation Française, p.109.
competition model. Every economy needs operators to compete with other economies, and operators need to achieve a size that enables them to survive, grow and innovate on increasingly extended geographical markets.

68. The Commission takes these things into account when it assesses the impact of mergers, acquisitions and abuses of dominant position. In doing so, it uses a definition of relevant markets that "includes their geographical scope and increased globalisation".\textsuperscript{16}

69. In their report on competition policy,\textsuperscript{17} David Encaoua and Roger Guesnerie say not only that "competition is only one factor of innovation and technological progress", but also "our conviction is clear: competition is a necessary but insufficient condition for the European Union to return to the path of growth and competitiveness".

70. In conclusion, competition policy and industrial policy share the same objective of economic efficiency and competitiveness and must be framed and implemented in a complementary and coordinated manner.

71. On this point, the competition policy report mentioned above\textsuperscript{18} recommends closer cooperation between DG Competition, DG Enterprise and Industry and DG Research, especially for the assessment of mergers that involve significant industrial competitiveness issues.

72. Under Article L. 430-7-1 II of France's Commercial Code these issues can be taken into account since the minister of the economy can include industrial policy criteria in merger decisions. In contrast, the Competition Authority's assessment is based strictly on competition criteria.

2.4. International competition issues in Community policies

73. Competition policy and industrial policy theoretically share the twin goal of making firms more efficient and better preparing them for domestic and international competition. The legal foundations for Community competition policy are laid at Articles 81 to 87 of the EC Treaty. The legal basis for Community industrial policy is provided by Article 157, which states that all policies should contribute to the objectives of industrial policy but also that "this title shall not provide a basis for the introduction […] of any measure which could lead to a distortion of competition". In practice, as we have seen, these two approaches can give rise to diverging or even conflicting interpretations.

2.4.1. Public action to favour the emergence of innovative firms

74. Encouraging firms to increase their spending on R&D and innovation must not of course disturb the normal operation of the market and of competition. Public intervention is designed to remedy the shortcomings of the market in compliance with Community rules on state aid. Some R&D and innovation projects do not come to fruition for various reasons:

- innovative small businesses do not have sufficient resources of their own and either cannot raise money from banks or can do so only on harsh terms;

\textsuperscript{16} L. Cohen-Tanugi, op. cit., p.152.
\textsuperscript{17} Op. cit.
\textsuperscript{18} D. Encaoua and R. Guesnerie, \textit{Politiques de concurrence}, Report by the Conseil d’Analyse Economique, 2006 (no. 60), La Documentation Française.
• firms are naturally disinclined to cooperate with each other even when a subject of research cannot be envisaged other than in partnership;
• the costs and risks are too great, even though substantial benefits for society could result.

75. In such situations, governments have over time developed complementary approaches to meet operators' varying needs. Such actions have been authorised by the European Commission after ensuring that there are good reasons for them and they do not have adverse effects on intracommunity competition.

76. Community control of aid for R&D and innovation is designed to forestall the adverse effects of aid on competing firms in Member States. But this line of reasoning, though legitimate with regard to the objectives of strengthening the common market, is not always satisfactory. The restrictive definition of research activities eligible for aid, the setting of maximum intensities, the institution of a long and cumbersome review procedure for the biggest projects at Community level, after a lengthy national procedure, are restrictions that exist only within the European Union. Yet competition in research is global.

77. It now seems essential to ask questions about the impact of these restrictions, of this control of R&D and innovation aid on European firms' competitiveness in a context of open and global competition.

78. The aim is not to dispense with all Community control of aid, which is one of the foundations on which the common market is built, but to reassert that the basis for controlling aid is the construction and strengthening of the common market in a changing international environment. It is an aim that concurs with the approach endorsed by the Commission itself in its action plan 2005-2009 adopted on 15 July 2005: "State aid policy […] must contribute by itself and by reinforcing other policies to making Europe a more attractive place to invest and work, building up knowledge and innovation for growth and creating more and better jobs".

79. Reinforcing policies for supporting R&D and innovation involves taking more account of international competition in internal Community policies. The emergence of European champions also involves developing high-risk projects that the market sometimes seems unwilling to finance itself.

80. A consideration of the strategic importance of projects and not merely of market shortcomings and the effect on competition should become an element of competition policy if Europe wants to see more European champions emerge. It is already the rule in the United States and Japan.

2.5. Introducing industrial policy criteria into the application of competition law: a recent French example

81. Following the recent reform of the French merger control system, the Competition Authority cannot take industrial policy considerations into account when assessing proposed mergers, though it may where appropriate include gains in economic efficiency that make up for restrictions of competition (see Section 2.3 above). However, the minister of the economy can take account of industrial policy considerations more broadly after the procedure is complete.

82. The Economic Modernisation Act (Act 2008-776 of 4 August 2008) reformed the competition aspect of market regulation in France, especially the rules on merger control. The Competition Authority will examine merger requests from a competition standpoint.

83. The minister of the economy retains a right of pre-emption (évocation) at the end of phase 2. Article L. 430-7-1 II of the Commercial Code states that "the minister of the economy may pre-empt the
matter and rule on the transaction at issue on general interest grounds other than the maintenance of competition and, where appropriate, making up for the anti-competitive effects of the transaction."

84. It goes on to say that "the general interest grounds other than maintenance of competition that may cause the minister of the economy to pre-empt the matter include in particular industrial development, the competitiveness of the undertakings concerned with regard to international competition and the creation or preservation of jobs".

85. Granting this right of pre-emption is justified by the need to allow for an overall assessment of mergers deemed to be strategic, where the authorities consider it essential that they should be allowed to continue to reconcile the requirements of regulating competition with those of other public policies. A minister who pre-empts a decision taken by the Competition Authority must take a reasoned decision which may be conditional on the fulfilment of undertakings (Article L. 430-7-1 II, paragraph 3).

86. The minister has considerable scope, since he or she may not only ignore a refusal but also veto a transaction authorised by the Competition Authority.

87. Similar procedures exist in other European countries:

- under Article 42 of Germany’s antitrust law, the federal government may authorise a merger prohibited by the competition authority (though not vice versa). Since the system was introduced in 1973, the German government has authorised a merger in 11 of the 170 cases where the proposed transaction was refused by the Federal Cartel Office;
- in the United Kingdom, under the Enterprise Act which came into force in June 2003, the government can ask the Competition Commission to conduct a detailed examination of mergers where a specific public interest is at stake (plurality of the media, water supply, defence procurement). The government can prohibit a merger authorised by the Competition Commission.

88. The procedure means that specific sectoral factors can be taken into account when competition policies are analysed, a measure that the competition policy report mentioned earlier\(^{19}\) regards as necessary.

89. By promoting greater competitiveness and greater overall efficiency, competition policy and industrial policy are thus entirely complementary.

\(^{19}\) CAE report, op. cit.
CONTRIBUTION DE LA FRANCE
1. Jusqu’au début des années 90 environ, on pouvait encore qualifier la politique industrielle d’instrument de politique économique conduite par le Gouvernement dans l’objectif de promouvoir certains secteurs d’activité pour des raisons d’indépendance nationale, d’autonomie technologique ou d’équilibre territorial. De facto, depuis plus de 15 ans maintenant, l’activité principale des autorités françaises en matière industrielle a tendu à avoir une politique d’innovation, et non pas une politique sectorielle, quitte à promouvoir les technologies génériques les plus porteuses (société de la connaissance et TIC, problématiques de santé et biotechnologies, matériaux et nanotechnologies, notamment).

2. De la même manière, on ne peut plus définir simplement la politique industrielle comme l’ensemble des politiques verticales par opposition aux politiques horizontales, telles que la politique de concurrence. Les politiques d’innovation notamment sont largement horizontales, ainsi que celles concernant la propriété intellectuelle, les formations supérieures orientées vers les entreprises, l’entrepreneuriat, l’environnement des PME, le design, les adaptations de l’appareil productif aux variations de la demande mondiale en termes géopolitiques, le développement durable et les éco-industries requises pour la réduction des gaz à effet de serre, les priorités fiscales s’agissant des entreprises, etc.

3. Les politiques verticales ne sont donc pas des politiques de structure qui viseraient à agir sur la rationalisation des industries et la concentration des entreprises, et qui ne porteraient que sur la coordination entre les différents acteurs d’un même secteur comme dans les années 70. A titre d’illustration, des métiers aussi « traditionnels » que la sidérurgie progressent non pas par « de la coordination entre les différents acteurs d’un même secteur », mais par de la percolation de technologies exogènes au secteur sidérurgique, d’une part (TIC, par exemple), et par de la diffusion de technologies nouvelles sur les matériaux ferreux dans d’autres secteurs (aciers spéciaux dans l’automobile, le bâtiment, le ferroviaire, la construction navale, etc.) en partenariat avec ceux-ci.

4. Les objectifs de la politique industrielle peuvent parfois passer par la constitution ou le développement de grands groupes soutenus par les États. On parle alors de champions industriels, nationaux, voire européens (1). Mais, dans les cas où le degré de concentration d’un domaine est assez élevé, se pose la question de l’articulation entre des gains de valeur liés à la taille et à la concentration, et les inconvénients qui résulteraient d’une réduction de la concurrence, le tout avec une problématique, désormais permanente, des marchés pertinents à l’échelle mondiale et des politiques stratégiques menées par différents grands acteurs à l’échelle régionale (US, UE, Chine, typiquement).

5. L’écueil est de ne pas céder à la tentation du nationalisme économique mais il convient également de ne pas être dogmatique : lorsqu’il y a, notamment au niveau européen, un nombre limité d’opérateurs, et de même aux États-Unis ou en Chine, avec des dispositions légales favorisant ces opérateurs, parfois de façon discriminatoire au regard des règles de l’OMC (ce qui est patent en Chine actuellement sur les TRIMs, par exemple), il est impératif d’avoir une réelle capacité de négociation pour réduire les principales distorsions de concurrence au niveau où elles se présentent, c’est-à-dire, désormais, très souvent à l’échelle mondiale ; cela peut passer par des concentrations à une échelle continentale, ou, dans certains cas liés à la défense notamment, plus réduite. Il s’agit alors de faire en sorte que politique industrielle et politique de concurrence soient édictées de manière suffisamment neutre pour permettre une

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1 Cette contribution est inspirée des ateliers de concurrence organisés par la DGCCRF le 20 avril 2005, autour du thème : “champions nationaux” et droit de la concurrence.
mise en œuvre dans le sens d’une complémentarité pour assurer une plus grande compétitivité et efficacité globale (II).

1. **La notion de «champion industriel»**

1.1. **La construction de la notion de champion en France**


7. La tradition française, du début du XIXème siècle jusqu’au début des années 60 - et au-delà, s’il s’agit des discours politiques - est faite prioritairement de défense des « petits » contre les « grands » opérateurs, comme dans le secteur de la distribution. La défense des petits commerces est en effet inscrite dans la législation dès le XIXème pour lutter contre les « chaînes de succursales » et elle est renforcée sous le Front populaire contre les « magasins à prix unique ».

8. La politique des « champions nationaux » s'est développée, selon deux versants principaux:

- le versant « gaullien »
  Ce versant est celui des grands projets industriels et technologiques des années 60 et 70, presque toujours portés par une entreprise publique ou un groupe public, ayant permis la création du Concorde durant la Présidence de Charles de Gaulle, puis d’Airbus sous Georges Pompidou, ou encore du plan télécommunications sous Valéry Giscard d’Estaing.

- le versant de la « Nouvelle Société » durant la Présidence de George Pompidou
  Ce volet se traduit quant à lui par l'accompagnement par l'État des concentrations dans le secteur privé. Ces concentrations font alors l'objet, soit d'une bienveillance attentive (à travers notamment des agréments fiscaux), soit d'une volonté de ne pas entraver la croissance des entreprises, même après l'adoption de la loi du 19 juillet 1977 sur le contrôle des concentrations économiques.

9. Le Conseil d’État a d'abord apporté son concours à la mise en œuvre de l'idée qu'il peut être conforme à l'intérêt général de concentrer le soutien de l'État sur une seule entreprise déterminée. Ainsi, le Conseil d’État, dans un arrêt du 29 juin 1951, * Syndicat de la raffinerie de soufre française* (Rec. p.377), énonçait que l'administration peut accorder des conditions privilégiées à une seule entreprise « lorsqu'elle estime qu'il est de l'intérêt national de favoriser l'expansion d'une entreprise déterminée ».

10. Une autre affaire était encore plus significative : en présence de deux entreprises françaises en concurrence pour la vente d'équipements pour des usines sucrières à Saint-Domingue, l'administration française avait délibérément contrecarré les initiatives de l'une et favorisé l'autre afin que cette dernière puisse être compétitive face aux entreprises étrangères concurrentes : « il résulte de l'instruction que la concurrence de deux groupes français en face d'offres de pays tiers était de nature à nuire aux intérêts français ;(que) les mesures dont se plaint le requérant se trouvaient ainsi justifiées par l'intérêt général » (CE 13 juillet 1963, Aureille, RDP 1964 p.205).
11. La jurisprudence a également permis, par exemple, de ne pas faire obstacle au développement de l'enseigne Elf délibérément encouragé par le gouvernement français. Un décret avait été pris pour limiter le développement des groupes pétroliers déjà présents sur le territoire français, en précisant qu'aucune nouvelle station-service ne pouvait être créée à moins de 40 kilomètres d'une station de la même marque ; le recours de la société Shell a été écarté au motif qu'une loi datant de 1928 - qui régissait l'importation des produits pétroliers et l'obligation de constituer des stocks de réserve - permettait au pouvoir réglementaire de réglementer tous les aspects de l'activité de ces entreprises (CE 19 juin 1964, Sté des pétroles Shell Berre et autres, Rec.334 ; RDP 1964 p. 1019 concl. Mme Questiaux ; D. 1964 J. p. 438 note A. de Laubadère). Les commentateurs de l'arrêt n'avaient pas manqué de relever qu'une telle solution donnait un certain confort à la politique industrielle de l'époque.

1.2. Les pratiques et textes actuels relatifs à la protection des intérêts nationaux

12. Certaines pratiques et certains textes favorisent la défense d’intérêts nationaux mais aujourd’hui, à une politique de la concurrence instrumentalisée par la politique industrielle, a succédé, dans une large mesure, une politique industrielle canalisée par le droit de la concurrence. Il ne s’agit pas cependant d’opposer politique industrielle et politique de concurrence : l’industrie prospère par la concurrence, son dynamisme en découle, et selon la théorie schumpétérienne, la politique industrielle, prise dans son ensemble, inclut largement des préoccupations de concurrence. On peut dire qu’elle est l’un des principaux moteurs de son existence même (voir par exemple le rapport du CAE de 2000, sur les politiques industrielles en Europe, Lorenzi, Cohen & alii).

1.2.1. La défense d’intérêts nationaux canalisée par le droit de la concurrence communautaire

13. Le contrôle de la Communauté européenne est un contrôle du respect des principes de non-discrimination et de proportionnalité : il n’empêche pas toute protection de certains intérêts légitimes nationaux. Par ailleurs, certaines dispositions du droit communautaire permettent la défense de ces intérêts.

14. En France, l’article L153-1 I du Code monétaire et financier prévoit que « Sont soumis à autorisation préalable du ministre chargé de l’économie les investissements étrangers dans une activité en France qui, même à titre occasionnel, participe à l'exercice de l'autorité publique ou relève de l’un des domaines suivants : a) Activités de nature à porter atteinte à l'ordre public, à la sécurité publique ou aux intérêts de la défense nationale ; b) Activités de recherche, de production ou de commercialisation d'armes, de munitions, de poudres et substances explosives ».

15. Un décret du 31 décembre 2005 codifié aux articles R.153-1 à R.153-5, et adopté sur le fondement de cet article indique une liste de secteurs stratégiques à protéger des investissements étrangers. Cette liste comprend 7 secteurs si ces investissements proviennent de pays de l’Union européenne (les activités de sécurité privée, les matériels d’interception des communications, la sécurité informatique, les biens et technologies à double usage…) et 11 secteurs si les investissements sont en provenance d’un pays tiers (crypotlogie, recherche et production d’armes et substances explosives, études et équipement au profit du ministère de la défense…).

16. Le Ministre de l’Économie peut donc demander certaines garanties aux investisseurs étrangers souhaitant racheter des sociétés françaises, appartenant à ces secteurs dits sensibles. Il pourrait exiger par exemple la pérennité des activités et des capacités industrielles.

17. La publication de ce décret n°2005-1739 le 30 décembre 2005 a amené la Commission européenne à s’interroger sur la conformité de ce décret aux principes de liberté de circulation des capitaux et de liberté d'établissement. Elle a donc envoyé à la France une lettre de demande d’information le 20 janvier 2006, une lettre de mise en demeure le 4 avril 2006 et un avis motivé le 12 octobre 2006 auquel le
gouvernement français a répondu le 11 décembre 2006 en indiquant que l’examen pouvait ne pas donner lieu à un blocage des investissements en demandant à l’investisseur « des engagements limités au seul établissement concerné ». Le décret n’a pas donné lieu à la saisine de la CJCE. Néanmoins, le cas n’est toujours pas formellement clos.

18. Il faut au demeurant noter que cela s’inscrivait dans une démarche commune avec d’autres puissances économiques:

- ainsi l’Allemagne par la loi du 6 mai 2004 et ses décrets d’application de juillet 2004 et septembre 2005 s’attachait à limiter certains investissements étrangers. Le gouvernement fédéral a adopté le 20 août 2008 un projet de loi qui étend ce dispositif, sous la pression des inquiétudes relatives aux actions possibles de certains fonds souverains (chinois et pétroliers notamment) dans un contexte de dépression des cours des actions, et d’asymétrie concurrentielle du droit commercial de ces pays ;


- le Japon dispose d’une loi sur le commerce extérieur de 1949, amendée en 1992 et 1998 ; un arrêté ministériel du 7 septembre 2007 complète cette loi et la liste des secteurs soumis à autorisation préalable ;

- la Chine, surtout, a 67 secteurs « stratégiques » dans lesquels les investissements étrangers sont restreints (notamment à une situation de minoritaire) et 34 dans lesquels ils sont interdits. Elle a durci ce dispositif le 1er août 2008 de façon discrétionnaire.

1.2.2. Des dispositions communautaires permettant la défense de certains intérêts légitimes sous contrôle de la Commission

a) L’article 21 du règlement relatif au contrôle des concentrations entre entreprises

19. L’application des règles européennes est parfois accusée de faire échec à toute stratégie politique en matière industrielle car elle conduit à exercer un contrôle strict de l’attribution des aides d’État ou à vérifier que les fusions d’entreprises, même lorsqu’elles permettent de construire un « champion national » ne conduisent pas à la création d’une position dominante. En réalité, la contradiction n’est pas si fréquente et le nombre de cas où la Commission a interdit une opération de concentration reste très limité.


2 L’Export trading company act de 1982 a assoupli les dispositions du Webb-Pomerene act : l’exemption ne s’applique plus uniquement aux associations ayant exclusivement une activité d’exportation, en revanche, l’exemption ne s’applique qu’aux activités d’exportation. En outre, il peut s’agir d’exportation de marchandises mais aussi de services et transferts de technologie.
21. Néanmoins, le point 4 de cet article 21 prévoit que

« les États membres peuvent prendre les mesures appropriées pour assurer la protection d'intérêts légitimes autres que ceux qui sont pris en considération par le présent règlement et compatibles avec les principes généraux et les autres dispositions du droit communautaire.

Sont considérés comme intérêts légitimes, au sens du premier alinéa, la sécurité publique, la pluralité des médias et les règles prudentielles.

Tout autre intérêt public doit être communiqué par l’État membre concerné à la Commission et reconnu par celle-ci après examen de sa compatibilité avec les principes généraux et les autres dispositions du droit communautaire avant que les mesures visées ci-dessus puissent être prises. La Commission notifie sa décision à l’État membre concerné dans un délai de vingt-cinq jours ouvrables à dater de ladite communication ».


22. La notion de sécurité publique visée par l’article 21 est relativement large en ce qu’elle comprend la défense nationale, la sécurité intérieure mais aussi la sécurité d’approvisionnement d’un produit ou d’un service ayant une importance fondamentale pour l’existence d’un État (CJCE, 10 juillet 1984, Campus Oil Limited e.a. c/ Ministre de l’Industrie et de l’Énergie :

« Les produits pétroliers, par leur importance exceptionnelle comme source d’énergie dans l’économie moderne, sont fondamentaux pour l’existence d’un État dès lors que le fonctionnement non seulement de son économie mais surtout de ses institutions et de ses services publics essentiels et même la survie de sa population en dépendent. Une interruption de l’approvisionnement en produits pétroliers et les risques qui en résultent pour l’existence d’un État peuvent dès lors gravement affecter sa sécurité publique, que l’article 36 (nouvel article 30) permet de protéger »).

23. Néanmoins, « la sécurité publique ne peut être invoquée que lorsqu’il y a une menace véritable et suffisamment sérieuse à un intérêt fondamental de la société » (Commission européenne, E.on c/Endesa, aff M.4197, §61)

24. Si cet intérêt de sécurité ou ceux de la pluralité des médias et des règles prudentielles sont invoqués, la Commission vérifie qu’il s’agit bien d’un intérêt public et légitime menacé mais également que l’État en cause respecte les principes de proportionnalité et de non-discrimination, et choisit la mesure la moins restrictive objectivement pour atteindre l’objectif poursuivi. Dans le cas contraire, elle peut saisir la CJCE sur le fondement de l’article 226 du Traité CE, après avoir émis des conclusions préliminaires.

25. La Commission est par ailleurs sévère vis-à-vis des mesures étatiques disproportionnées et bloquantes à l’encontre des fusions transfrontières et ce d’autant plus qu’une politique industrielle européenne se développe, avec l’idée de « champions européens ».

26. La politique communautaire relative aux aides d’État vise également à empêcher les distorsions de concurrence sur le marché intérieur. En effet, les restrictions de la concurrence peuvent être le fait des gouvernements lorsque ceux-ci accordent des aides publiques aux opérateurs économiques.

3 JO L 24 du 29 janvier 2004, p. 1–22
27. L’article 87 du traité déclare incompatibles avec le marché intérieur « dans la mesure où elles affectent les échanges entre les États membres, les aides accordées par les États ou au moyen de ressources d’État sous quelque forme que ce soit, qui faussent ou qui menacent de fausser la concurrence en favorisant certaines entreprises ou certaines productions ».

28. Tout avantage accordé par l’État ou au moyen des ressources de l’État est considéré comme une aide d’État lorsque :

- il confère un avantage économique à son bénéficiaire ;
- il est octroyé de manière sélective à certaines entreprises ou certaines productions ;
- il risque de fausser la concurrence ; et
- il affecte les échanges entre les États membres

29. Seules peuvent être exemptes de cette interdiction les aides notifiées à Bruxelles et expressément autorisées par l’Union européenne.

30. Les aides d’État sont régies par trois règlements communautaires et la Commission apprécie les mesures qui lui sont notifiées en fonction de lignes directrices qui n’ont pas de valeur réglementaire mais qui permettent aux États membres de connaître les critères d’appréciation de la CE par catégories d’aides.

   c) Des champions nationaux aux champions européens ?

31. En pratique une application trop rigoureuse des règles de concurrence communautaire peut empêcher l’émergence de « champions européens » tout en favorisant indirectement la création de concurrents extra européens (Cf. le retrait de la fusion Pechiney/Alcan face aux demandes d’engagements de la Commission alors que cette opération sera suivie de la fusion Alcan/Pechiney qui se fera au détriment d’une grande entreprise européenne).

32. Cependant, la Commission européenne tend à réaliser l’importance de ne pas opposer stratégie industrielle et règle du marché intérieur dans le contexte d’une économie mondialisée.

33. Lors d’une rencontre sur la concurrence entre le Japon et l’Union européenne organisée à Tokyo le 7 mars 2006, Nelly Kroes déclarait : "national champions are outdated (…) The borders are gone. It is all about European champions, and global champions" (« les champions nationaux sont dépassés (…) Les frontières ont disparu. Ce qui compte aujourd’hui, c’est seulement les champions européens et les champions mondiaux »).

34. Dans un discours, la même année, elle déclara que les fusions transfrontalières intra-UE étaient « plus susceptibles de créer de grands groupes européens forts et capables de gagner sur les marchés internationaux tout en permettant aux consommateurs européens, industriels et privés, de bénéficier d’un meilleur choix et d’une meilleure qualité » (Challenges to the Integration of the European Market: Protectionism and Effective Competition Policy, 12 juin 2006).


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4. - Règlement de procédure CE 659/1999 du conseil complété par un règlement CE784/2004 de la Commission
   - Règlement autorisant les exemptions par catégories CE994/98 du conseil et un règlement d’exemption par catégories CE 800/2008 de la commission
déclarait également que « Réussir l’Europe, ce n’est pas proposer de bâti des champions nationaux, mais bien des champions européens qui seuls offrent cette capacité de développement adaptée aux enjeux d’une économie globalisée ».

36. Cette logique n’est pas loin de celle des champions nationaux en ce qu’elle se conçoit comme une défense face à la concurrence mondiale. Ainsi, dans son discours de mars 2008, Viviane Reding, en parlant de la nécessité de champions européens, indiquait que le marché intérieur est à la fois « un rempart face à la globalisation et un moteur pour que les entreprises européennes s’affirment comme leaders mondiaux ».

37. Cette logique des champions nationaux ou européens n’est pas en contradiction avec la politique de concurrence. Ces politiques sont deux instruments de la politique publique qui peuvent utilement être mis en œuvre de concert dans le sens d’une plus grande compétitivité. Il convient aujourd’hui de chercher les voies d’une meilleure articulation.

2. La complémentarité des politiques industrielles et de concurrence

2.1. L’importance de l’industriel

38. L’industrie est le lieu principal des innovations technologiques et des gains de productivité. L’industrie peut aussi avoir un rôle stratégique en termes d’indépendance et de compétitivité.

2.1.1. L’exemple français


« Même si la part des services dans l’économie s’accroît, une industrie solide est nécessaire à un équilibre vertueux de la balance commerciale et à la croissance. En effet, la demande en biens industriels des pays développés reste importante, car elle assure l’essentiel de leur qualité de vie. Si ces biens ne sont pas produits, ils doivent être achetés à l’étranger. Quels services exportables peuvent être la contrepartie de l’achat des biens industriels à l’étranger ? Selon un scénario envisagé par certains auteurs, la France pourrait devenir essentiellement agricole et touristique et acheter ses biens à d’autres pays spécialisés dans la production industrielle. Cette évolution de la spécialisation vers des secteurs à faible valeur ajoutée appauvrirait la France et fragiliserait sa position dans le commerce international.

Par ailleurs, l’opposition entre services et industrie perd son sens. En effet, le développement des services est essentiellement porté par les services aux entreprises, qui croissent bien plus vite que les services aux particuliers (INSEE première n° 972, juin 2004). Il faut ainsi penser le développement industriel et le développement des services comme complémentaires et non comme substituables.

diffusion des innovations technologiques à l’ensemble de l’économie et, par extension, sur sa productivité globale ».

2.1.2. Au niveau européen

40. L’industrie est une composante déterminante de l’économie européenne. L’industrie manufacturière assure ainsi 20% de la production totale de l’Union européenne, 75% de ses exportations et plus de 80% des dépenses privées de recherche et développement (R&D).

41. La croissance de la productivité y est près de deux fois plus élevée que dans le reste de l’économie. Employant près de 50 millions de personnes dans l’Union européenne, l’industrie a également un rôle d’entraînement en raison de son lien avec le secteur des services, lesquels sont largement utilisés par l’industrie et bénéficient des innovations industrielles pour leur développement.

42. Suite au Conseil européen de Lisbonne de mars 2000 qui s’était fixé pour objectif de faire de l’Union européenne « l’économie de la connaissance la plus compétitive et la plus dynamique du monde » à l’horizon de 2010, la Commission européenne a posé les bases d’une politique industrielle communautaire, en raison de l’importance de l’industrie dans l’économie européenne. Les orientations de cette politique sont présentées dans un ensemble de textes : le programme-cadre pour l’innovation et la compétitivité, la communication sur l’industrie manufacturière, la communication relative à la mise en place du programme communautaire de Lisbonne en matière de recherche et d’innovation et le septième programme-cadre pour la recherche.

2.2. L’analyse économique relative aux champions industriels : les politiques industrielles comme facteur de compétitivité


44. L’école de Chicago renverse la causalité : selon elle, la performance des entreprises va causer leur conduite, laquelle va causer la structure du marché. Naturellement, la modalité de l’intervention publique est radicalement différente selon la nature de la causalité.

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5 Rapport Beffa au Président de la République, « Pour une nouvelle politique industrielle », La Documentation française, 2005.


10 Proposition de décision du Parlement européen et du Conseil relative au septième programme-cadre de la Communauté européenne pour des activités de recherche, de développement technologique et de démonstration (2007-2013), COM (2005) 119
45. Selon l'école de Chicago: à partir du moment où il est possible d’entrer, d'investir sur un marché où les barrières à l'entrée sur le marché sont absentes, les autorités de concurrence ne devraient pas se soucier de régulation des dits marchés : puisque la performance des entreprises cause la structure du marché, il ne sert à rien d'agir sur cette structure.

46. A l'inverse, dans l'optique de l'école de Harvard, il peut être optimal d'agir sur la structure du marché ; la politique industrielle - et notamment la politique des champions nationaux - peut être pertinente. Si l'on accepte l'idée qu'une taille minimale sur certains marchés est synonyme d'une certaine efficacité en termes de coûts de production et d'innovation. Il s'agit alors de favoriser une plus grande performance, à travers deux principaux aspects : l’efficacité productive et l’innovation. Ceci dit, cela n’est vrai qu’à un certain degré de concurrence.

2.2.1. L'efficacité productive

47. Le premier argument en faveur de la politique industrielle est le suivant : la globalisation des économies accroît la taille des marchés. Cette globalisation incite donc à la création de grands groupes, de manière à bénéficier d'économies d'échelle plus importantes.

48. Cependant, il existe peu de preuves empiriques d'une corrélation positive entre une certaine concentration sur le marché et une plus forte productivité. En revanche, Nickell a étudié en 1996 la relation entre différents indicateurs de concurrence et la croissance de la productivité des facteurs. Il en déduit qu'une intensification de la concurrence se traduit par une accélération de la productivité globale des facteurs, laquelle ralentit avec le renforcement de la concentration et la hausse des profits.

2.2.2. L'innovation

49. L'innovation est un moteur de la croissance. Les défenseurs de la politique industrielle arguent du fait que le champion national - dans certains cas - peut être utilisé pour stimuler l'innovation.

50. Cette question remonte aux travaux de Schumpeter. Si l'on suit le paradigme de l'école de Harvard, on dira qu'une entreprise importante va innover plus parce qu'elle le peut, qu'elle a les moyens de prendre des risques.

51. Le rapport Beffa préconise le retour des programmes nationaux, chacun de ces programmes étant coordonné par un leader ou un champion national. Derrière cette défense de l'innovation se profile l'idée de diffusion technologique de la recherche et développement (R&D) des grosses entreprises vers le reste de l'économie, tel que cela a été le cas dans le domaine des télécoms en France.

52. D'après Schumpeter, l'activité de R&D est une activité dans laquelle il existe des rendements d'échelle. En outre, une innovation sera plus facilement diffusée au sein d'une grande entreprise. Par ailleurs, une moindre concurrence sur le marché des produits va permettre la création de rentes, laquelle va inciter d'autres entreprises à rentrer sur le marché en innovant. Par conséquent, l'entreprise leader sera incitée à innover plus pour conserver sa position.

53. Cet argument peut être complété par un argument de course à l'innovation. En cas de course à l'innovation entre un monopole et son concurrent, si le monopole innove en premier, il conserve son pouvoir de monopole. Si au contraire le rival potentiel innove en premier, le marché se transforme en duopole. Par conséquent, le monopole a donc plus à perdre à ne pas innover que son rival.

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Un autre argument repose sur la diversification des risques. En effet, la R&D est une activité risquée. Une grosse entreprise multi-activités va diversifier le risque de ne pas trouver entre toutes ses activités. Ce rôle de diversification des risques peut également être joué par l'État dans le cadre des grands programmes.

Le dernier argument est un argument de financement. Puisque les marchés financiers sont imparfaits, les entreprises doivent financer en partie leurs investissements en R&D sur leurs ressources propres. Les grosses entreprises, qui disposent de ressources propres plus importantes ont donc plus de capacité d'innover que les entreprises de moindre taille.

Au contraire, il existe une théorie de l’effet de remplacement selon laquelle l’innovation est un processus de "destruction créatrice de valeur". Chaque innovation va créer une externalité négative pour le détenteur de l'innovation détruite. Un monopole qui innove se voit donc contraint à détruire sa précédente innovation. Par conséquent, il sera moins enclin à innover, à moins que le marché, de par son caractère concurrentiel, ne l’incite à le faire.

Toutefois, le mécanisme de destruction créatrice de valeur sera favorable à l’emploi qualifié découlant de l’innovation.

En conclusion, l’incitation à innover, comme l’efficacité productive peuvent être améliorées du fait de l’existence d’un champion national, à condition qu’un certain degré de concurrence existe sur le marché. Mais, en définitive, tout dépend de la taille des marchés.

Les politiques industrielles et de concurrence vont donc, complémentairement, dans le sens d’une plus grande efficacité et d’une plus grande compétitivité de l’économie.

2.3. La complémentarité des politiques industrielle et de concurrence


Or, rien ne démontre le caractère systématique des effets sur la localisation des activités des changements de contrôles d’entreprises et rien ne démontre que, si de tels effets existent, ces derniers sont dus au fait que l’investisseur en cause est étranger. Les entreprises étrangères sont, il est vrai « moins sensibles aux pressions des syndicats, des médias, des politiques, voire des États » mais il n’empêche que les éventuelles suppressions d’emplois qu’elles opèrent peuvent simplement être rationnelles économiquement. Dans le contexte d’une économie mondialisée, le choix stratégique de la localisation de la production dépend en grande partie de la qualification des employés. L’Union européenne doit faire face à une concurrence croissante, notamment de la part des pays émergents. Les évolutions en cours portent en elles un risque de désindustrialisation de l’Europe, caractérisée aujourd’hui par la délocalisation d’un nombre non négligeable de centres de productions vers les pays tiers.

12 Fermetures de sites en France lors de l’acquisition de Pechiney par Alcan
13 Augustin Landier et David Thesmar « Quel patriotismé économique au XXIe siècle ? » in Problèmes économiques de la Documentation française du 5 juillet 2006 (n°2.903), p.29
62. Par ailleurs politique industrielle et politique de concurrence ne sont pas contradictoires : en ce qu’elle vise une compétitivité accrue et une situation économique saine, elles sont au contraire complémentaires à long terme. Des interventions au titre de la politique industrielle ne peuvent trouver un sens et une efficacité durables que si les entreprises touchées par ces interventions sont soumises à une concurrence réelle dans le contexte d’un commerce international sain et loyal.

63. De plus, la politique de concurrence n’est pas en contradiction avec les politiques industrielles mises en œuvre au plan national et/ou européen. Elle n’interdit pas la construction de champions industriels. Elle pourrait seulement entraîner l’interdiction de concentrations portant une atteinte irrémédiable à la concurrence.

64. Mario Monti, alors commissaire européen chargé de la concurrence, a déclaré, lors d’auditions de la Commission des affaires économiques du sénat, le 8 juin 2004, que non seulement les règles européennes de la concurrence n’entraient pas l’émergence de champions industriels, mais qu’au contraire, elles la facilitaient, en raison, d’une part, de la taille du marché européen et, d’autre part, du «guichet unique» et de l’unité des règles de la concurrence au niveau communautaire. Il a rappelé que, dans le domaine du contrôle des concentrations, très peu d’opérations donnaient lieu à un refus, ce qui permettait la création de grands groupes, compétitifs au niveau mondial.

65. Le rapport « Une stratégie européenne pour la mondialisation » de la mission L’Europe dans la mondialisation présidée par Laurent Cohen-Tanugi et rendu public en avril 2008, en vue de la présidence française du Conseil de l’Union européenne, indique ainsi que la Commission « n’a fait obstacle qu’à une trentaine de fusions ou acquisitions européennes au cours des vingt dernières années (sur plus de 3 000 notifiées), permettant (...) la constitution de très nombreux «champions» européens et nationaux ».

66. La concurrence peut donc aller dans le sens d’une politique industrielle efficace. L’ouverture à la concurrence dans les télécoms a par ailleurs provoqué l’émergence de champions européens comme, Ericsson ou Siemens par exemple. Ainsi « La politique de concurrence ne peut être conçue au service de la seule défense de la concurrence mais plutôt comme un moyen parvenir à l’efficacité économique ».

67. Enfin, une prise en compte des objectifs de politique industrielle n’implique pas nécessairement un abaissement des objectifs et des moyens de la politique de concurrence, contrairement à ce que pensent certains économistes qui affirment que la notion de champion industriel est en totale contradiction avec le critère d’atomicité du modèle de la concurrence pure et parfaite. Ainsi, toute économie a besoin d’opérateurs pour entrer en concurrence avec d’autres économies. De plus, il est nécessaire que les opérateurs acquièrent une taille leur permettant de survivre, de construire et d’innover sur des marchés de plus en plus vastes géographiquement.

68. La Commission prend cela en compte lorsqu’elle évalue l’impact des fusions, acquisitions ou abus de position dominante qui lui sont soumis. Elle s’appuie ainsi sur une définition de marchés pertinents « qui intègre leur dimension géographique et leur mondialisation accrue ».

69. Par ailleurs, David Encaoua et Roger Guesnerie dans leur rapport « Politiques de concurrences » diront non seulement que « la concurrence n’est qu’un des facteurs de l’innovation et du progrès

technique » mais aussi ceci : « notre conviction est claire : la concurrence est une condition nécessaire mais non suffisante pour que l’Union européenne retrouve le chemin de la croissance et de la compétitivité ».

70. En conclusion, politique de la concurrence et politique industrielle visent un même objectif d’efficacité économique, de compétitivité, et doivent être édictées et mises en œuvre de manière complémentaire et coordonnée.

71. Le rapport « Politiques de concurrences » préconise à ce titre un renforcement de la coopération entre la DG Concurrence, la DG Entreprise et Industrie et la DG Recherche, notamment pour l’évaluation des opérations de concentration comportant des enjeux marqués de compétitivité industrielle.

72. Le nouvel article L 430-7-1 II du Code de commerce en France permet la prise en compte de ces enjeux en introduisant la possibilité pour le Ministre de l’économie de prendre en compte des critères de politique industrielle en matière de concentration. L’Autorité de la concurrence sera quant à elle en charge d’une évaluation strictement concurrentielle.

2.4. La prise en compte de la concurrence internationale dans les politiques communautaires internes

73. La politique de la concurrence et la politique industrielle poursuivent, a priori, un objectif commun à savoir, (i) accroître l’efficacité des entreprises et (ii) mieux les préparer à la concurrence domestique et internationale. La base légale au niveau communautaire pour la politique de concurrence est déterminée par les articles 81 à 87 du Traité, celle pour la politique industrielle l’est à l’article 157 qui précise que toutes les politiques doivent contribuer aux objectifs de la politique industrielle mais aussi que « le présent titre ne constitue pas une base pour l’introduction ...de mesures pouvant entraîner des distorsions de concurrence. » Sur un plan pratique, on l’a vu, ces deux approches peuvent être source de divergence voire de conflit.

2.4.1. Des interventions publiques pour favoriser l’émergence d’entreprises innovantes

74. Encourager les entreprises à augmenter leurs dépenses de R&D et d’innovation ne doit pas conduire, naturellement, à perturber le fonctionnement normal du marché et de la concurrence. Les interventions publiques visent à pallier les défaillances du marché, et ce en conformité avec les règles communautaires en matière d’aides d’État. Certains projets de R&D et d’innovation, en effet, ne se réalisent pas pour des raisons diverses :

- manque de moyens propres des PME innovantes et difficulté d’en obtenir sur le marché bancaire ou à des conditions trop pénalisantes ;
- pas d’inclinaison naturelle des entreprises à la coopération avec d’autres, alors même qu’une thématique de recherche n’est envisageable qu’en partenariat ;
- coûts et risques trop importants de certains projets, alors même que les bénéfices sociétaux qui pourraient en découler sont importants.

75. Les pouvoirs publics, ont, face à ces raisons diverses, développé au fil du temps des approches complémentaires pour répondre aux besoins différents des acteurs économiques. Ces interventions ont été

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17 Rapport du Conseil d’Analyse économique, 2006 (n°60) La Documentation française, p.109
18 Idem
19 Rapport du Conseil d’Analyse économique, 2006 (n°60) La Documentation française, p.109
autorisées par la Commission européenne, qui a constaté leur bien-fondé et l’absence d’effets néfastes sur la concurrence intra communautaire.

76. Le contrôle communautaire des aides à la R&D et à l’innovation vise à prévenir les effets négatifs d’une aide sur les entreprises concurrentes des États membres. Cette logique, légitime au regard des objectifs de renforcement du marché intérieur, n’est toutefois pas toujours satisfaisante : la définition restrictive d’activités de recherche éligibles aux aides, la fixation d’intensités maximales, la mise en place d’une procédure longue et lourde d’instruction des projets les plus importants au niveau communautaire, après une instruction longue au niveau national, sont des contraintes qui n’existent qu’au sein de l’Union européenne. **Or la concurrence en matière de recherche se joue au plan mondial.**

77. Il semble fondamental aujourd’hui de s’interroger sur l’impact de ces contraintes, de ce contrôle en matière d’aides à la R&D et à l’innovation sur la compétitivité des entreprises européennes, dans un contexte de concurrence ouverte et mondiale.

78. Il ne s’agit pas de s’affranchir du contrôle communautaire des aides, qui est l’une des bases de la construction du marché intérieur. Il s’agit de réaffirmer que le fondement du contrôle des aides est la construction et le renforcement du marché intérieur dans un contexte international évolué. En ce sens, ceci rejoint l’approche souhaitée par la Commission elle-même dans son plan d’action 2005-2009 adopté le 15 juillet 2005 : « La politique des aides d’État (…) doit contribuer, par elle-même et aussi en venant appuyer d’autres politiques, à faire de l’Europe un lieu plus attractif pour les investissements et l’emploi, à renforcer les connaissances et l’innovation pour susciter de la croissance et à créer des emplois plus nombreux et meilleurs. »

79. Renforcer les politiques de soutien à la R&D et à l’innovation passe par une meilleure prise en compte de la concurrence internationale dans les politiques communautaires internes. L’émergence de champions européens passe aussi par le développement de projets dits à risque que le marché ne semble parfois pas à même de vouloir financer.

80. L’examen de l’intérêt stratégique des projets et non de la seule défaillance de marché et de l’impact sur la concurrence devrait devenir un élément de la politique de concurrence si l’Europe veut voir émerger davantage de champions européens. Ceci est d’ailleurs la règle aux États-Unis et au Japon.

### 2.5. L’introduction de critères de politique industrielle dans la mise en œuvre du droit de la concurrence : un exemple français récent

81. La récente réforme de l’organisation du système français du contrôle des concentrations prévoit que des impératifs de politique industrielle ne peuvent pas être pris en compte par l’autorité de la concurrence, qui pourra toutefois, si il y a lieu, intégrer les gains d’efficacité économique compensant les atteintes à la concurrence évalués dans le cadre de l’examen de projets de concentrations (cf. point 2.3 ci-dessus). Ces impératifs de politique industrielle pourront, en revanche, être pris en compte de manière plus large par le Ministre de l’économie à l’issue de la procédure.

82. En effet, la loi de modernisation de l’économie du 4 août 2008 a réformé la régulation concurrentielle des marchés en France, notamment en ce qui concerne les règles relatives au traitement des affaires de concentration. L’Autorité de la concurrence traitera ces opérations sous l’angle concurrentiel.

83. Pour sa part, le Ministre de l’économie conservera un pouvoir d’évocation en fin de phase II. Ainsi l’article L430-7-1 II du Code de commerce indique que « le ministre chargé de l’économie peut évoquer l’affaire et statuer sur l’opération en cause pour des motifs d’intérêt général autres que le maintien de la concurrence et, le cas échéant, compensant l’atteinte portée à cette dernière par l’opération ». 

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84. L’article continue en indiquant que : « Les motifs d’intérêt général autres que le maintien de la concurrence pouvant conduire le ministre chargé de l’économie à évoquer l’affaire sont, notamment, le développement industriel, la compétitivité des entreprises en cause au regard de la concurrence internationale ou la création ou le maintien de l’emploi ».

85. L’octroi de ce pouvoir d’évocation se justifie par la nécessité de permettre un bilan global des opérations de concentration jugées stratégiques et pour lesquelles les autorités considèrent comme indispensable de pouvoir continuer à concilier les impératifs de la régulation de la concurrence avec ceux d’autres politiques publiques. S’il décide d’évoquer une décision de l’Autorité de la concurrence, le Ministre devra prendre une décision motivée, éventuellement conditionnée à la mise en œuvre effective d’engagements (article L 430-7-1, II alinéa 3 du Code de commerce).

86. Par ailleurs, le Ministre disposera d’une large marge de manœuvre, en ce qu’il pourra non seulement passer outre une décision d’interdiction, mais également mettre son veto à la réalisation d’une opération autorisée par l’Autorité de la concurrence.

87. Des procédures similaires existent dans d’autres États européens :

- l’article 42 de la loi antitrust en Allemagne prévoit la possibilité pour le Gouvernement fédéral d’autoriser une fusion interdite par l’autorité de concurrence (mais non l’inverse) ; depuis l’instauration de ce système en 1973, et sur les quelques 170 cas d’interdiction prononcés par le Bundeskartellamt, le Gouvernement allemand a autorisé l’opération à 11 reprises ;
- au Royaume Uni, l’Enterprise Act, entré en vigueur en juin 2003, prévoit la possibilité pour le Gouvernement de saisir la Competition Commission afin d’engager une procédure d’examen approfondi des opérations de concentration mettant en jeu un intérêt public spécifique (pluralité des médias, approvisionnement dans le domaine de l’eau, défense) ; le Gouvernement peut ainsi interdire une concentration autorisée par les autorités de concurrence.

88. Cela permet une prise en compte des spécificités sectorielles lors de l’analyse des politiques de concurrence, que le rapport « Politiques de concurrences »²⁰ considère comme nécessaire.

89. Cela conduit en effet à une plus grande compétitivité et à une plus grande efficacité globale. En ce sens, politique de concurrence et politique industrielle sont tout à fait complémentaires.

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²⁰ Rapport du Conseil d’Analyse économique, 2006 (n°60) La Documentation française, p.109
CONTRIBUTION BY GERMANY
COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL CHAMPIONS

--Germany--

1. Introduction

1. This contribution focuses on the relationship between industrial policy, including the issue of national champions, and competition law in Germany.

2. Economic policy thinking in post-war Germany has been strongly influenced by the so-called Freiburger Schule or ordoliberalism. Ordoliberalism is a German variation of neoliberalism, which stresses the importance of economic freedom, competition as a market organising principle and the role of government in protecting competition without interfering with the market forces, wherever possible.\(^1\)

3. The Bundeskartellamt endorses this thinking. In its view, competition is the best means to innovate and produce better and cheaper goods and services. Or, to use Friedrich August von Hayek’s famous words: Competition is a “discovery process”. In this respect, firms are generally closer than the state to market developments and the opportunities the markets offer. This means that firms rather than the state are likely to discover the technological as well as the product and service developments worth pursuing. Consequently, the state should limit itself to guaranteeing the necessary regulatory framework and intervening only in cases of genuine market failures.\(^3\)

4. The principle to let market forces work freely and limit state intervention to a minimum is reflected in modern-day economic policy formulation in Germany. The German Federal Ministry of Economics and Technology, for instance, stresses this principle of non-interference under the rubric “Industrial Policy” on its website: “Entrepreneurial initiative, contractual freedom between business partners, competition and a functioning price system are the central pillars of a market economy. These essential market mechanisms must not be distorted by state interference.”\(^5\)

5. This position is reflected in the principle that the government does not interfere with mergers and acquisitions by either domestic or foreign-owned or foreign-based firms. The fundamental freedom enshrined in Article 56 of the Treaty establishing the European Community (EC) (free movement of

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\(^1\) See also Michael Glos (German Minister for Economics and Technology from 2005 to 2009), Schlaglichter der Wirtschaftspolitik, Sonderheft Finanzkrise, available in German at [http://www.bmwi.de/BMWi/Redaktion/PDF/S-T/sonderheft-finanzkrise.property=pdf.bereich=bmwisprache=de.rwb=true.pdf](http://www.bmwi.de/BMWi/Redaktion/PDF/S-T/sonderheft-finanzkrise.property=pdf.bereich=bmwisprache=de.rwb=true.pdf).


\(^4\) See the section on the present financial crisis below.


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capital) allows firms based in the European Union to invest in Germany. As for third countries, however, the German parliament is currently working on an amendment to the Foreign Trade Act (“Außenwirtschaftsgesetz”) based on a government proposal. The new amendment would allow the Ministry for Economics and Technology to investigate whether the acquisition of interests in “resident undertakings” amounting to at least 25% of the voting rights would endanger the “public policy or public security” of the Federal Republic of Germany.

2. Competition law, industrial policy and national champions

2.1. The Bundeskartellamt bases its decisions solely on competition aspects

6. German competition law strictly separates competition and non-competition aspects. The Bundeskartellamt (as well as the competition authorities of the German Länder) assesses and decides solely on competition grounds. The Bundeskartellamt must not and does not take any other aspects into account, including industrial policy aspects. The track record of the Bundeskartellamt underlines that it has not shied away from adopting decisions that conflicted with the agenda of industry leaders as well as politicians when there were competition concerns.

2.2. Institutional aspects – independence of the competition agency

7. Apart from the substantive law, the institutional setting of the Bundeskartellamt helps to ensure that it can focus exclusively on competition aspects. In that respect it is of the greatest importance that the relevant decision-making bodies within the Bundeskartellamt are independent of external influence when they deal with individual cases. This also means independence from the Government, in particular the Ministry of Economics and Technology. But the principle of independent decision-making goes even further: The decisions are taken in a decentralised manner by each of the Bundeskartellamt’s twelve decision divisions (by the chair and two members of the competent division in a majority vote); the President of the Bundeskartellamt may not give any instructions.

2.3. Section 42 ARC – Ministerial Authorisation

8. With respect to mergers, however, Section 42 of the German Act against Restraints of Competition (ARC) empowers the Minister for Economics and Technology the authority, in exceptional cases, to override a prohibition decision by the Bundeskartellamt on strictly non-competition grounds. More precisely, the provision allows the Minister “upon application, [to] authorise a concentration prohibited by the Bundeskartellamt if, in a specific case, the restraint of competition is outweighed by advantages to the economy as a whole following from the concentration, or if the concentration is justified

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8. Firms based in EFTA countries are considered to be community-based in the context of the proposed Section 53 of the Foreign Trade Act (“Außenwirtschaftsgesetz”).

9 The proposal is available at http://dip21.bundestag.de/dip21/btd/16/107/1610730.pdf (in German only).

10 In the view of the Bundeskartellamt this separation of objectives, i.e. the use of a purely competition-based standard by competition agencies, is highly preferable to a mixed standard that may allow non-competition objectives to be taken into account. In relation to the latter approach, see Evenett, The Return of Industrial Policy – A Threat to Competition Law, in: Competition Law Today (Dhall, ed.), 2006, p. 452-476, p. 472.


12 No such provision exists with respect to anticompetitive agreements and unilateral conduct.
by an overriding public interest.” The formulation of the provision already indicates what is common in practice, namely that a ministerial authorisation is difficult to obtain. In fact, since the introduction of merger control and the institute of the ministerial authorisation in 1973, parties to merger projects have only rarely applied for such an authorisation and have in even fewer cases done so successfully. There may be various reasons for this: The criteria laid down in Section 42 set a high standard, the Minister for Economics and Technology conducts a transparent procedure involving third parties, the German Monopolies Commission is heard on the matter, a decision is published and the parties to the procedure may appeal against the decision in court. Furthermore, German Economics Ministers so far have made it very clear by applying Section 42 cautiously that the ministerial authorisation of mergers that had previously been prohibited by the Bundeskartellamt due to competition concerns is only granted in exceptional cases.

9. Section 42 shows that, whereas the Minister may invoke broader political reasons for his decisions, the Bundeskartellamt in its analysis of merger projects is confined solely to competition aspects. This is, besides its institutional independence, another shield protecting the Bundeskartellamt from outside pressure. Furthermore, it may be argued that the instrument of ministerial authorisation strikes the balance between the strictly competition based analysis of the Bundeskartellamt, that leaves no room for discretion in merger cases, and – in rare cases – the overriding interests of the public that may nevertheless justify the merger.

Case example – E.ON/Ruhrgas

10. A recent example in which it was decided by ministerial authorisation that the serious competition concerns of the Bundeskartellamt – which had blocked the merger – were outweighed by overriding public interest, is the E.ON/Ruhrgas merger. This case concerned the energy sector, in particular the supply of gas. The Bundeskartellamt had found that the merger would strengthen dominant positions both in the gas and electricity sales markets. The Bundeskartellamt held that the merger would be problematic in particular with respect to the gas markets where the merger would lead to a cementation of Ruhrgas’ dominant position and would significantly diminish the likelihood of any effective competition from other grid gas companies. In the ministerial authorisation it was argued that the merger would strengthen the international competitiveness of Ruhrgas on the supply as well as the demand side. Furthermore, the merger would improve security of energy supply through the long-term supply of well-priced gas, in particular from Russia.

11. After the merger was consummated it became clear that competition in the energy sector remained unsatisfactory despite the liberalisation process in Germany.

12. To open the markets to competition, the Bundeskartellamt initiated proceedings based on Articles 81 and 82 EC to investigate E.ON/Ruhrgas’ practice of long-term gas supply contracts with its customers. A survey had shown that almost three-quarters of the contracts concerned cover 100% of the gas distributor’s requirement or at least quantities of between 80% and 100%. Almost all of these contracts ran for more than four years, in some cases up to twenty years. This combination of long contract periods and a high degree of requirement satisfaction leads to considerable foreclosure effects. In its decision in

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13 In the 22 cases in which parties to a merger have applied for a ministerial authorisation, the Minister has issued (at least partial) authorisation in five cases, some of them subject to obligations.


January 2006, the Bundeskartellamt prohibited E.ON Ruhrgas’ existing long-term contracts with distributors, which covered more than 80% of their actual gas requirements. These contracts were to be terminated at the latest by the end of the same gas year, on 30 September 2006.

2.4. Other political measures that are relevant to competition

There are of course other means that may have the effect of protecting “domestic” firms from competition by “foreign” firms: One example is the adoption of laws that raise barriers to entry for (potential) competitors of the incumbent firm. A recent illustration can be found in the postal services sector. Germany has formally opened up the market with the discontinuation, from January 2008, of the last exclusivity rights of the incumbent Deutsche Post. However, Deutsche Post still enjoys considerable advantages such as the exemption from value added tax obligations. Further to this, a rather high minimum wage was introduced for the postal sector in 2007 that has rendered the offer of postal services in competition with the incumbent Deutsche Post uneconomic for many newer competitors in the market. In the view of the Bundeskartellamt the measure is effectively a barrier to market entry for new competitors that may undermine the full legal market opening that took effect at the beginning of 2008.

3. Measures adopted in the recent economic crisis

3.1. The Financial Market Stabilisation Act

The last months have been characterised by a severe crisis in the financial markets with implications extending to the real economy. To address the extraordinarily difficult situation and restore confidence in the financial markets, the German parliament has enacted the Financial Market Stabilisation Act that came into effect in October 2008. The Act comprises a package of measures aimed at stabilising the financial markets. The primary objectives of the act are (i) to secure the liquidity of financial institutions that have their seat in Germany and (ii) to prevent a general credit crunch. The concern was that systemically indispensable banks could fail with consequences which were unpredictable for the wider economy in Germany and beyond. The core of the package is a rescue fund which may (inter alia and under certain conditions) acquire (or otherwise secure) loans, securities, derivative financial instruments and other risk positions, acquire equity in the recapitalisation process and thus strengthen the core capital ratio of the undertakings or also acquire a participation, in particular, shares in firms.

According to Article 2 Section 17 of the Act, Parts I-III of the German Act against Restraints of Competition are not applicable. This means that the acquisition of interests by the fund in financial institutions is not subject to German merger control law. This does not imply, however, that the

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17 The German Monopolies Commission has criticized this step in a special opinion entitled “Monopoly fight with all means, see press release (in German only) available at http://www.monopolkommission.de/sg_51/presse_s51.pdf. A leading competition lawyer, Prof. Wernhard Möschel, argued in an expertise for a hearing before the German parliament’s Committee on Economics and Technology on 19 January 2009 that the minimum wage (based on the in-house wage scale of the Deutsche Post) deprives (potential) competitors of the most important competitive instrument. Prof. Möschel concludes that the decision to declare the collective agreement between Deutsche Post and the labour union ver.di as binding for the whole sector is in violation of the German constitution, German and European competition law (as an anticompetitive agreement, Article 81 EC and Section 1 ARC), and also in violation of the freedom of establishment, Article 43 EC.
acquisition of these interests from the fund by third parties in the future would also escape merger control law.

3.2. Specific measures taken on the basis of the Stabilisation Act

16. The Stabilisation Act is of great importance to rescue financial institutions that are vital for the financial market to function (“systemic banks”). However, such extraordinary measures are fraught with the problem of distinguishing between genuine rescue situations and cases where this instrument may be used to pursue other objectives. This question has been raised in the press with respect to the merger case of Commerzbank and Dresdner Bank\(^\text{19}\). In this case, it has been argued that the objective of granting aid from the rescue fund has been to support the envisaged concentrations between the respective parties rather than to rescue a bank in serious financial turmoil. Whatever the merit of the criticism, it highlights the problem that with a powerful instrument like a rescue fund, the state is likely to be lobbied to intervene for all kinds of special interests.

17. Such intervention would run counter to ordoliberal traditions where the state was supposed to leave the market forces to work independently where possible\(^\text{20}\). Industrial policy measures bear the risk of the state taking wrong decisions that have to be paid for by taxpayers. Furthermore, competition may be seriously distorted. State intervention should therefore, as mentioned before, be restricted to the minimum necessary.

18. It is feared that the financial crisis may extend to other sectors and affect the real economy. Parliament has therefore adopted a broader investment and stimulus package to bolster the economy. As far as the implementation of the measures is concerned, the government will have to ensure that they will not lead to significant market distortion, to the detriment of those competitors that do not benefit from the measures adopted\(^\text{21}\). Furthermore, the state measures should not provide an incentive for firms to take money from the state although the aid is not needed to gain a competitive advantage over their competitors. The issue of aid by the state may finally run counter to the objective of creating a level playing field for firms in different countries\(^\text{22}\).

4. Conclusion

19. The Bundeskartellamt takes a critical view of state intervention that goes beyond setting a regulatory framework for markets to function. Generally, developments within the markets and developments which open up new markets should be left to firms, not the state, since these will normally have a much better insight into how markets function than the state. Thus, it should be left to firms and competition to identify key sectors, technologies as well as goods and services that merit investment and development. Or, as the former Chairman of the United Kingdom’s Competition Commission, Prof. Paul Geroski, put it: “[T]he kind of ‘competitiveness’ which competition policy actually strives to create is
virtually the only way a nation state can achieve the kind of “competitiveness” which industrial policy proponents aspire to.\textsuperscript{23}

20. If market intervention is in fact necessary, for instance in these difficult times of financial crisis and spill-over to the real economy, governments setting up rescue funds and granting state aid to firms in trouble should limit themselves to rescuing or supporting firms that are crucial for the functioning of the system. Any other measure may only lead to high costs for the tax payer and seriously distort competition in the markets concerned.

CONTRIBUTION BY JAPAN
COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL CHAMPIONS
--Japan--

1. Introduction

1. Today, the importance of competition policies has been widely acknowledged throughout the world and the pursuit of fair and free competition is regarded to contribute to the promotion of trade and investment, the maintenance of sustainable economic growth by enhancing economic efficiency and productivity and the further achievement of national and consumer welfare. Viewed from a historical perspective, however, a culture of competition was not widespread among the general public in Japan from the beginning, even though the Japanese economy had long been based on a market economy. This is suggested by the fact that government policies that inclined to draw a picture of a desirable industrial structure and encourage harmonious cooperation among entrepreneurs received general support even after the Antimonopoly Act (“AMA”) was enacted as a part of post-World War II economic democratisation policy.

2. This contribution paper introduces how the relationship between industrial policy and competition policy has changed through the process of increasing understanding of competition policy up to today.

2. Experience of Japanese competition law and policy


3. In 1947, the AMA, the Japanese competition law, was enacted and the Japan Fair Trade Commission (JFTC) was established as an independent commission.

4. After World War II, as part of the democratisation of the Japanese economy, the AMA was introduced for the purpose of establishing a competitive economic system based on a market economy. It aimed to maintain a permanently competitive market through structural measures, such as the dissolution of giant conglomerates known as the Saibatsu, the elimination of the concentration of economic power and the removal of private controlling groups. The competition law and policy in Japan was introduced drastically and at the same time. While some assess that the resulting competitive market structure of the Japanese economy through this effort made a great contribution to the development of the Japanese economy overall, the concept of competition policy and economic development through competition did not take root rapidly.

2.2. “Dark Ages of the Antimonopoly Act” (1950s)

5. The immediate challenge for Japan after the departure of the occupying forces was to achieve economic independence. Government policy, therefore, focused on fostering and strengthening domestic industries to earn foreign exchange through exports. This led to the enactment of various laws exempting a wide range of industries from the AMA, mainly with the objective of easing cartel regulations. In addition, administrative guidance, which might harm competition and was incompatible with competition policy, was implemented in many industries during periods of recession with a view to preventing excessive competition or stabilising the market. Thus, from the viewpoint of both the legal systems and the legal institutions, competition policy was restricted and forced to step back.
2.3. **Approach to large-scale mergers and acquisitions (1960s)**

6. The deregulation of trade, foreign exchange and capital was strongly promoted in the Japanese economy during this period. At this time the Japanese economy was considered to be more closely connected with global markets through these deregulations and competition among entrepreneurs in the Japanese economy was taken as having an international scale. However, in order to strengthen the management base of enterprises, industrial policies that intensively facilitated the concentration of capital gathered more support based on the so-called “theory of excessive competition”; that is, the idea that the characteristics of Japanese entrepreneurs, which are comparatively too small in size, was thought to lead to excessive competition.

7. For example, a bill of the Law for Temporary Measures to Promote Specified Industries, which aimed to promote industrial reorganisation, was submitted to the Diet in March 1963. In this law, the government, in cooperation with the private sector, was to designate particular industries for reorganisation such as automobiles, special steels and petrochemicals, which needed to strengthen their international competitiveness, and set up policies regarding capital investments, mergers and the rationalisation of cartels of enterprises. Although the bill did not necessarily garner any positive support from political and industrial circles and was withdrawn in the Diet, an increase in large-scale mergers of enterprises followed in key industrial fields.

8. One typical large-scale merger during this period was a merger between two major steel companies, Yawata and Fuji (Consent Decision on 30 October, 1969). This merger would have greatly influenced the national economy because it was to be the largest post-war merger in Japan and steel products were significant basic materials for a variety of industries. Japan’s industrial community supported this merger as necessary for promoting industrial reorganisation under the open economy. However, it can be said that the merger was going to have a serious influence on competition because it would merge the 1st and the 2nd largest entrepreneurs in the key steel industry and the new entrepreneur’s market share would exceed 30 percent in more than 20 products. The JFTC considered that the merger would raise a lot of problems in terms of competition policy and its decision was viewed with great interest. Although the JFTC accepted the merger proposal in the end, with delivering a consent order demanding various remedies, discussions on the role of the AMA became more active, and it was made clear that approval for larger-scale mergers would not be easy to obtain. The merger of Yawata and Fuji marked a tuning point, and the existence of the AMA and the JFTC were strongly recognised in Japan’s industrial community from then on.

2.4. **Greater awareness of competition policy through elimination measures against anti-competitive activities that affect the whole national economy (1970s)**

9. During this period, the international monetary crisis and the oil crisis shocked the Japanese economy. Unusual inflation psychology followed the oil crisis in 1973, leading to skyrocketing prices. Many suppliers such as manufacturers rushed to form illegal cartels in order to raise prices in advance before their costs rose. The JFTC uncovered the illegal cartels one by one and rendered cease-and-desist orders. On 15 February 1974, the JFTC filed with the Public Prosecutor General criminal accusations against 11 oil wholesalers and their executives, who were involved in the price cartel case of oil products, based on the provision of Article 73, Paragraph 1 of the AMA, which was the first case of criminal accusation in a cartel after the AMA was enacted.

10. In addition, because administrative guidance was involved in this cartel case, the relationship between administrative guidance and cartels became an issue for debate. Concern about the relationship between administrative guidance and cartels became an issue for debate.
between administrative guidance and cartels had been discussed for many years, and the JFTC had consistently taken the position that cartels, even those concluded under administrative guidance, were violations of the AMA. The prosecution in this case and a guilty verdict at the Supreme Court marked a turning point of changing past practices to restrain competition by administrative guidance.

11. During the structural depression after the oil crises, the so-called Structurally Depressed Industry laws, that is, the Law on Temporary Measures for Stabilisation of Specified Depressed Industries (1978), the Law on Temporary Measures for the Structural Improvement of Specified Industries (1983) and the Law on Temporary Measures to Facilitate Industrial Structural Adjustment (1987) were drafted. In the process of the legislation of these acts, there was, at first, a strong tendency of requiring government intervention from the viewpoint of industrial policy, such as considering or implementing instructed cartels by the government and exemptions to the AMA. However, because of the JFTC’s actions and the influence of so-called “Positive Adjustment Policy” approved by the OECD, these laws ended up substantially taking into consideration competition policy, which is shown by the fact that the JFTC’s agreement was required even if cartels instructed by the relevant Ministers were allowed. In addition, in the later legislation of the above laws, in order to implement business alliances within the framework of the AMA, consideration of competition policy resulted in the development of a coordination scheme between the relevant minister and the JFTC regarding the relevant minister’s approval of the alliances; furthermore, cartels instructed by the relevant ministers were not allowed in the 1987 law.

2.5. Expansion of the scope of application of the competition law through deregulation and reduction in exemptions (1980-90s)

12. In the latter half of the 1980s, deregulation was promoted to open the Japanese market and boost imports in order to mitigate trade friction caused by Japan’s enormous trade surplus. Further in the 1990s, the yen’s appreciation led to calls for structural reform of the Japanese economy, as it revealed the price differential within and outside the country as well as concern for the hollowing-out of industry and employment uncertainty as it encouraged enterprises to shift overseas. In order to construct an economic society based on the principle of self-responsibility and market principles, the importance of strengthening competition policy as well as deregulating Japan’s economic and social systems was emphasised. Thus, the active development of competition policy proceeded in this period.

13. In 1995, the Cabinet adopted “The Deregulation Action Plan”, which included the active development of regulatory reform and competition policy. There have been several Cabinet Decisions concerning regulatory reform since then.

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2 On the occasion of the Tokyo High Court’s ruling in the cartel case of Petroleum Products, the JFTC published the “Interpretations Concerning the Relation between the Antimonopoly Act and Administrative Guidance” (the former Administrative Guidance Guidelines) in March 1981, which organised its view, centred on administrative guidance concerning prices and quantities. The JFTC sent the guidelines to the relevant ministries and agencies and requested them to consider them in their administrative management.
14. In order to clarify the guidelines under the AMA about ensuring the transparency of distribution and business practices, which was discussed in the Structural Impediments Initiative (SII) talks between Japan and the United States starting in 1989, the JFTC published “Guidelines Concerning Distribution Systems and Business Practices” (1991). In addition, the JFTC formulated and published “Guidelines Concerning the Activities of Firms and Trade Associations with Regard to Public Bids” (1994) and “Guidelines Concerning the Activities of Trade Associations under the Antimonopoly Act” (1995), which were intended to contribute to preventing firms and trade associations from violating the AMA and to help them in their pursuit of appropriate actions. Furthermore, the JFTC reviewed the former Administrative Guidance Guidelines in June 1994, and then formulated and published new “Guidelines Concerning Administrative Guidance under the Antimonopoly Act” (1994) that show the agency’s views on administrative guidance regarding the entry of firms and provide concrete examples indicating each category of administrative guidance that may pose a problem under the AMA.

15. The need for exemptions has changed significantly since the inception of the exemption system in accordance with the improvement of the economic environment as Japan gained global economic power and the financial conditions of Japanese companies strengthened. Therefore, reflecting several Cabinet Decisions since “the Revised Deregulation Action Plan” (in March 1996), the JFTC has reviewed exemptions to the AMA significantly. The number of exemptions was reduced from 89 systems under 30 laws, as of the end of FY 1995, to 21 systems under 15 laws as of the end of 2008.

2.6. Efforts for strengthening the enforcement power of the AMA (ongoing)

16. As is shown in the processes mentioned above, it may be no exaggeration to say that the importance of competition law and policy has become widely perceived to a considerable degree in Japan and competition law and policy has become firmly established in the Japanese economy. As a result, when considering a policy or measure applicable to any individual industry for example, the government now carefully considers how it will serve to improve competitive environments or promote competition in the relevant market. Also firmly established is the realisation that for the further development of our economy, it is indispensable for entrepreneurs in many industries not only to improve technology and productivity in the face of stiff international competition but also to compete actively in domestic markets.

17. On the other hand, in the face of Japan’s ever-changing economic realities, the JFTC is continuously reviewing the AMA and competition policy in order to make them more effective for maintaining and promoting fair and free competition in consideration of whether the legal system of the AMA is designed to function sufficiently or is comparable to that of the level of international standards.

a) Enhancement of law enforcement functions through the amendment of the AMA

In order to strengthen the measures against antimonopoly violations, a comprehensive amendment of the AMA, which was the largest since 1977, including (a) an increase of the surcharge rate, (b) introduction of a leniency program, (c) introduction of criminal investigative power and (d) revision of the hearing procedures, was approved by the Diet in April 2005 and came into effect in January 2006.

In compliance with the provisions contained in Article 13 in the Supplementary Provisions of the amended AMA of 2005, the Act’s amendment bill, including (a) the introduction of a surcharge system imposed on those entrepreneurs engaging in exclusionary type private monopolisation, unfair trade practices, etc., (b) the review of the surcharge rate imposed on entrepreneurs that have been playing a leading role in cartel, bid-riggings, etc., (c) the introduction of a joint application system for the leniency program by those entrepreneurs affiliated with each other and implicated in the same infringement and (d) the revision of the notification system regarding
business combinations, was approved at the Cabinet meeting held on March 11, 2008, and was submitted to the 169th ordinary session of the Diet on the same day³.

b) Efforts for regulatory reforms

To realise sustained economic growth led by private-sector demand, it is a pressing task to push ahead with the structural reform of our economy through regulatory reform. By means of structural reform, we are expected to build a socioeconomic system that is open to the world and permits the private sector to fully utilise its initiative and vitality acting on the principles of self-responsibility and the market mechanism.

In such circumstances, the Japanese government places the revitalisation of the economy based on regulatory reform as the top priority, and has been promoting regulatory reform since the mid-1990s. Most recently, reform has been promoted in accordance with the Three-Year Plan for the Promotion of Regulatory Reform (Cabinet Decision of June 2007, revised in March 2008).

The JFTC actively participates in formulating programs designed to promote such regulatory reform, makes necessary recommendations for improving individual government regulations and makes efforts for a clearer application of competition laws through the formulation of guidelines. As part of such efforts, since 2000 the JFTC has conducted studies, presented recommendations and formulated guidelines on some 35 regulatory reforms in total.

c) Improvement of corporate compliance

There are increasing movements toward requiring improved corporate compliance, such as through the amendment of the AMA, the creation of a system of whistleblower protection and rulemaking for internal control under the Companies Act and the Financial Instruments and Exchange Act. Because improvement of corporate compliance is important for advancing fair competition in the economy and trade, the JFTC promotes support for improvement of compliance as a key policy designed to enhance compliance under the AMA, and conducts a questionnaire survey on corporate compliance and publishes reports. In 2007, for instance, the JFTC developed a questionnaire survey for foreign-owned companies operating in Japan and summarised the data and situation of their compliance in Japan. At the same time, the JFTC developed a similar survey among domestic companies and examined how foreign-owned companies differ from domestic companies in their compliance. The JFTC also surveyed lawyers, asking how companies changed in their awareness of compliance in response to the required improvement of corporate compliance following enforcement of the amended AMA. The JFTC analysed the results obtained in all these surveys and published “Compliance by foreign-owned companies and compliance by foreign-owned and domestic companies as viewed by lawyers - with a focus on the Antimonopoly Act.” (Published in May 2008)

3. Conclusion

18. Implemented as part of the policy designed to democratise Japan’s post-war economy, the AMA has since made steady progress, struggling through war-derived devastation and turmoil, rapid economic growth, oil crises, collapse of the bubble economy, etc. At times, the process was a rocky road as the AMA was subjected to relaxed revisions on some occasions and insufficient recognition among the general public on others. Little by little the AMA has struck root in our economic society and is now widely recognised.

³The bill was withdrawn at the end of the 170th Diet in December 2008.
19. One of the reasons why it took such a long time to gain understanding of competition law and policy is that there was a recognition that government policy that had been inclined to protect and foster domestic industries had contributed to the high growth of the Japanese economy, which is now the second-largest in the world. However, during the period of Japan’s rapid economic recovery and growth following World War II, fierce competition continued in many industries among entrepreneurs with many new market entries. Therefore, the policy of growing so-called National Champions has never functioned as the core of industrial policy in Japan. We should also take note of the fact that the AMA as a comprehensive competition law has consistently existed and the JFTC has continued enforcing the AMA since 1947 until today. While regulations to protect specific industries or entrepreneurs through industrial policy may temporarily bring about a certain level of growth and contribute to maintaining the economy, it is recognised that on a long-term basis, as the creative initiatives of entrepreneurs do not function sufficiently and diverse resources are not utilised efficiently, economic structural reform does not occur smoothly and autonomously, and continuous economic growth can be hindered.

20. From around the 1970s, a competition policy perspective began to be considered in implementing industrial policy oriented government intervention. In and after the 1980s, the government worked more actively on implementing competition policies in accordance with deregulations amid the growing recognition of the necessity for structural reform. Today, the importance of improving competitive environments and promoting competition in the market is widely recognised. As a result, for instance, the JFTC and relevant ministries are in close contact and coordinate with each other in such a manner that policies to be determined under relevant business laws of specific industries are drawn up and implemented in a manner consistent with the policies worked out under the AMA.
THE RELATIONSHIP BETWEEN COMPETITION POLICY AND INDUSTRIAL POLICY

--Korea--

1. Introduction

1. During the 1960s and 1970s, Korea enjoyed a phenomenal economic growth by employing a strategy that aims to nurture certain industries through financial support and protection like tax incentives and safeguard measures. However, during the same period, problems like monopolistic market structure and market distortion were created, which undermined the Korean economy’s fundamentals. Today, departing from a government-oriented growth strategy through support and protection, Korea has adopted a market-oriented growth strategy in which promotion of competition, regulatory reform lead to technological innovation and enhanced productivity.

2. This paper will first study Korea’s past industrial policies, then explore the conflicts between industrial policy and competition policy and seek possible viable solutions. This is an issue on which much discussion is recently taking place in Korea.

2. Thoughts on Korea’s industrial policies of the past

2.1. 1960s - 1970s: To nurture strategic industries through selection and concentration

3. With the first 5-year economic development plan launched in 1962, Korea went about economic development in earnest. At that time, the development strategy was “government-driven export-oriented industrialisation” aiming to overcome unfavourable conditions of small domestic markets and lack of natural resources and thereby to find new growth momentum in exports.

4. In order to develop heavy and chemical industry, the Korean government employed mainly indirect subsidy programs like the provision of low-interest loans, tax breaks and safeguard measures to protect local industry. At the same time, with monopolistic market structure worsening, it enacted the “Price Stabilisation Act,” to control prices.

5. Into the 1970s, a high growth of an average of 9.6% continued. However, protectionism and excessive regulations in the form of over-investment in heavy and chemical industry and price controls caused multiple adverse effects, like worsened monopolistic market structure and inefficient resource allocation.

2.2. 1980s: to shift to a system that promotes self-compliance and competition

6. Going through the second oil shock, the Korean government had a rude awakening over the government-driven economic management system, perceiving the limitation of government intervention. Hence, under the principles of “self-compliance, competition and market opening,” Korea embarked upon transforming its economic management style into a market-oriented one.

7. To that end, the Korean government reduced government financial assistance on a large scale, abolished individual laws for industrial development and significantly eased safeguard measures by removing the import prohibition list. Besides, with the view of overhauling the industrial assistance system and carrying out industrial rationalisation effectively, the government introduced the Industrial Development Act. The law confined the role of the government to a “trouble shooter,” limiting government intervention only to the case in which market fails to function properly, for example, restructuring of sunset industries. As a result, the 1980s saw regulations on manufacturing industry largely scaled back and market disciplines greatly increased.
8. In the 1990s, Korea proceeded with deregulation in the service sector including finance, telecommunications and transportation in full swing. The purpose of deregulation was to eliminate barriers to entry into the industries and to make it clear when the government should intervene and when it shouldn’t, so as to change the framework of the role of the government. Plus, Korea’s entry to the WTO in 1995 paved the way for removing trade barriers like tariffs and quantity controls to a level of advanced countries.

9. Into the 2000s, the policy paradigm of greater market disciplines and market opening was consistently maintained and evolved. Sweeping restructuring of corporate sector and financial industry was carried out, which aimed in the short term, to remove factors that might make the sector and the industry unhealthy and in the long term, to raise transparency, efficiency and fairness of the economy and thereby to strengthen competitiveness through market disciplines.

3. Recent development of industrial policy and competition policy of Korea

10. Currently, Korea’s industrial policy takes very measured approaches. The Industrial Development Act as the framework law governing the national industrial policy does not contain major policy tools to nurture national champions, such as sector-specific subsidies, entry restriction, easier access to credit and exemption from antitrust law. The Act, instead, presents long-term-based workforce training assistance, R&D investment in basic science and technology and institutional innovation as primary tools of industrial policy.

11. The Monopoly Regulation and Fair Trade Act (the MRFTA), Korea’s competition law, currently applies to all industrial sectors without exception. Exemption from antitrust law is granted only to legitimate exercise of intellectual property rights pursuant to the relevant law or conduct deemed reasonable under other laws and regulations.

12. Therefore, it is fair to say that since the 1980s, Korea has not adopted a national champion promoting strategy and so its leading exporters in shipbuilding, automobiles, and electronics sectors have gotten on their feet without government assistance to survive fierce competition at home and abroad and become the world’s leaders. Yet, some regulated industries like finance, telecommunications and energy are keeping anti-competitive regulations for the sake of protecting users’ interest and ensuring universal access.

13. In recent years, Korea’s competition authority often has conflicted with regulatory authorities mainly for the following two issues. First, undertakings’ conduct involving administrative guidance frequently used by regulatory authorities to achieve the purpose of industrial policy like industrial vitalisation and the securing of public interest, often infringes competition law. Second, regulatory authorities’ entry restriction or price controls to protect related industry and companies often go against competition advocacy efforts. Accordingly, the Korea Fair Trade Commission is responding to the first issue by establishing principles with which to enforce its law while for the second issue, consulting with the relevant regulatory authorities to improve anti-competitive regulations under their jurisdiction.

(1) Antitrust infringements involving regulatory authorities’ administrative guidance.

In case undertakings’ conduct induced by administrative guidance of government agencies in charge of industrial policy is in violation of competition law, the issue comes down to the matter

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1 The term “administrative guidance” means any administrative action for an administrative agency to guide a specific person in performing or failing to perform any certain act or to recommend or advise him/her to do so or not to do so in order to accomplish administrative purposes within the scope of affairs falling under its jurisdiction.
of whether the conduct can be exempted from application of the MRTFA, deemed as legitimate act pursuant to the relevant law or can be considered legal under the MRFTA. This issue has mainly been relevant in cartel cases.

Guidelines for Review of Cartels involving Administrative Guidance

The KFTC established a set of conditions and allowed administrative guidance to be exempted from antitrust law only when those conditions are met. First, the relevant laws should stipulate detailed conditions under which collaboration between competitors is allowed. Second, the relevant laws should explicitly grant administrative agencies authority to issue administrative guidance regarding collaboration between competitors.

Meanwhile, where administrative guidance is involved, the case in which undertakings have made a mutual agreement based on the guidance constitutes a cartel activity, but the case when undertakings follow individually the guidance without the mutual agreement does not.

Two local phone companies’ cartel involving local call rates

In 2003, two local phone companies KT (market share at about 91% by number of subscribers) and Hanaro Telecom (market share at about 8%) made an agreement in an attempt to bridge the gap in the two’s call rates. Under the agreement, KT would maintain its existing call rates but if Hanaro Telecom adjusts its call rates, KT would give its market share in the local phone market by 1.2% on an annual average by 2007. At that time, the examinee KT argued that its conduct should be exempted from competition law, citing that it was inevitable according to administrative guidance of the Ministry of Information and Communication\(^2\), which tried to prevent the then ailing Hanaro Telecom from being driven out of the market.

The KFTC recognised the existence of the guidance, but concluded that there was no cause-effect relationship\(^3\) between the guidance and the cartel conduct and the guidance was a mere recommendation, thereby imposing a corrective order and 118.4 billion (about 9.1 billion dollars) in surcharge on KT and Hanaro Telecom.

(2) KFTC’s efforts to reform anti-competitive regulations.

Korea’s competition advocacy system

Pursuant to Article 63 of the MRFTA, the KFTC introduced and has had preliminary consultation on enactment and reinforcement of anti-competitive regulations. Under this system, where regulatory authorities wish to enact or amend laws and regulations that have anti-competitive provisions like the determining of price or transaction terms, restriction in market entry or business activities, or cartels, or to approve of or take actions regarding such anti-competitive laws and regulations, they are required to have consultation with the KFTC in advance or to inform the KFTC of such matters. Then the KFTC suggests recommendations to the relevant authorities, which in turn reflect them in their laws and regulations.

\(^2\) The Ministry was in charge of promoting and regulating the IT industry, and after governmental reorganisation, is currently named “Korea Communications Commission.”

\(^3\) Under the agreement, provisions other than the one related to call rate fixing were not put into practice, and the MIC did not take any action on the specific measures for compliance with the agreements or the part of the agreement which failed to be carried out.
Plus, when it comes to statutory amendment in Korea, all proposals should receive examination by the Regulatory Reform Committee, where the KFTC participates in as the government representative and is actively engaged in competition advocacy efforts. Particularly, from this year, the competition assessment among the Regulatory Impact Analysis items will be carried out solely by the KFTC. This shows that competition authority’s role is gradually increasing in the area of regulatory reform in Korea.

Accomplishments

As the awareness of and consensus on the preliminary consultation on anti-competitive regulations (Article 63 of the MRFTA) is growing within the government, the number of consultation since 2004 has noticeably increased. In addition, the percentage of accepted KFTC recommendations to the number of the submitted ones is more than 80%, and increasing.

The ongoing efforts to reform anti-competitive regulations launched in 1988 have been successful, with a notable feat in the late 1990s when the Omnibus Cartel Repeal Act enacted to abolish more than 20 cartels from 18 laws. In 2007, based on the survey of the demand side (or those regulated), the KFTC reviewed 52 regulations and agreed with the relevant authorities to improve 23 of them. Since last year, the KFTC has been focusing on anti-competitive regulations like entry and business activity restrictions in major 3 regulated industries that are finance (banks, securities, non-life insurance), broadcasting & telecommunications, and aviation & transportation. Besides, the KFTC is also making efforts to ferret out and improve anti-competitive ordinances and rules of local municipalities.

Cases demonstrating economic effect of regulatory reform

In theory, there is no doubt that regulatory reform boosts the economy and brings positive effects on various economic growth indicators. Here are Korea’s experiences of regulatory reform in the IT sector introduced.

Since 1990, in concerted efforts with the relevant authority, the KFTC has been spurring efforts to shift the telecommunication market to a competitive one through the easing of entry restriction and price controls. As a result, Korea’s telecommunication industry saw new entrants entering to the market one after another after the mid 1990s and the each service sector form a competitive environment, and in 1998, call rating system changed from approval-based to notification-based. As a result, the overall call rates gradually decreased, with distant call and international call rates both plummeting by more than 50%.

4. Conclusion

14. In hindsight, policy to protect local industry with measures like subsidies, exemption from competition law and entry restriction as seen in Korea seems to be an effective policy at a time when a country with little resources and small domestic market is in its early stage of industrialisation. However, as the economy gets bigger and more complex, a government-oriented strategy that promotes national champions may deepen monopolistic market structure, create inefficiencies and have other adverse side effects. After all, Korea’s change in policy paradigm to strengthen market economy in the 1980s amid the oil shocks turned out to be a major contributor to its substantive growth thereafter.

15. In the era of global competition, the key to success lies in creating an environment where companies can develop problem-solving capability themselves and so enhance their productivity. In this light, only policies that create such a pro-competitive microeconomic environment for companies will facilitate productivity growth and efficiency gains and ultimately sustainable economic development.
CONTRIBUTION BY LITHUANIA
1. Introduction

The main guidelines for the industrial policy of Lithuania are set out in the Long-term Economic Development Strategy of Lithuania until 2015. Its provisions favour the so-called horizontal industrial policy and clearly speak against the sectorial industrial policy. Such a view is based, firstly, on the doubt about the ability of the State to select the “right” activities and the optimal amount of support as regards positive externalities, and secondly, on the lack of comprehensive and reliable information as well as on the risk of retaliation from other countries as regards the pursuit of monopoly profits. It is not enough to take into account the market share of a sector or its growth rate. There is a lack of reliable information and methods to analyse costs and benefits of such a policy. The analysis of examples of other countries can also hardly provide any guidelines for the selection of State-supported sectors.

2. Priority is therefore given to the development of industrial and social infrastructure (energy, transport and telecommunications, education and science, culture, health care and environment) serving as basis for the effective functioning of the economy, as well as of knowledge-based and high-technology activities in all fields of the economy. The need for the sustainability of industrial development is also highlighted. It is however emphasised that those fields should not necessarily be subsidised or otherwise supported by the State.

2. History and Evaluation

2.1. To what extent does the industrial policy in your country target firms on the basis of their nationality (e.g., by granting state aids/subsidies to national firms only, or by controlling their ownership)? If so, how is nationality defined?

3. The Law on Enterprises and Facilities of Strategic Importance to National Security and Other Enterprises Important to Ensuring National Security specifies the enterprises and facilities which are of strategic importance to national security, which must belong to the State by the right of ownership and in which (and the conditions under which) a proportion of the capital may be held by the private national and foreign capital meeting the criteria of European and trans-Atlantic integration provided the power of decision is retained by the State. The latter are e.g., Lithuanian Railways, Lithuanian Radio and Television Centre, AB Kaunas Hydro Power Plant.

4. The Constitutional Law on the Implementation of Paragraph 3 of Article 47 of the Constitution of the Republic of Lithuania defines foreign subjects meeting the criteria of European and trans-Atlantic integration as foreign legal persons as well as other foreign organisations set up in:

- the EU Member states or states parties to the Europe (Association) Agreement concluded with the European Communities and their member states;
- Member states of the OECD, NATO and states parties to the EEA Agreement.

These criteria are also met by nationals and permanent residents of the said states, as well as permanent residents of the Republic of Lithuania who are not citizens of the Republic of Lithuania.
2.2. What economic conditions have been associated with government industrial policy and support for national champions in your nation and region? Has this changed over time as economic development advanced?

5. The peculiarity of the examples mentioned hereafter lays in the fact that those particular companies were established to supply the vast market of the Soviet Union, they operated under regulated economy conditions and were owned by the State for a long time. After Lithuania declared its independence, the companies had to adapt to a completely different situation, they were also fully or partially privatised. The intention of the State was to get the companies on their feet under the market economy conditions. This policy has now lost its ground, especially after Lithuania joined the EU.

2.3. Are there major success stories of industrial policy or national champions that are prominent in policy discussions? Are there any perceived major failures of industrial or national champion policies? How do you define “success” and “failure” in this context? Are successful national champion stories supported by best practice competition policy standards?

6. There have been no major success stories of industrial policy or national champions in Lithuania.

7. One example that could be presented as a failure is the State policy in respect of AB “Alytaus tekstile”. This company is now subject to bankruptcy proceedings, its debts amount to more than EUR 12 million.

8. The company was established in 1965, it was the biggest undertaking in Alytus (a city with 68 thousand inhabitants) and the biggest textile manufacturer in Lithuania. The company was not profitable since Lithuania declared its independence in 1990. In 1998, 47 percent of the company’s shares were sold to the Singaporean business concern “Tolaram group”. The investor committed to pay 13 million Litas (approx. EUR 3.8 million), to maintain 3500 jobs and to invest 240 million Litas (approx. EUR 70 million). The State kept 11.82 percent of the shares.

9. In 2002, the Competition Council did not approve the plans of the Ministry of Finance to prolong repayment of the loan (approx. EUR 3.4 million, provided in 1995) until 2009 and to lower the annual interest rate to 5 percent, presented along with the restructuring plan of AB “Alytaus tekstile”. The Competition Council concluded that the restructuring plan did not ensure restoration of long-term solvency and viability. Moreover, the investor “Tolaram group” had committed, signing the agreement to purchase the shares of the company, to invest money therefore the involvement of the State was deemed to be unnecessary.

10. However, “Tolaram Group” failed to fulfil its commitments: it paid 10 million Litas (approx. EUR 2.9 million), reduced the number of employees to 2648 and invested merely 10 million Litas (EUR 2.9 million). The volume of sales decreased from EUR 49 million in 1999 to EUR 37 million in 2002.

11. In 2003, the State repurchased the 47 percent of the company’s shares for approx. EUR 300 thousand. Since the Law on Management, Use and Disposal of State-Owned and Municipal Assets did not allow for buying shares from natural persons and private legal persons, an ad hoc law was passed: the Law on Acquisition of Shares of AB “Alytaus tekstile”. In December 2003, the Government approved the rehabilitation plan of AB “Alytaus tekstile” in order to avoid serious social, economic and employment problems in Alytus. Following that and shortly before the accession to the EU, the State provided assistance to the company for approx. EUR 8 million. The assistance comprised release from refunding a loan given on behalf of the State (the same loan of 1995) and from paying fines and interests, a new payment schedule in respect of the Personal Income Tax and social security contributions overdue, and
financial assistance of approx. EUR 1.5 million in the form of capital injection. As the implementation of such measures was not possible pursuant to the national laws in force, an ad hoc law was passed.

12. Despite the assistance, expected results were not achieved: volume of sales did not increase, costs did not decrease, and performance indicators did not essentially improve. In 2004 and 2005, the company suffered a net loss of more than EUR 4.6 million each year.

13. In 2007, AB “Alytaus tekstile” asked for further financial injection of approx. EUR 9 million to continue its activities. After long and very intensive discussions, the decision was taken not to provide any more assistance and to sell the shares owned by the State. The price was set at 1 cent (approx. 0.3 Eurocents) a share; the shares were sold on the Vilnius Stock Exchange in 2007. The new owners (a group of natural and legal persons) declared bankruptcy shortly thereafter.

14. Another example could be the State policy regarding AB “Mazeikiu nafta”, the only crude oil refinery in the Baltic States. It illustrates a difficult case where it is very complicated to strike the balance: it is not a failure but it can neither be perceived as a success. The overriding ground to support this company was the strategic importance of oil supply (the company is also included in the list of Enterprises of importance to ensuring national security); beside that, AB “Mazeikiu nafta” has been the main supplier of gasoline and diesel fuel for the Lithuanian, Latvian and Estonian markets, the largest buyer of services in Lithuania, largest Lithuanian company in terms of revenues and payment of taxes (approx. 230 million Euros or 4% of all taxes in 2007) as well as one of the major exporters.

15. The refinery was built in 1970s, the State policy in favour of this company continued until the accession of Lithuania to the EU. It consisted mainly of loans and loan guarantees for 520 million USD in total, import duties for oil products (5% from 1998; 15% from 1999 to 2004) and compensations for some of the losses (e.g., caused by interruption of the supply) until 2003. It has to be mentioned that the State was the owner or controlled the majority of the company’s shares at that time (59% in 1999). At the end of 2008, the State held 9.98% of the shares but the decision has been taken to sell the remaining part.

16. Speaking of the effectiveness of the State support, it has to be mentioned that the State did not impose any conditions on the use of the loans / guaranteed loans, no planning took place. It followed that only 8% of the sums received were used for investment, the rest of it covered the operating expenses.

17. AB “Mazeikiu nafta” operated at a loss for a long time. The productivity indicators have been very high all the time, 7-8 times higher than those of the whole economy; however, this could be based on the capital-intensive character of this particular industry and did not help to create new value or to at least ensure revenues covering costs. Only in 2003, after the Russian company “Yukos” became shareholder of AB “Mazeikiu nafta”, the company turned a profit. Until that year, it could not demonstrate successful economic activity and the State did not get any Corporate Income Tax revenues from this company. The tax revenues came from excise duty therefore they depended solely on the consumption of oil products and would have been collected anyway, irrespective of the origin of those products.

18. It has to be pointed out that, despite the good performance of the company in the past few years, AB “Mazeikiu nafta” is considerably dependent on the crude oil supply from Russia, and its performance indicators are very susceptible to the interruptions of this supply. Given the importance of this company to the Lithuanian economy, this embodies the risk of considerable negative effects.

19. The Competition Council carried out three investigations concerning AB “Mazeikiu nafta”, which resulted in conclusions (in 2000, 2001 and 2005) that AB “Mazeikiu nafta” had infringed the Law on Competition.
20. The first investigation was based on a complaint that the company is providing exclusive conditions of distribution of its products to a limited number of companies, fixing exclusive discounts to them. The investigation concluded that the AB “Mazeikiu nafta” held dominant position in the A-80 and A/92/95/98 brand gasoline and diesel fuel markets and that it took advantage of its unilateral decisive influence in the markets and, concluding similar agreements with different companies, fixed dissimilar conditions for the purchase of oil products. These actions of the company constituted an infringement of Article 9(3) of the Law on Competition, which prohibits abuse of the dominant position through application of dissimilar (discriminating) conditions to equivalent transactions with certain undertakings, thereby placing them at a competitive disadvantage.

21. While conducting the abovementioned investigation, the Competition Council established restrictions with regard to import of oil products. Consequently, the Competition Council initiated an investigation on the compliance of actions of the AB “Mazeikiu nafta” and 5 companies trading in oil products with Article 5 of the Law on Competition (“Prohibition of Agreements Restricting Competition”). AB “Mazeikiu nafta” was operating in the production level of the oil products (gasoline, diesel fuel, aviation fuel and fuel oil), while other 5 companies were engaged in the distribution of the said oil products in the trade level. The investigation established that AB “Mazeikiu nafta” selected companies holding or potentially holding import licenses, also maintaining relations with producers of oil products in other countries and holding a significant share of the market for trade in oil products. AB “Mazeikiu nafta” concluded agreements with 5 companies providing for discounts for them in exchange for their obligations not to import the said oil products. In practice it meant that where any actual or potential foreign producer would have an intention to sell its products on Lithuanian market, the binding contractual obligations would prevent the resellers from purchasing and distributing the products of such a producer. As a result, the possibilities of the AB “Mazeikiu nafta” to increase the sale of its products in the said markets and thus reduce the competition between its own products and imported ones were significantly improved.

22. In 2004, the Competition Council initiated ex officio an investigation to establish whether the activity of the company could have possibly had an impact upon the constant rise in gasoline and diesel fuel price levels in Lithuania as compared to those in other Baltic States, also whether the lasting price differences could have resulted through the abuse of its dominant position in Lithuania. Although initially the investigation was started in accordance with Article 9 of the Law on Competition, suspicions having arisen in the course of the investigation that actions of AB “Mazeikiu nafta” also could affect the trade between the EU Member States (Lithuania, Latvia and Estonia), the Competition Council decided to supplement the investigation with the provisions of Article 82 of the EC Treaty. As the European Commission did not exercise its legal authority to subject the investigation to its jurisdiction, therefore the investigation was further continued by the Competition Council. The investigation allowed a conclusion that higher prices of fuels in Lithuania as compared to those in Latvia and Estonia have resulted from a number of reasons stemming both from the different conditions in individual areas of the Baltic markets, as well as actions restricting competition exercised by AB “Mazeikiu nafta”. To a degree the price differences might have resulted due to differences in the excise duty conversion, also due to the requirements operational in Lithuania to accumulate the reserves of fuel, which in turn results in freezing part of the funds thus increasing the fuel prices, etc. However, the investigation established a number of facts and circumstances constituting a proof of the abuse of dominant position by AB “Mazeikiu nafta” by applying different strategies and economically groundless and discriminative pricing policy for Lithuanian, Latvian and Estonian buyers, as well as the annual loyalty and non-competing obligations, as well as other restrictive practices which resulted in dissimilar conditions for the entities operating in the market and allowed discrimination of individual companies. Therefore the companies were forced to sell fuels to Lithuanian consumers at higher prices than in Latvia and Estonia.
2.4. Does your competition agency use benchmarks to assess the economic costs and benefits of government interventions that promote industrial policy or national champions? Have you communicated benchmarks to other economic policy makers? Is there any dependable analytical approach that allows you to distinguish industrial policy from competition policy? Do you engage in competition advocacy in this policy area?

23. Rules of Procedure of the Government of the Republic of Lithuania stipulate that draft legal acts proposed to the Government and related to competition and state aid to economic entities must be sent for comments to and agreed on with the Competition Council. The analysis is made to ensure that the provisions proposed do not contradict any national or EU competition legislation in force, our agency is however not engaged in any other industrial policy considerations.

2.5. Have merger review laws ever been suspended in your country? If so, why? Were concerns expressed either explicitly or implicitly about the way in which merger efficiencies are typically examined or in the way in which failing firms are analysed?

24. Merger review laws have never been suspended in Lithuania nor were any concerns expressed about the way in which mergers or failing firms are analysed.

2.6. Have any of your decisions ever been overridden on grounds of industrial policy? Are there any recent examples? What reasons were given? To what extent had the competition agency already considered the market characteristics or considerations that were the basis for the override? What have been the consequences of the override for consumers and competition policy?

25. None of our decisions has been overridden on grounds of industrial policy. The existing legal framework does not provide for such a possibility, yet it leaves some freedom of manoeuvre in other aspects.

26. Article 2(1) (“Application of the Law”) of the Law on Competition lays down that this law “shall prohibit undertakings from performing actions which restrict or may restrict competition, regardless of the character of their activity, except in cases where this Law or laws governing individual areas of economic activity provide for exemptions and permit certain actions prohibited under this Law”.

27. Article 4(2) (“Duty of Public and Local Authorities to Ensure Freedom of Fair Competition”) of the Law on Competition stipulates that “Public and local authorities shall be prohibited from adopting legal acts or other decisions which grant privileges to or discriminate against any individual undertakings or their groups and which bring about or may bring about differences in the conditions of competition for competitors in the relevant market, except where the difference in the conditions of competition cannot be avoided when the requirements of the laws of the Republic of Lithuania are complied with.”. Moreover, the provisions of Article 19(1)(4) (“Powers of the Competition Council”) of the Law on Competition say that if public or local authorities infringe Article 4 of the Law on Competition and fail to comply with the request to amend or revoke legal acts or other decisions restricting competition, the Competition Council shall have the right to appeal against those decisions to the court, with the exception of the statutory acts issued by the Government of the Republic of Lithuania.

28. None of the above-mentioned exceptions were as yet applied in any resolutions of the Competition Council on the conformity of certain actions or decisions with the provisions of the Law on Competition.
2.7. Does your government implement some policies directly dedicated to innovation? If so, could you specify the sectors that benefit from these policies as well as the instruments used to foster innovation?

29. There are different measures, both national and co-financed by the EU Structural funds. These measures are not sector-specific. For the period 2008-2013, there are grant schemes for technical feasibility studies for SMEs, for R&D activities and facilities (labs, research centres etc.), for cluster management and infrastructure, for investment into new equipment and technologies, for investment into launching new e-business systems, new management methods and systems by SMEs, etc. These grant schemes conform to the EU State aid rules. There are also instruments of e.g., funding of public infrastructure in incubators, science and technology parks, i.e. public services in respect of innovation. Tax incentives are also provided: all companies investing in R&D are eligible for Corporate Income Tax reduction.

2.8. Did measures adopted in your country to deal with the recent economic crisis raise competition concerns? If so, could you describe the measures and the concerns? Have these competition concerns been taken into account, and, if so, how? In particular, have initial proposals been amended in order to comply with competition law? Have some of these measures been exempted from competition policy scrutiny?

30. On the contrary, due to the fact that Lithuania has a very limited access to financial resources, there are no measures to support undertakings, e.g., the Government tends to abolish all tax reductions. In case any support measures were to be introduced, the Competition Council would scrutinise them carefully for possible competition and state aid concerns.

3. Means and Goals

3.1. Please specify whether any of the following are instruments of industrial policy in your country:

- Government procurement
- Exemptions from antitrust laws
- Regulatory barriers to competition
- Access to credit
- Arranged mergers and acquisitions
- Control of acquisitions of national companies by foreign investors
- Other?

31. The exemptions provided for in the relevant public procurement laws should not be attributed to the instruments of industrial policy since they are granted to public contracts related to State secrets or official secrets, to international agreements with other countries, to military supplies, to financial services etc. In conformity with the provisions of the relevant EU legislation, exemptions may be granted for entities operating in the water, energy, transport and postal services sectors.

32. The exemption from antitrust laws pursuant to Article 2(1) of the Law on Competition is described in the answer to Question 6 above. Other possible exemptions are only granted to agreements of minor importance which do not appreciably restrict competition (de minimis) and to agreements covered by the relevant EU block exemption regulations.

33. Regulatory barriers to competition exist only in respect of activities regarded as public services, e.g., in the field of heat and electricity sectors, universal postal services etc.
34. The Law on State Debt foresees the possibility for legal persons of the Republic of Lithuania as well as of the EU or EEA Member States established in the Republic of Lithuania to receive loans from the funds borrowed on behalf of the State, as well as State guarantees. Undertakings (i.e. legal entities engaged in economic activity) are eligible for loans and guarantees if they carry out an investment project included into the State Investment Programme. Such loans and guarantees must respect the EU State aid rules. In practice, these instruments are now targeted towards financing of public infrastructure.

35. The only arranged merger took place in 2008 when the national electricity company LEO LT was established merging three companies controlling the electricity production and distribution system in Lithuania. This merger was determined by the obligation, included in the Accession Treaty, to close the Ignalina nuclear power plant at the end of 2009. The new company is designated to invest in a construction of a new nuclear power plant and power connections with Poland and Sweden.

36. Control of acquisitions of national companies by foreign investors is exercised only if a particular company is included in the list of enterprises of strategic importance to national security (see above).

3.2. To what extent are industrial policies in your country motivated or rationalised as regional or national economic development initiatives? Has this explanation been used more sparingly over time as your economy expanded?

37. Lithuania is still one of the least-developed regions of the EU, the whole country is regarded as a region eligible for assistance under Article 87(3)(a) of the EC Treaty (aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment) therefore the main objective of different Lithuanian policies, including industrial policy, is national economic development. This explanation has so far not lost its importance and priority. State aids are also predominantly awarded under the objective of "regional development".

3.3. To what extent are industrial policies motivated or rationalised as an effort to help domestic firms withstand the exercise of market power by foreign firms? How does this rationale square with rules against market distortions caused by state aids? How has your competition agency analysed these circumstances?

38. There were no industrial policies motivated or rationalised referring to this motive.

3.4. Are industrial policies motivated or rationalised as a means to correct market failures in your country? If so, what types of market failures have been involved? How do you compare industrial policy or national champions with other policy approaches for correcting these market failures (such as taxes or subsidies on consumption of the product)?

3.5. Do you think that one nation engaging in industrial policy or supporting national champions attracts retaliation from other nations? To what extent are projected gains from industrial policy and national champions dependent on other nations not pursuing these policies, too? Do industrial policy and national champions constitute a “prisoners’ dilemma” situation?

39. As an answer to both Questions 4 and 5, the following arguments against industrial policy, presented in the Long-term Economic Development Strategy of Lithuania until 2015, can be highlighted:

- the fact that, even if the market is deformed, there is no guarantee that industrial policy measures will distribute the resources more effectively than the imperfect market and
- the “risk of revenge from foreign countries”.
CONTRIBUTION BY MALTA
COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL CHAMPIONS

--Malta--

1. History and Evaluation

1.1. To what extent does the industrial policy in your country target firms on the basis of their nationality (e.g., by granting state aids/subsidies to national firms only, or by controlling their ownership)? If so, how is nationality defined?

1. Malta’s industrial policy does not target firms on the basis of their nationality nor does Malta’s legislation or regulators interfere with or control the ownership of market operators in any sector. There are no nationality prerequisites for the registration of companies or for the approval of mergers and acquisitions by the competition authority and generally nationality requirements are not attached to the granting of trading or operating licences.

2. In recent years the government has embarked on a sustained privatisation programme for government controlled entities that had enjoyed a state monopoly for a number of years. However, in none of the privatisation projects was Maltese nationality a requirement; indeed in most cases the business was acquired by foreign interests or a consortium involving foreign interests as in the banking, telecommunications and energy sectors.

3. Furthermore, legislation empowering the State to provide financial assistance and other forms of aid and incentives to industry does not make this grant of state aid conditional on the Maltese nationality of the beneficiary nor allow discrimination on the basis of nationality.

4. The Malta Enterprise, a government agency set up by the Malta Enterprise Act\(^1\) to replace the pre-existing Malta Development Corporation, the Malta External Trade Company Limited and the Institute for the Promotion of Small Enterprise Limited, is entrusted by the said Act to inter alia originate, lead and further initiatives relating to the economic and social development of Malta in line with Government objectives, policies and goals; to lead Malta’s strategy as relates to all forms of enterprise; to promote, assist and develop the establishment, competitiveness and internationalisation of enterprise in Malta; to develop the technological, human resource, and skills bases, and to strengthen the capacity of undertakings, to undertake strategic assessment and formulation, to innovate, and to undertake research, development and design activities; and to administer schemes, grants and other financial facilities requiring the disbursement of funds, including funds originating from foreign sources\(^2\). Neither this Act nor the Business Promotion Act\(^3\) (following amendments in 2001) which is also administered by the Malta Enterprise empowers this government agency to exclude non-Maltese beneficiaries or to discriminate against them in the incentive schemes devised and operated by it.

5. Indeed the role of the Malta Enterprise is to provide incentives for both foreign direct investors as well as local enterprises demonstrating commitment towards growth and increase in value added and employment. To date it has provided incentives that fall in the following six categories:

- **Investment Aid**: Companies engaged in specific activities can benefit from tax credits on capital investment and job creation.

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1 Chapter 463 of the Laws of Malta.
2 Ibid, Article 8.
3 Chapter 325 of the Laws of Malta.
- **SME Development**: Grants targeting the creation and development of innovative start-ups, and the development of forward looking small and medium-sized enterprises.

- **Enterprise Support**: Assistance to businesses to support them in developing their international competitiveness, improving their processes and networking with other businesses.

- **Access to Finance**: Companies may be assisted through loan guarantees, soft loans, loan interest subsidies or royalty financing in the case of highly innovative projects.

- **Employment and Training**: Enterprises are supported in recruiting new employees and training their staff.

- **R&D and Innovation**: Various incentives to stimulate innovative enterprises to engage in research & development.

1.2. **What economic conditions have been associated with government industrial policy and support for national champions in your nation and region? Has this changed over time as economic development advanced?**

6. In the 1970s and early 1980s, as Malta was seeking to develop, strengthen and diversify its industrial and economic base. having recently (in 1964) obtained its independence from foreign rule when the economy was heavily based on military expenditure, government policy was largely based on an interventionist, protectionist approach through the use of price and import controls devised to protect the local industry and the creation of state monopolies or government-granted monopolies. After 1987 and especially following Malta’s application for EU membership in 1990 (Malta joined the EU in 2004) more pro-market policies were adopted, leading to the dismantling of import barriers, liberalisation of markets and privatisation of state-owned enterprises and reduction of subventions. The extensive liberalisation and privatisation programme is still under way as temporary derogations won during the EU negotiation process expire. Today, the government is focusing its role in the economy on the regulatory aspect, facilitating rather than participating as an operator in economic activities while in certain sectors promoting the use of public-private partnerships and building strategic partnerships as part of its strategy to stimulate economic growth. Current industrial policy strategy, apart from maintaining and upgrading existing investment (most of which involves SMEs), is to attract new foreign direct investment (FDI) targeting primarily the sectors of pharmaceutical manufacturing and services; the ICT; biotechnology and bio-informatics; high-tech manufacturing; creative sectors; and the maritime and aviation industries.

1.3. **Are there major success stories of industrial policy or national champions that are prominent in policy discussions? Are there any perceived major failures of industrial or national champion policies? How do you define “success” and “failure” in this context? Are successful national champion stories supported by best practice competition policy standards?**

7. In the 1990s Malta managed to successfully diversify its economy from one initially based on tourism and light and heavy manufacturing such as textiles and shipbuilding to an economy thriving on ‘new’ economy products and services such as in the Information and Communication Technology (ICT) and financial services sectors and on high value-added manufacturing industries by for instance attracting foreign direct investment in the pharmaceutical industry.

8. The country’s ICT vision has registered considerable success in the attraction of ICT companies operating from Malta. Government’s commitment to establish Malta as an ICT centre of excellence has led to vertical strategic alliances with the leading international ICT firms, while a number of other foreign ICT companies are locating their operations in Malta. A major deliverable of this strategy was the development and implementation of a Technology Centre of Excellence in the region. SmartCity Malta is the vehicle for the realisation of this deliverable as it will create a state-of-the-art ICT and Media Park on the models of
Dubai Internet City and Dubai Media City and is the largest foreign direct investment in the ICT and media sectors ever made in Malta.

9. However, industrial policy and competition policy have always been considered as complementary rather than conflicting policies. The small size of the domestic market tends to limit the scope for competition in a number of markets. In the presence of imperfect market structures, one of the tenets of Malta’s industrial policy, as reiterated in several policy documents, has been that ever more aggressive regulation and supervision of market players should be adopted. The strengthening of competition policy and competition authorities has thus always been a key priority, with further liberalisation of economic sectors deemed necessary to enhance the degree of competition in the domestic markets.

1.4. Does your competition agency use benchmarks to assess the economic costs and benefits of government interventions that promote industrial policy or national champions? Have you communicated benchmarks to other economic policy makers? Is there any dependable analytical approach that allows you to distinguish industrial policy from competition policy? Do you engage in competition advocacy in this policy area?

10. The Office for Fair Competition does not use benchmarks to assess the economic costs and benefits of government interventions that promote industrial policy or national champions but it uses competition advocacy to ensure that industrial policy does not damage competition: it comments on and recommends changes to proposed or adopted legislation, government measures or government policy that it considers not to be in line with competition principles or that raise competition concerns. Moreover, since 2004, no undertaking, including public undertakings or state controlled entities with special or exclusive rights, and no economic sector is excluded from the scope of the competition rules; so national champions are subject to the full rigours of competition law as any other undertaking. The only exception is where the undertaking is entrusted with the operation of services of a general economic interest or has the character of a revenue producing monopoly where the Office would refrain from subjecting such activities to the full rigour of the competition rules if their application would obstruct the performance, in law or in fact, of the particular tasks assigned to the undertaking; yet even here this exemption is applied very restrictively. As for state aid, there is a specific agency, the State Aid Monitoring Board that reviews and assesses existing and new state aid and provides advice about their compatibility with EU State Aid law and acts as an interlocutor with the European Commission on State aid matters.

1.5. Have merger review laws ever been suspended in your country? If so, why? Were concerns expressed either explicitly or implicitly about the way in which merger efficiencies are typically examined or in the way in which failing firms are analysed?

1.6. Have any of your decisions ever been overridden on grounds of industrial policy? Are there any recent examples? What reasons were given? To what extent had the competition agency already considered the market characteristics or considerations that were the basis for the override? What have been the consequences of the override for consumers and competition policy?

11. The Control of Concentrations Regulations, Malta’s first merger review law, entered into force on 1st January 2003 and has never been suspended. Industrial policy considerations have never featured in the assessment of concentrations, the test being solely whether the concentration might lead to a substantial

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4 Competition Act, Chapter 379 of the Laws of Malta, Article 30.
5 Business Promotion Act, Chapter 325 of the Laws of Malta, Articles 57-58.
6 LN 294 of 2002 as subsequently amended.
lessening of competition in the Maltese market or a part of it. No concerns have ever been expressed about the way that the Office for Fair Competition that is responsible for its implementation assesses efficiencies or failing firms under these provisions, though to date there has been no concentration that though raising competition concerns was cleared on the basis of efficiencies or the failing firm defence. The Regulations and the Competition Act do not empower the government to override any decision of the Office for Fair Competition on grounds of industrial policy or any other ground. The decisions are reviewable only by the Commission for Fair Trading, an independent administrative tribunal, which may overturn these decisions only on competition grounds.

1.7. Does your government implement some policies directly dedicated to innovation? If so, could you specify the sectors that benefit from these policies as well as the instruments used to foster innovation?

12. Malta, with the exception of the ICT sector, has been lagging behind in R&D expenditure and has been regressing in terms of its competitiveness and the supporting role played by research and innovation in this regard. The figures for business research and innovation for 2003 show that expenditure on R&I from the private sector constituted only 0.069% of GDP while the public R&I expenditure stood at a mere 0.19% of GDP. However, the government has now embarked on a strategy of actively promoting research and development and innovation and the European Innovation Scoreboard (EIS) for 2008 places Malta in the category of countries that are ‘catching up’. It certifies that Malta’s innovation performance is below the EU27 average but the rate of improvement is above that of the EU27. The report confirms that Malta’s relative strengths are in the availability of finance for innovation projects and the support by the government for innovation activities; however, the number of firms that have introduced innovations onto the market or within their organisations, covering technological and non-technological innovations, remains low.

13. R&D activity in the business sector is largely concentrated in 30-40 firms and is clustered around a number of specific sectors, mainly related to high-value-added manufacturing in ICT, manufacture of machinery, manufacture of chemicals and medical instruments, financial intermediation, food and beverage, and printing, among others. The precise level of sectoral R&D activity is difficult to determine, since official statistics are not readily available, and are often not reliable since firms do not always report their R&D activity or give incomplete information. This makes it difficult to determine the level of intensity of private R&D investments as a percentage of sectoral GDP.

14. Malta’s industrial sector is characterised by a dual structure. On the one hand, industry predominantly consists of domestically-owned micro enterprises primarily local market oriented and engaged at the lower end of the technological ladder generally lacking the critical mass to engage in research, technological development and innovation. On the other hand, Malta’s industry comprises a number of foreign owned affiliates of multinational conglomerates which undertake research, technological development and innovation activities in home economies and merely transfer technology to Malta in accordance with corporate strategies to serve the needs of the local manufacturing arms. This state of affairs has so far resulted in limited inter-linkages between the domestic and foreign sector, primarily as a result of lack of economies of scale and scope.

15. Government initiatives to boost research and development and innovation have taken mostly the form of aid schemes administered by the Malta Enterprise. As stated above, some of the financial and fiscal incentives provided by the Malta Enterprise are directly devised to facilitate R&D expenditure and encourage innovation and to attract to Malta foreign enterprises that are innovation driven such as the package of aid schemes specifically designed to stimulate innovative enterprises to engage in research &

development. Malta’s National Reform Programme 2008–2010 envisages that further aid in this category will be granted via incentives such as the EUREKA and the EUROSTARS initiative together with the R&D grant schemes funded under the European Regional Development Fund (ERDF). Encouraging innovation will take place through the implementation of a grant scheme funded under the ERDF promoting product and process innovation together with eco–innovations.

16. Moreover, in the National Reform Programme the government undertakes to raise its R&D expenditure in relation to GDP from its current 0.3% to 0.75% by 2010, to support innovation through public procurement, to participate in joint programming activities and to target research strategies for identified priority areas. For the next two years government has identified two priority areas: (i) increased efforts towards more and better research in the manufacturing sector and (ii) formulation of a health research strategy and action plan.

17. Furthermore, in the Industry Strategy for Malta: 2007–2010 the Government advocates clustering and networking for industry as it considers that inter alia the mix of competition and co-operation would act as underlying drivers of learning and innovation.

18. Malta’s accession to the European Patent Convention in March 2007 as well as Malta’s strong patent laws have also served to encourage innovation.

1.8. Did measures adopted in your country to deal with the recent economic crisis raise competition concerns? If so, could you describe the measures and the concerns? Have these competition concerns been taken into account, and, if so, how? In particular, have initial proposals been amended in order to comply with competition law? Have some of these measures been exempted from competition policy scrutiny?

19. None of the measures taken so far to deal with the current economic crisis have raised competition concerns.

2. Means and Goals

2.1. Please specify whether any of the following are instruments of industrial policy in your country:

- Government procurement
- Exemptions from antitrust laws
- Regulatory barriers to competition
- Access to credit
- Arranged mergers and acquisitions
- Control of acquisitions of national companies by foreign investors
- Other?

20. The Public Contracts Regulations ensure that there is no discrimination between economic operators and that all economic operators are treated equally and transparently in all calls for tenders whatever their estimated value\(^8\). There are some contracts that are exempted from this rule but this exception is not there for industrial policy purposes as it applies to public contracts awarded in pursuance of an international agreement concluded by Malta in accordance with EC rules, public contracts linked to the protection of Malta’s security, public contracts relating to public telecommunications networks and various public service contracts.

\(^8\) LN 177 of 2005 as subsequently amended, Reg 4.
21. No economic sectors or undertakings are exempt from antitrust laws. Any remaining regulatory barriers to competition post EU accession are being progressively dismantled and markets fully liberalised to competition. Though certain state monopolies remain (e.g. in respect of transmission of electricity where Malta obtained a derogation from certain provisions of the Electricity Directive because it is a ‘small isolated system’) and some licensing systems have been retained to limit the number of operators in the markets concerned, these are justified and necessitated by the constraints and market imperfections inherent in small market economies (like Malta) and not driven by any industrial policy considerations.

22. There are no government restrictions on access to credit but, as shown above, Government through the Malta Enterprise facilitates access to credit through various schemes. As for mergers and acquisitions there is no government or regulator interference except for oversight by the Office for Fair Competition that, as explained above, may block or force changes to mergers or acquisitions only on purely competition grounds.

2.2. To what extent are industrial policies in your country motivated or rationalised as regional or national economic development initiatives? Has this explanation been used more sparingly over time as your economy expanded?

23. As reiterated by various policy documents, Malta’s industrial policies are essentially geared at promoting a competitive and high value adding economy and achieving sustainable socio-economic development for a better quality of life and a more sustainable use of the environment.

2.3. To what extent are industrial policies motivated or rationalised as an effort to help domestic firms withstand the exercise of market power by foreign firms? How does this rationale square with rules against market distortions caused by state aids? How has your competition agency analysed these circumstances?

24. Malta’s industrial policy is not devised as a means of protecting local industry against the exercise of market power by foreign firms but, operating within the confines of EU State Aid law and Maltese and EC antitrust rules, as explained above, it is intended to increase the competitiveness of local industry (largely composed of SMEs) particularly in so far as their R&D and innovation efforts are concerned or where they are expanding into new international markets.

2.4. Are industrial policies motivated or rationalised as a means to correct market failures in your country? If so, what types of market failures have been involved? How do you compare industrial policy or national champions with other policy approaches for correcting these market failures (such as taxes or subsidies on consumption of the product)?

25. None of the industrial policy measures are intended as a means of correcting market failures.

2.5. Do you think that one nation engaging in industrial policy or supporting national champions attracts retaliation from other nations? To what extent are projected gains from industrial policy and national champions dependent on other nations not pursuing these policies, too? Do industrial policy and national champions constitute a “prisoners’ dilemma” situation?

26. Supporting national champions by exempting them from the full rigour of the competition and state aid rules or by shielding them from competition on the home market through regulatory barriers is counter-productive as it invites retaliation from other States and actually weakens the firm’s competitiveness in the international markets as the challenge of facing competition at home would drive the firm to lower its costs and boost its efficiency and sharpen its innovative drive. If all States were to adopt a pro-national champion approach the result would be less efficient firms in the market to the detriment of consumer welfare and consumer interests. Thus, even for a small nation it is not in its interests
to promote champions by following a lax competition policy. On the other hand, one should distinguish industrial policy from a national champion policy as an industrial policy that seeks to sharpen the competitiveness of local industry and instil or heighten the innovative drive and make industry more high-tech and knowledge intensive has the same goal as competition policy – that of consumer welfare.

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CONTRIBUTION BY NORWAY
COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL CHAMPIONS

--Norway--

1. Introduction

1. During the last decades we have witnessed increased globalisation of the world’s economy. Trade barriers have been broken down and enabled us to exploit huge benefits from increased competition and international trade. Important progress has also been made in international coordination and harmonisation of competition rules and practices, although much work remains in this area.

2. Recently the international financial crisis poses a serious threat to this positive development, at least in the short run. The danger is now that the current crisis will bring this positive trend to a halt and induce world economies to be more protective, at least in the short run. Instead of focusing on the long term benefits from competition and international trade in a globalised economy, many fear that world leaders will focus on short-term national interest and the protection of local industries and labour markets.

3. The long term consequences of the current crisis may still be many. First we run the risk of increased general mistrust of market based solutions, which in turn also may influence competition policy. Second, we may experience that public interference in free markets may become more acceptable. We have seen many and large rescue packages for the banking sector which for the most part are sensible, but the danger is that also other industries would be covered by this. This could lead to a phase of state aid race where national governments seek to improve the competitiveness of local industry by granting them subsidies. We clearly see such tendencies within the car industry world wide. Moreover, efforts toward international convergence of competition policy may experience a setback, not only in the US-EU relations but also when it comes to implementing modern competition policy in emerging economies such as China and India.

4. There is also a danger of politicising competition policy which would mean a setback for effects-based and bureaucratic competition enforcement. Examples of this are already starting to pop up worldwide, and the danger is that this tendency will continue. The lifting of normal merger control for the Lloyds TSB takeover of HBOS in the UK may serve a case in point. In this case the OFT found serious competition concerns with the proposed takeover and referenced the case to the Competition Commission. However, in late October 2008 the UK Secretary of State cleared the merger without reference to the Competition Commission.

5. Finally, national states may be tempted to promote national champions to alleviate short run economic problems, even in the absence of market failure.

6. Event though the current financial crisis may involve a temporary setback to globalisation and increased international competition, it is hard to imagine that this will be a permanent trend. After all, the crisis is largely due to improper regulation of the financial sector and unwise policies, and not too much competition. When the current crisis blows over, the efforts to globalise markets will continue. The question then is whether promoting national champions to counter this short run crisis, is a good long run solution.

7. The national champion debate is also inherently linked to industrial policy (see Seabright, 2005; Falck and Heblich, 2007). One way to define industrial policy is (Foreman-Peck (2006): “state intervention that affects, or is intended to affect, industry but not other economic activities directly.” The rationale for industrial policy is normally perceived as to correct market failures. One of the central elements of the EU’s Lisbon Strategy is “... to make EU the most competitive and dynamic knowledge-based economic
region of the world.” One way to fulfil this goal is to promote European or national champions through industrial policy.

8. National champions can be categorised with at least four different types (Cohen, 1995; Falck and Heblich, 2007): Chicks, lame ducks, big project firms and strong firms. Strong firms are the real champions: competitive and technologically advanced firms. Lame ducks are lagging behind in technology and competitiveness, while big-project firms operate in strategic fields targeted by local governments.

9. There is strong evidence that radical innovations are more frequently introduced by new firms rather than incumbents (Audretsch, 1995). Hence, industrial policy targeting high-tech chicks (infant industries) should promote diversity and small and medium sized industries to promote experimentation and variety. Hence a national champion policy towards chicks is almost deemed to fail. Lame ducks are found in none-competitive environments and declining industries, historically protected from international competition. Optimal industrial policy towards these firms often is to allow them to die and to support the process of structural change.

10. Big-project firms are in many respects similar to lame ducks, but the need to support these firms is not found in poor economics performance or market failure. Instead the justification is strategic and firms from the energy or military sector are often involved. Hence, in fact the only scope for industrial policy should be to promote the real champions, i.e. firms that operate on or close to the technological frontier that has the potential to be highly competitive on the world market. The question is whether these firms are an industrial policy issue?

11. The current financial crisis may tempt policy makers to promote national champions as a short run remedy even in the absence of market failure. This could for instance be done by introducing lax merger control. The question is whether lax competition policy is a good long term solution to the current crisis. The next section explores some theoretical arguments for creating national champions though lenient merger control.

2. A theory of national champions

12. The basic question explored in this section is the effects of lenient merger control to promote a national champion. I will illustrate the theoretical effects by constructing a very simple example which I will gradually make more complex and realistic. The main ingredients of the examples will be some merging firms and some firms that are outsiders to the merger. I will distinguish a situation with a closed economy, which can be thought of as the financial crisis, where all relevant firms are domestic. This will be contrasted with a second scenario with an open economy where some firms are owned by foreigners. The latter can be thought of as a more globalised economy. The focus will be on how any proposed merger will affect national welfare in the two settings, i.e. we are concerned about both domestic consumers and domestic firms’ profits.

13. To make it really simple, consider first a national market with three symmetric firms with constant marginal costs in an industry. The market is characterised by some form of imperfect competition. The economy is closed and all firms are owned nationally. Then consider a proposed merger between two of the firms involving no cost savings. The standard effect of the merger will be a price increase followed by an increase in the dead weight loss. This can be illustrated as in Figure 1 below.
14. Before the merger the joint profit of all three firms is $D + E + F + G$. After the merger the joint profit is $A + B + D + E + F$. Hence, the increase in profit is $A + B - G$. Consumers have lost $A + B + C$ due to increased price. Hence, the loss to society from the merger is $C + G$.

15. Then consider a similar merger in an open economy. Recall that now (the outsider) is a foreign-owned firm. This situation is illustrated in Figure 2.
16. We see that the consequence for consumers is the same; the price increases by the same amount as before. The joint profit is also the same, but now some of the profit ends up with the foreign firm. Area E in the figure is the profit shift from the domestic to the foreign firm. When the merging firms contract their joint output, the outsider (foreign firm) will expand output and earn more profit. In addition, some of the reduced consumer surplus is now transferred out of the country as profit to the foreign firm. This is illustrated by area A in the figure. Thus, the loss in national surplus from the merger is now C + G (the dead weight loss) plus A + E, where the latter stems from the fact that the outsider to the merger is a foreign owned firm.

17. The lesson we can learn from this simple example is that a merger between domestic firms to create a national champion is generally detrimental to national welfare, and more so in an open economy where outsiders may be foreign firms. Hence, from a national perspective we should be more sceptical to national mergers in open economies than in closed economies.

18. Clearly, this is a very simple example and we need to develop this further. An obvious objection is that if the merger involves substantial cost synergies the result may differ. However, this depends largely on the nature of the cost savings involved with the merger. If the savings are predominantly fixed costs – for instance due to savings of a head quarter – there will still be a price increase and a profit loss out of the country as in our first example. On the other hand, if the savings are made in variable costs, we might experience a price decrease following the merger. However, in order to achieve a price decrease, the savings in variable costs have to be quite substantial. Moreover, the profit loss out of the country still counts negative for the national surplus even in this case. There is no clear evidence of substantial and systematic cost reductions from mergers. For instance, in the banking industry there are studies suggesting that economies of scale are exhausted for quite small operations. The implication for merger policy is that claims about cost savings should be met with sound scepticism unless they are backed by convincing documentation. Also, one should focus on savings in variable costs more than fixed cost savings.

19. Another potential objection is that the domestic market may be a part of a larger international market. One example is the common Nordic spot market for electricity. Can this be an argument for being more lenient towards domestic price-increasing mergers? Clearly, if the country is a net importer of electricity, the answer is clearly no. However, if the opposite is true – i.e. the country is a net exporter; domestic welfare might increase even with a price-increasing merger. The reason is of course that the increase in profit for national firms from exports may outweigh the negative impact domestically. In the Nordic electricity market Norway is on average a net exporter, but this is about to disappear. This means that nationally it can be beneficial to allow domestic mergers, especially if the price-cost margin is very low at the outset. However, it is clear that consumers will always lose from a price-increasing merger. With a consumer standard for evaluating mergers, this can never be beneficial. Moreover, allowing mergers for this reason will be a beggar-thy-neighbour policy, and other countries may be tempted to do the same. The result would be a prisoners’ dilemma where all countries are worse off compared to the situation where no countries pursued such a policy. This illuminates the need for supranational competition policy where all national states coordinate their policies.

20. Yet another scenario is that a merger between two domestic firms may be a move to prevent a takeover from a foreign firm. If we allow such an international merger we must recall that the outsider will be a domestic firm. The profit shift will be as above, but this time into the country. A question that arises is whether the cost savings are larger or smaller with an international merger than with a domestic merger. There are at least two reasons why an international merger may induce more costs savings. First the domestic firm may get access to knowledge and more efficient technology from the multinational firm. Second, an international merger may lower wages as some competition may be induced between trade unions in different countries, as the merged firm may threaten to move production from one country to
another. Therefore the price increase following an international merger may very well be smaller than the price increase from a domestic merger.

2.1. Examples

21. Two examples from the Norwegian market might help illustrate the point above. In the Norwegian industry for farmed salmon the government imposed a restriction on ownership and thereby prevented the development of a national champion. In spite of this the Norwegian salmon industry has experienced a considerable international success. Between 1990 and 2001 the sales of Norwegian salmon tripled and costs and prices dropped substantially over the same period. This development is illustrated in Figure 3 below.

Figure 3. Prices and costs for Norwegian farmed salmon 1985-2006

22. A different example is the rather sad story of the Norwegian cement industry. For a long time, this industry escaped antitrust scrutiny which enabled the industry to sustain a national price cartel from 1923 to 1967. The cartel was set up in a way that the market shares for the different producers were distributed according to each producer’s share of total capacity. To no one’s surprise, this setup induced the firms to overinvest in capacity, which the firms did especially after World War II. This of course led to huge costs and the price that could be obtained on international markets did not cover the costs associated with the expansion in capacity. Figure 4 below depicts domestic production relative to Norwegian consumption of cement.
Figure 4. Domestic production and consumption of cement 1927-1988

3. Conclusion

23. Industrial policy to promote national champions should be motivated and based on the existence of a market failure. However, absent market failures, policy makers may still be tempted to promote national champions for a variety of reasons. The current financial crisis is one reason why policy makers may be extra tempted to promote national champions. The financial crisis will pass, and then the process of globalisation will continue. Hence, the question is whether promotion of national champions to solve a short term problem is a good long term solution.

24. Globalisation in the long run involves increased international competition, but also increased competition for acquisitions. The question then is whether policy makers should help their national champions by introducing lenient competition policy to allow already large domestic firms to grow even larger? In the same vein, should national policy makers try to avoid foreign acquisitions of national champions?

25. As I have illustrated through theory and examples there is scant evidence that a policy of promoting national champions will be beneficial for national welfare even in the short run, and much less so in the long run. On the contrary, one might argue that fierce competition at home will induce firms to be innovative and cost efficient. This in turn, will pave the way for success in an international market. Moreover, promoting national champions by one state may induce neighboring states to pursue the same policy. If so, the only consequence will be concentrated national markets and potentially serious harm to consumers.

26. Thus promoting national champions in the short run to counter the current crisis may be potentially very damaging in the long run. Creating national monopolies will certainly harm consumers by increased prices at home. This could - in principle - be justified if the international success of a national champion would feed back to the domestic market. However, it is not a straightforward issue that a
national champion will be successful internationally, and even if it were, it is not clear whether this success would be channelled back domestically. It is tempting to paraphrase Gerosky (2005): “Competitive markets create champions, not governments.”

4. References


CONTRIBUTION BY PAPUA NEW GUINEA
1. Introduction

1. Papua New Guinea (PNG) has been an independent nation since 1975. For many years it was thought that the economy had not developed enough to warrant competition law. There was some limited consumer protection law and price control. Furthermore with most utilities being provided by the national Government time was not ripe for competition law. Industry was largely Government run or controlled.

2. However with the move to privatisation of some utilities and the development of the PNG economy competition law was introduced. That process commenced in 1996.

3. Competition Policy and Industrial Policy became part of the same goal, economic efficiency and consumer welfare.

4. The policy was to open up markets to imports, foster exports and generally encourage competition. Industries that lacked competition were subject to regulation by the competition regulator, including price control in some limited circumstances.


6. The competition provisions, referred to as the Market Conduct Rules, are based on those in the New Zealand Commerce Act and are similar to the competition provisions applying in most developed economies. Broadly speaking, the Market Conduct Rules prohibit arrangements which substantially lessen competition (with a per se prohibition of price fixing); resale price maintenance; exclusionary conduct (primary boycotts); and misuse of market power (abuse of dominant position). Anti-competitive mergers or acquisitions are also prohibited. Authorisation by the ICCC on public benefit grounds can be applied for – a small number of authorisations on public benefit grounds have been approved by the ICCC since 2003 for business acquisitions or for anti-competitive arrangements.

7. The law is tailored to meet PNG needs. In particular there are provisions regulating PNG’s monopoly (government owned) utilities. There is also provision for price control, though the number of products which are currently subject to price control or price monitoring is very few.

8. In effect the ICCC Act has an overall competition and consumer protection mix. In addition the Act has some unique provisions relating to essential utilities which affect the bulk of PNG consumers.

2. Clearance and authorisation.

9. The Act provides for both clearance and authorisation in relation to mergers and has set time limits for both. In relation to clearance the ICCC has to make its decision within 20 days, in relation to authorisation it is 72 days. [Clearance is where the ICCC is requested to declare whether or not a merger may result in a substantial lessening of competition. Authorisation is where a merger or acquisition which would or might substantially lessen competition, and thus be in breach of the law, can be exempted on public benefit grounds.]
10. Authorisation (but not clearance) is also available for conduct which would otherwise be prohibited by the other competition provisions of the Act, except for taking advantage of market power (abuse of dominant position) which cannot be authorised. In a small non trade exposed economy such as PNG there is a very high likelihood that many mergers will substantially lessen competition. Further, conduct such as resale price maintenance and exclusive arrangements that have no doubt been prevalent in PNG for many years are now either clearly unlawful or potentially unlawful.

11. The clearance and authorisation processes allow other factors and policies to be taken into account when considering competition issues, including industry policy.

3. Regulatory and price control provisions of the ICCC Act

12. In addition to its functions in administering competition law, the ICCC has other industry regulatory and price control roles.

13. PNG industry regulatory framework relates specifically to government owned monopoly utilities, where there is a “regulatory contract” between each of the utilities and ICCC (on behalf PNG consumers), which sets a price path for the monopoly services provided by that utility, going forward into the medium to long term future, as well as setting out required service quality standards.. Those regulatory contracts with the ICCC exist in relation to electricity, water, ports, telecommunications and postal services.

14. The regulatory contracts are developed and enforced and reviewed by the ICCC. The contracts relate to pricing, service standards, innovation, capital expenditure plans and increased efficiencies.

15. Price control has been rolled back in recent years but still applies to some basic commodities used by PNG citizens. For example price control or price monitoring exists in relation to fuel, public transport services, rice and flour.

16. In addition to its regulatory contracts and price regulation functions, the ICCC conducts regular reviews of sectors of PNG industry and advises the Government on possible changes to regulation or policies generally in those industries. Recent reviews include petroleum, coastal shipping, tourism, general insurance, and the water and sewage industries. Through these reviews, the ICCC’s views on competition policy can be injected into the debate on industrial policy in these industries.

4. The ICCC

17. The ICCC is the only national regulatory body that acts as a consumer and business watchdog. The provisions of the ICCC Act apply to all businesses in Papua New Guinea including government enterprises. The ICCC Act also applies to conduct outside PNG which affects the PNG market.

18. The ICCC was set up to be independent from government interference or pressure from individual Ministers or politicians, in recognition of the importance of the industry regulator having integrity and a totally professional and objective approach to its tasks, protected from outside influence. This was seen as being particularly important in the PNG environment where, as with many developing countries, corruption and lack of transparency in decision making have been major impediments to business confidence – particularly so where PNG has in recent years received an adverse rating from Transparency International on its worldwide corruption index – 161st out of 179 countries.

19. To ensure this independence and integrity, the Commission consists of a full time Commissioner and two part time Associate Commissioners, all of whom are appointed by a committee which includes both the Prime Minister and the opposition leader. One Associate Commissioner position is allocated to an overseas industry regulation expert. Commissioners, who are appointed for five years, are protected
against arbitrary dismissal by having, in effect, the tenure of a senior judge. In addition, the ICCC Act expressly provides that the Commission is not subject to direction or control by a Minister or anyone else in the performance of its functions, except for certain specific, publicly notified directions.

20. In performing its functions and exercising its powers under the ICCC Act, the ICCC is required to have regard to the following primary objectives:

- to enhance the welfare of the people through the promotion of competition and fair trade and the protection of consumers’ interests;
- to promote economic efficiency in industry structure, investment and conduct; and
- to protect the long term interests of the people with regard to the price, quality and reliability of significant goods and services.

21. The ICCC Act also gives the ICCC a number of facilitating objectives:

- to promote and protect the bona fide interests of consumers with regard to the price, quality and reliability of goods and services;
- to ensure that users and consumers (including low-income or vulnerable consumers) benefit from competition and efficiency;
- to facilitate effective competition and promote competitive market conduct;
- to prevent the misuse of market power;
- to promote and encourage the efficient operation of industries and efficient investment in industries;
- to ensure that regulatory decision making has regard to any applicable health, safety, environmental and social legislation; and
- to promote and encourage fair trading practices and a fair market.

22. These primary and facilitating objectives require the ICCC to focus on industrial policy in carrying out its functions, and thus gives the ICCC a central role in the administration of industry policy.

5. Interaction between the ICCC’s promotion of competition, and its regulatory roles

23. The ICCC’s primary objective is the enhancement of consumer welfare, while the protection and promotion of competition is one means towards achieving that end. PNG is a small economy and competition is not always possible but consumer protection is essential. There may be circumstances where price regulation or other government intervention is needed to protect consumers and make sure that they have access to best value goods and services.

24. The competitiveness of a market affects the level of consumer protection required. In PNG we strive for competitive and informed markets but that is not always possible and hence substantial reliance on regulatory and price controls.
25. In circumstances where there is little or no competition in the market (e.g. in a natural monopoly situation such as a telephone or electricity utility, and particularly in small economies that tend to have less competitive markets) there may be greater justification for intervention to ensure that consumer welfare is maintained because competition is not driving the market.

26. In short, the amount and type of regulation there should be to ultimately benefit consumers will depend on the competitiveness of markets. In highly contested markets, regulation should be only introduced with great care, while in markets where there is little or no contestability, some form of regulation may be more readily justified. That regulation may extend, in some cases, to price regulation or price control for particular commodities or services, where market forces alone cannot restrain prices, even though price control is, in one sense, the antithesis of competition regulation.

27. Given the high degree of interaction between the two policies, it is not possible to determine competition law policies and consumer protection policies in isolation. It is not only possible, but necessary, to administer these laws in harmony to achieve the ultimate goal of consumer welfare.

6. Importance of competition policy to a small economy

28. Competition policy, which is appropriately designed and effectively enforced, can be more important in small economies than in larger ones.

29. Small economies can support only one or two competitors in many industries, because of the small size of the markets. Openness to trade is a good solution to many of the problems of small size, because it enlarges the market, but competition policy also plays a crucial role in regulating market activity; it helps trade by reducing barriers to both foreign importer entry and domestic product exports; it plays a critical role where exposure to international trade is not sufficient to solve a small economy’s efficiency problems; and where artificial trade barriers (such as tariffs) are not reduced, competition policy is an alternative for regulating ‘closed’ small markets. In this sense, competition policy is a subset, or an integral part, of industry policy.

30. However, since competition policy is adopted to address various failures of the market, the policy should be carefully designed to deal effectively with the unique obstacles to competition that are present because of the small size of the economy.

31. The main goal of competition policy in small economies should be to promote efficiency. But when considering competition policy for small economies you are faced with a dilemma.

32. On the one hand, large firm or plant size may be required in order to achieve efficient scales of production, so it may be that only one or two firms can operate in an industry in order to achieve efficiency.

33. But on the other hand, the high level of concentration, or even monopoly control, of a market that results can lead to certain types of industry behaviour that is very damaging to efficiency.

34. The case studies on national champions, set out below, demonstrate how this damage can occur unless it is carefully managed.
7. Industry Policy issues - interaction and conflict with competition law

7.1. Protectionism

35. Starting in 1999, significant unilateral trade liberalisation began in PNG under the Tariff Reform Program. Most imports (about 75% in value) enter duty free. Tariffs are applied to those products that are made, or could be made, in PNG. Rates on these imports have declined by 5% in each of January 2001, 2003 and 2005 to their current rates of 40%, 25% and 15% for the prohibitive, protective and intermediate product rates respectively.

36. PNG has no antidumping, countervailing duty or safeguard mechanisms (trade remedy instruments). Some manufacturers, feeling the effect of the Tariff Reform Program, are urging the PNG government to legislate for such trade remedy instruments. PNG’s Import-Export Impediments Subcommittee has been specifically requested to address, and potentially prepare legislation and procedures, for the trade remedy instruments. It is possible that unless some reasonable trade remedy instruments are designed, legislated and enacted, future Tariff Reforms will be stalled. Some PNG negotiators consider trade remedy instruments necessary before considering future cuts.

37. PNG has entered into FTA agreements with the Pacific (Pacific Island Country Trade Agreement and sub regionally with the Melanesian Spearhead Group Trade Agreement) and the EU. The latter being part of the EU’s EPA initiative for the Pacific ACP countries (PACPs). An interim agreement has been intialled and a comprehensive agreement including services and development issues are to be negotiated. The latter may include a competition law provision.

38. The entry into the above FTAs has triggered Article 6 of the Pacific Agreement on Closer Economic Relations (PACER) agreement which requires the Pacific states to commence negotiations for a full FTA with Australia and New Zealand. Australia has indicated their desire to enter into these PACER+ negotiations. Australia is the exporter for 56% of PNG’s imports. If negotiated, PACER+ will have significant implications.

39. The likely precedent to be used in the PACER+ negotiations will be the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZERTA). ANZERTA has one of the strongest set of competition law provisions of any regional trade agreements. We understand that the competition law provisions go beyond co-operation and comity issues and require competition principles to be used in applying trade remedy instruments.

40. Generally speaking, both trade remedy and competition policy legislation and application has been prone to regulatory capture by protectionist influences, industrial policy advocates and self-interest groups. With PNG looking for rapid industrial and resource development, this is potentially a minefield for PNG’s competition, trade and investment liberalisation objectives. Some potential investors in PNG have taken advantage of PNG’s situation of a small and underdeveloped economy needing to develop its industrial base, combined with PNG’s relatively high perceived sovereign risk, to extract concessions and competition advantages from the government including tax holidays, import protection, and short or long term monopoly rights, as conditions required before the new investment will be made. Successive governments have felt obliged to accede to these demands, being concerned that the investments will not go ahead without it. Some instances of this can be seen in the case studies on national champions.

8. National Champions

41. Since independence in 1975, PNG has had a policy of supporting some national champions which are seen as of strategic importance to the national economy or to the effective operation and development of infrastructure. However, this is a relatively limited policy; PNG does not have any
significant number of statutory monopolies (though the size and nature of its economy means that there are many areas of natural monopoly) and the statutory monopoly protection or statutory market preference which does apply, has been diminishing in recent years.

42. This diminution is due to the introduction of general competition law and industry regulation in 2002 through the ICCC Act, described earlier. The general competition law (market conduct rules) in the ICCC Act have universal application across all industries in PNG, and also apply to government insofar as it carries on a business. There is provision for exemption from the application of the Act to acts which are specifically authorised by legislation, though such instances are rare.

43. More particularly, when competition law was introduced in 2002, the statutory frameworks supporting major utilities (such as electricity, water, telecommunications, ports and harbours and the like, which had until then been government owned and run state monopolies), were changed to allow competition in those industries, with a licensing regime for both the existing monopolists and any new competitors. Those utilities had by then been corporatised with the intention of their being privatised, though that privatisation has not generally occurred.

44. However, while competition is now permitted in most of these utility sectors, some of the utilities retained some statutory monopoly positions, at least for a limited time. As explained earlier, the utilities regulatory framework involves the ICCC setting long term price paths and service quality standards for the monopoly activities of these utilities, either through the ICCC Act or through price regulation under the Prices Regulation Act. Thus some of the utilities can be regarded as “national champions” because of their strategic importance to the national economy and social structure.

45. With the utilities reforms of 2002 it was intended that the statutory monopoly protection which the utilities retained, would be reduced over time until that protection was fully removed and those markets became fully competitive. It was hoped that at that stage the special regulatory arrangements regulating consumer price paths and specifying service quality standards may also be able to be removed, with regulation of prices and service quality for utility industries being driven by market forces and the general application of competition law.

8.1. Telikom PNG Limited

46. The best example of what has occurred since 2002 with utilities regulation and the continued protection of national champions in PNG is in the telecommunications sector, with Telikom PNG Limited (Telikom).

47. Telikom (originally the Postmaster General’s Department) was, in 2002, the sole licensed operator for fixed lines and also the sole licensed mobile (cell phone) operator. When the 2002 reforms were introduced, Telikom’s existing statutory monopoly was expected to continue for five years, ending in 2007. This monopoly was secured by the ICCC being prevented from issuing any competing fixed line carrier or mobile carrier licences until October 2007. It was anticipated that by that time, Telikom should have developed and improved its business and services to a point where it would be able to effectively compete with other mobile and fixed line operations, which would then be licensed to develop and operate new mobile and fixed networks in open competition with Telikom. It was felt that those five years’ additional protection from competition for Telikom, until 2007, should have been sufficient to protect Telikom, as a national champion, to allow it to then operate successfully in a competitive environment.

48. In December 2005, Government Policy changed, to require the introduction of two new competitors to compete with Telikom in mobile telephones after March 2006, while Telikom’s monopoly in fixed lines was to remain until October 2007. There is now active and vigorous competition between
Telikom and Digicel in the mobile market (the second new competitor not yet having commenced operations). However, attempts were made in 2006 and 2007 by some in government to reinstate Telikom’s monopoly in mobiles as well as fixed lines, on a permanent basis. These moves, which were strongly criticised at the time by the business and wider communities in PNG, were not successful in preventing Digicel from competing with Telikom in mobiles. However, Government Policy was changed in 2008 to, in effect, continue Telikom’s monopoly over fixed lines beyond 2007, and to legislate Telikom’s monopoly over international gateways (and thus monopolise all international telephone business) for an indefinite period until full competition is achieved.

49. This change in policy was explained as being necessary to enable Telikom, as the national champion in telecommunications, to continue to receive monopoly rents from fixed line and international telecommunications, to enable Telikom to transform itself into a strong and effective competitor. The Government has said that this is stage one of a two stage process leading towards open competition in international markets and, presumably, in all other areas including fixed lines. The Government has committed to the European Union that stage two, open competition (in international gateways at least), will occur during 2009.

50. Thus the national champion in telecommunications, Telikom, is continuing to receive government monopoly protection in fixed lines and international, though with the stated objective of moving into a fully open competitive environment in the future.

8.2. **PNG Power Limited**

51. The only other utility which has statutory monopoly protection is PNG Power Limited, formerly the Electricity Commission, though only in a limited way. Since 2002, persons operating electricity generation, transmission, distribution and retailing businesses have been required to be licensed by the ICCC and can operate in competition with each other. PNG Power has licences for each of those four activities. However, its electricity retailing licence is a monopoly in respect of those places which were supplied retail electricity by PNG Power in 2002 and which are still being supplied by it. In new areas for supply, PNG Power does not have any monopoly rights.

52. Thus electricity generation, transmission and distribution are fully competitive (though few licences have been requested or issued to anyone other than PNG Power), while PNG Power retains its retailing monopoly in those areas which it serviced prior to 2002, and new service areas are also open to retail competition.

53. There are no statutory monopolies for other utilities, though some retain effective natural monopolies.

8.3. **Air Nuigini Limited**

54. Air Nuigini, which is government owned, originally had an effective monopoly over scheduled air services domestically and internationally. For several years, Air Nuigini has faced competition on domestic routes from privately owned competitors, principally Airlines of PNG Limited, and in the last year or so Airlines of PNG has been competing with Air Nuigini on some international services. There are no statutory or legislated monopoly rights for Air Nuigini.

55. However, in recent months, the government, in promoting Air Nuigini as the national carrier, and in effect a national champion, has provided financial assistance to Air Nuigini on non-commercial terms, including by way of non-repayable grants, to enable Air Nuigini to purchase additional aircraft and, in at least one instance, giving a grant to allow Air Nuigini to continue to operate a seriously loss making international route.
56. While Air Nuigini enjoys no special statutory advantages over its competitors, the financial assistance given by the government to its national champion, air Nuigini has the capacity to distort competition in PNG’s domestic and international airline markets.

8.4. Major Oil and Gas Projects

57. There have been instances where the Government has chosen national champions for special treatment or exemption from competition laws, as an inducement to the development of projects in PNG involving oil and gas. In 1997, the then government agreed, as part of an arrangement for the construction of an oil refinery in PNG, to ensure that the refinery operator, InterOil Limited, would have an effective monopoly over the supply of fuel to all domestic fuel distributors in PNG. After the competition law was enacted in 2002, the government was obliged, by its project agreement with InterOil, to make a regulation exempting InterOil’s monopoly over supplying fuel to domestic distributors from the application of the competition law. This means that InterOil has an effective stranglehold over the supply, by imports or otherwise, of petrol, diesel and kerosene throughout PNG.

58. In 2006 when InterOil sought to acquire domestic fuel distributors in PNG which would give it a retail market share in excess of 60%, as well as its monopoly on supply to all distributors, the government submitted very strongly to the ICCC that InterOil’s acquisition should be authorised on public benefit grounds, notwithstanding the anti-competitive effects of the acquisition. That acquisition was authorised by the ICCC, largely on the basis of the government’s strong submission in favour.

59. In more recent times, the government has also granted exemption from various regulatory provisions, through amendments to several pieces of legislation, to a consortium headed by Exxon Mobil in relation to a major oil and gas exploration/production project in PNG. The exemptions include no price regulation over any products produced by the consortium (though most or all of that product would be exported anyway) and exemption from the essential pipeline access legislation which otherwise applies in PNG.

60. There is another major oil and gas exploration project under discussion in PNG involving InterOil, amongst others, and there is a probability that this project will also be granted a range of exemptions from the application of PNG law.

61. It is, of course, impossible to say whether these major oil and gas projects would have got off the ground if the exemptions they had sought had not been granted, but they do provide real life examples of the government picking national champions, albeit foreign owned, for special favourable treatment not accorded other industry participants in PNG.

9. Conclusion

62. The favourable treatment accorded these national champions may not be in the best interests of national industry policy nor in accord with best practice competition policy, however the circumstances of PNG’s economic and political development have forced the government to accord that special treatment to those particular enterprises.
CONTRIBUTION BY THE RUSSIAN FEDERATION
COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL CHAMPIONS

--Russian Federation--


2. This Concept contains tasks for development of social aspects and different sectors of economy, including raising of competitiveness of the Russian products on the global market. This envisages structural changes of industries and industry’s diversification. The major objective is moving to the high-technology-based economy.

3. The notion of necessity of competition threads the whole Concept. Therefore the balance of competition policy and industrial policy is seen with unaided eye.

4. What is more the Federal Antimonopoly Service (FAS Russia) provides on an annual basis the Report to the Government “On Competition in the Russian Federation” that addresses major challenges for competition development in all the sectors of economy, including oil and gas, power energy, transport, retail, construction and many others. Along with describing the current situation the Report contains specific actions to be undertaken to eliminate the threats for competition development and aimed at pro-competitive development of different sectors of the Russian economy. This Report is available online on the official web-site of the FAS Russia.

5. Along with this Report the FAS Russia together with the Ministry of Economic Development has elaborated the Program for Competition Development in the Russian Federation (to be adopted shortly), which covers the issues of threats to competition and means for their elimination, competition development in the sensitive and socially-important sectors of economy. Moreover, this Program contains proposals on competition policy improvement.

6. All the above mentioned documents determine the strategy of pro-competitive development of the Russian economy and ensure the balance of competition and industrial policy in Russia.

7. Moreover, the Russian Ministry of Industry and Trade has been elaborating a number of industrial sectors policies that determine the strategy of their development for the certain period of time. For instance these policies include:

- Development Strategy for aviation industry till 2015;
- Development Strategy for electronic industry till 2025;
- Development Strategy for shipbuilding industry till 2020, etc.

8. All of them have been adopted in compliance with the Russian legislation and procedure which means that all the interested state agencies are to agree on them. The FAS Russia has taken an active part in introducing competition principles to all of these documents.

9. The great load of the FAS Russia activity concerns natural monopolies regulation (gas and oil sector, railways, post, etc) aimed primarily at achieving the balance of consumers and natural monopolies.
interests that ensures availability for consumers of the sold goods and effective functioning of natural monopolies.

10. The FAS Russia has a number of successful implementations of reforms of monopolistic sectors in order to ensure their pro-competitive development, such as the one in power energy sector (which is considered to be the best one in the world from the competition perspective), telecommunications, railways, oil and gas sector, air transportation, etc. Usually in order to implement such reforms basic structural and institutional reorganisations are being conducted, fundamentals of the sector legal base meeting the market conditions are being formed, functions of state management and economic activity are being separated, a system of state regulation complying with the new conditions is being created.

11. Other tools of this state economic regulation is formation of rules on non-discriminatory access to the infrastructure of the natural monopolies and continuous activity on separation of potentially competitive and naturally monopolistic sectors which is based on the fact that natural monopolies were initially created as vertically integrated companies. It should be underlined that according to the law on natural monopolies constraint of economically justified transfer of the spheres of natural monopolies to the competitive market is prohibited.

12. The FAS Russia is also concerned with the growth of the price pressure on economy by natural monopolies due to their non-effectiveness. In order to settle this problem the FAS Russia suggests introducing significant amendments to the legislation on natural monopolies aimed at reduction of their costs, at toughening of state control over them (one of the options is to introduce the procedure of confirmation and agreement by all the state authorities of investment programs of the natural monopolies).

13. What is more the FAS Russia is truly concerned with threats to the competition development that are posed by creation of state corporations in various sectors of economy, which was explicitly described in the 2007 Annual Report of the FAS Russia to the Government of the Russian Federation. State participation in such entities leads to distortion of competition on the relevant markets.

14. To eliminate these concerns the following measures are considered by the FAS Russia as appropriate:

   a) Enhancement of competition control over public entities. Despite that public entities are created as non-commercial organisations they conduct economic activity and get profit, this is why they are fully applicable to the competition law. The competition authority has a right to get access to any information of public entities.

   b) Restitution of powers (bill drafting, supervising, control and enforcement) from all the public entities back to state and setting of legal prohibition for such delegation of functions.

   c) Expansion of using tender mechanisms by public entities under purchase of goods, works, services from private Russian companies. Practice of holding auctions for public procurement has shown high effectiveness of these market mechanisms.

   d) Ensuring transparent functioning of public entities for which is necessary to: determine clear criteria of assessment of their activity, introduce according to the principles of the administrative reform the system of indicators of their work, toughen requirements to report, modernise system of state statistic supervision over public entities and companies controlled by them.

   e) Introduction of moratorium on creation of new public entities until organising effective system of monitoring and control over activity of already existing entities, as well as their demonstration of their results.
 Adoption of regulation envisaging fixed amount of the state financial resources given to the public entity to eliminate opportunity of permanent state financial support to the public entities.

15. The Russian Federal Law №135-FZ “On Protection of Competition” does not contain any sectoral exemptions. However according to the provisions of the Article 13 of this Law the Government of the Russian Federation has the right to determine the cases of permissibility of agreements and concerted practices meeting the conditions stated in items 1 and 2 of part 1 of the present article (perfection of production, sale of goods or stimulation of technical, economic progress or raising of competitive capacity of the Russian goods in the world market; obtaining by consumers of benefits (advantages) which are proportionate to the benefits (advantages) obtained by the economic entities in the result of actions (inaction), agreements and concerted practices, transactions, other actions) (general exemptions).

16. Presently the Government of the Russian Federation is considering the adoption of the Resolution “On adoption of the list of block exemptions in respect of agreements (concerted actions) between economic entities” elaborated by the FAS Russia. This Resolution contains three block exemptions in respect of agreements:

- between buyers and sellers of products;
- between banks and insurers;
- on scientific and technical cooperation and joint use of the gained results of such cooperation.

17. However in order to ensure competition development in different sectors of economy the FAS Russia introduces competition principles to various sectoral legal acts (Water Code, Forest Code, laws on fishery, power industry, finance, etc).

18. Talking about the balance between the merger control and promotion of the so-called national champions as the tools of competition and industrial policies respectively, each case is considered carefully by the FAS Russia. And should the companies justify their merger as bringing more social and economic benefits the FAS Russia has no grounds to refuse it, according to the law.

19. For instance, the merger of OJSC “Volgaburmash” and OJSC “Uralburmash”, which are virtually the single representatives of Russia in drill bits production for oil and gas and mining industries respectively on the world market of drill bits, was thoroughly considered by the FAS Russia. Having analysed this market the FAS Russia gave its satisfaction on this merger. The FAS Russia came to the conclusion that this market in Russia, as well as in the whole world, is characterised by high concentration of production. The group of consumers of these two plants doesn’t practically overlap. And the merger of these plants would have a number of benefits in respect of enhancement of their positions on the global market. This merger would allow getting an access to cheap credit resources in order to increase capacities and to invest into the development of new products. Moreover there would be an opportunity to get a synergetic effect from optimisation of logistics, raw supply discounts and savings from research and development. As a result of the analysis the FAS Russia anticipated enhancement of competition by foreign producers. Moreover after the merger the Russian Holding could be rated on the 6th place in the world and occupy 13% of the global market under the scope of production and under the diversity of its product line the Holding could be on the 3rd place in the world which is consistent with the long-term strategy of development of Russia stated by the Government of the Russian Federation and will allow Russia to have an equal right in adopting new product standards on the market in future. The overall economic effect from reduction of costs is estimates as US $12,9mln annually.
20. Another illustrative merger case is the merger of OJSC “NLMK” and “VIZ-Steel” Ltd., two major producers of transformer steel, which was also satisfied by the FAS Russia due to its social and economic benefits for Russia. 90% of the produced transformer steel is exported and should the Russian companies lose their competitiveness on the foreign market the production of transformer steel will be ceased. The presence of Russia on the global market of high-technology metal products is considered to be as one of strategic priorities. At the same time taking into consideration that the European Commission does not limit the geographical borders of the transformer steel market by the territory of one country, the market of transformer steel in Russia is competitive. The major peculiarity of the Russian market is the horizontal integration of transformer steel producers due to the fact that their joint efforts aimed at development of scientific and technical base, development and introduction of new technologies provide for their competitiveness both on the domestic and global market of electric steel.

21. To sum up, the FAS Russia is not against creation of national champions but only in those sectors where it is justified and necessary for enhancing competitiveness of Russia on the global markets. What is seen as a means to restrain their negative impact are severe sanctions that are provided by the turnover fines, an opportunity to determine collective dominance on the market and the established procedure of compulsory separation of company’s activities.
CONTRIBUTION BY SLOVENIA
COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL CHAMPIONS

--Slovenia--

1. Introduction

The answer to the question why some countries are more successful than others in promoting their economic development is multi-dimensional and involves diverse aspects of the effects produced by advanced entrepreneurship and entrepreneurial culture and also by governmental industrial policy. Industrial policies differ across countries in terms of the aims they pursue and the measures and instruments they apply. They also vary in the achieved results. In any case, they should not overlap with competition policy aims and issues.

The outlines and goals of industrial policy are set in the frame of Slovenia's Development Strategy, including five development priorities with the corresponding action plans for the period of 2006-2013. The Strategy does not focus solely on economic issues but also involves social, environmental, political, legal and cultural issues. Due to such prioritisation of the objectives, it also serves as Slovenia's strategy of sustainable development. At the same time it integrates the Lisbon goals with the national settings, keeping Slovenia's specific development opportunities and setbacks in view.

2. History and evaluation

2.1 To what extent does the industrial policy in your country target firms on the basis of other nationality (e.g. by granting state aids/subsidies to national firms only or by controlling their ownership)? If so, how is nationality defined?

3. There is no specific legislation framework related to nationally targeted instruments of industrial policy. However, there seems to be an important restriction in controlling the ownership of state-owned companies. These restrictions derive from the fact that the State has, directly and indirectly via the two parastatal funds (Pension Fund and Restitution Fund), controlling shares in a number of important Slovenian enterprises.

2.2 What economic conditions have been associated with governmental industrial policy and support for national champions in your nation and region? Has this changed over time as economic development advanced?

4. Slovenia is a relatively young country. After independence and the period of privatisation, the country started the post-privatisation period with the key goal of economic growth. The EU accession strategy was created to define and outline a set of consistent medium-term economic policies required to complete the economic transformation and to prepare the economy for the accession to the EU.

5. To assist in accomplishing this aim, the state contributed towards creating a suitable climate for an accelerated development in the new private sector, facilitating the entrance of new enterprises on the market and improving the investment climate. Above all, the aim of economic growth asked for the strengthening of competitiveness in the enterprise sector.

6. High degree of internationalisation of the national economy requested considerable structural changes. Slovenia as a small market economy could hardly afford to provide the support of national industrial policy favourable to national champions. Foreign direct investment (FDI) deserved special attention in the reform of the enterprise sector which is a clear indicator of an open economy.
2.3 Are there major success stories of industrial policy or national champions that are prominent in policy discussions? Are there any perceived major failures of industrial or national champions policies? How do you define “success” and “failure” in this context? Are successful national champions stories supported by best practice competition policy standards?

7. There have been no major success stories of industrial policy or national champions.

8. As regards competition policy standards, existing measures in the frame of competition legislation provide for effective prohibition or control of actions which could potentially affect competition by abusing a dominant position and market power or cartels and other restrictive agreements.

9. In general, Slovenian competition legislation applies to all undertakings active in Slovenia. Such activity may be performed through establishment in Slovenia or through marketing products in Slovenia. Therefore, even companies established and merging outside Slovenia are required to notify the concentration if they sell the products in Slovenia and meet the set thresholds. When deciding on the approval of such a merger, the CPO would take into consideration only the geographical market in Slovenia and would be concerned mostly with local effects.

2.4 Does your competition agency use benchmarks to assess the economic costs and benefits of government intervention that promote industrial policy or national champions? Have you communicated benchmarks to other economic policy makers? Is there any dependable analytical approach that allows you to distinguish industrial policy from competition policy? Do you engage in competition advocacy in this policy area?

10. In Slovenia there are no specific rules or practices related to using benchmarks to assess the economic costs and benefits of government intervention that promote industrial policy or national champions nor a dependable analytical approach that allows to distinguish industrial policy from competition policy. From this perspective, competition advocacy activities play an important role. Competition Protection Office (CPO) is entitled to providing comments in the mandatory review process with regard to legislative proposals.

11. Moreover, competition advocacy is an important tool in the promotion of competition principles and market methods. Successful advocacy may contribute to a higher quality of regulation or to accelerate deregulation processes in situations where new market conditions do not lead to increased competitiveness of the companies.

2.5 Have merger review laws ever been suspended in your country? If so, why? Were concerns expressed either explicitly or implicitly about the way in which merger efficiencies are typically examined or in the way in which failing firms are analysed?

12. Merger review law has never been suspended in Slovenia nor was any concerns expressed about the way in which merger efficiencies are examined.

2.6 Have any of your decisions ever been overridden on grounds of Industrial policy? Are there any recent examples? What reasons were given? To what extent had the competition agency already considered the market characteristics or considerations that were the basis for the override? What have been the consequences of the override for consumers and competition policy?

13. None of the decisions of CPO has ever been overridden on grounds of Industrial policy. According to the existing legislation such a possibility is not provided.
2.7. Does your government implement some policies directly dedicated to innovation? If so, could you specify the sectors that benefit from these policies as well as the instruments used to foster innovation?

14. The central strategic research and development document in Slovenia is the National Research and Development Programme 2006-2010 (NRRP) which was adopted in 2005. The priority measures encompass also “further changes in industrial policy and the system of financing research activities so as to encourage cooperation between research companies and industry”. The important group of measures in the NRRP is included in the plans and documents related to the utilisation of EU Structural Funds resources.

15. Concrete measures to promote technical development and innovations are defined in the implementation programmes of the Ministry of Economy—Programme of measures to promote Entrepreneurship and Competitiveness. Measures are aimed at improving the ability to innovate of enterprises and for general support to innovations. Moreover, the importance of non-technological innovations is emphasised in addition to technological ones. The sub-program includes measures related to the innovation environment as well as direct incentives to enterprises to increase innovations in their operations. The measures are aimed at establishing and operation of an innovation environment and culture, promoting creativity and innovativeness of enterprises in all business areas, supporting growth of early-stage innovative companies and promoting various forms of linking.

16. According to the analysis provided in the Development Report 2008, innovation activity of companies increased significantly in 2004-2006 compared to the previous period, particularly in the services sector.

2.8. Did measures adopted in your country to deal with the recent economic crisis raise competition concerns? If so, could you describe the measures and the concerns? Have these competition concerns been taken into account, and, if so, how? In particular, have initial proposals been amended in order to comply with competition law? Have some of these measures been exempted from competition policy scrutiny?

17. Slovenia is facing the effects of the financial crisis and the cooling down of the economic environment both in the EU and globally. This affects the Slovenian economy in two ways: through the paralysis of the interbank market in the Euro zone and the decrease in export demand in all its key markets.

18. Economic policy measures, which follow the recommendations of the European Commission while considering Slovenia’s characteristic features as a small and open economy, apply to both aggregate demand and aggregate supply. The measures are intended for the financial and industrial sectors. In the financial sector, the Government seeks to maintain the trust of savers in the financial system and ensure credit activity and solvency. Measures with regard to industry are aimed at maintaining production facilities and jobs. So far, a key part of the measures was a subsidy scheme that would shorten working hours to below 40 a week in order to keep salaries unchecked and prevent the loss of jobs as a result of falling demand.

19. The adopted measures did not raise any competition concerns so far.

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1 Slovenia – Reform Programme for achieving the Lisbon Strategy Goals 2008-2010
3. Means and Goals

3.1 Please specify whether any of the following are instruments of industrial policy in your country:

- Government procurement
- Exemptions from antitrust laws
- Regulatory barriers to competition
- Access to credit
- Arranged mergers and acquisitions
- Control of acquisitions of national companies by foreign investors
- Other?

20. There are certain exemptions in the relevant public procurement laws provide for; however, they should not be attributed to the instruments of the industrial policy since they are related to public contracts which include classified information, or involving international agreements with other countries, financial services etc. Moreover, exemptions may be granted for entities operating in the water, energy, transport and postal services sector.

21. The provisions of PRCA-1 do not include any exemption from antitrust law. The only possible exemptions could be granted to agreements of minor importance which do not appreciably restrict competition (de minimis) and to agreements covered by the relevant EU block exemption regulations.

22. As regards control of acquisitions of national companies by foreign investors, existing measures in the frame of competition legislation provide for effective prohibition or control of actions which could potentially affect competition by abusing a dominant position and market power or cartels and other restrictive agreements. In general, Slovenian competition legislation applies to all undertakings active in Slovenia. Such activity may be performed through establishment in Slovenia or through marketing products in Slovenia. Therefore, even companies established and merging outside Slovenia are required to notify the concentration if they sell the products in Slovenia and meet the set thresholds. When deciding on the approval of such a merger, the CPO would take into consideration only the geographical market in Slovenia and would be concerned mostly with local effects.

3.2 To what extent are industrial policies in your country motivated or rationalised as regional or national economic development initiatives? Has this explanation been used more sparingly over time as your economy expanded?

23. According to the provisions of the Slovenia's Development Strategy, industrial policy measures are strongly motivated by national economic development initiatives. Among the key national objectives for the period of 2006-2013, the first priority is a competitive economy and faster economic growth, aiming at fostering entrepreneurship and increasing competitiveness.

24. The development issue was present more or less also in all the previous strategies, however, before they were more restructuring-oriented. For the time being, strategies are in line with the Lisbon Strategy goals as applied by the EU.

3.3 To what extent are industrial policies motivated or rationalised as an effort to help domestic firms withstand the exercise of market power by foreign firms? How does this rationale square with
rules against market distortions caused by state aids? How has your competition agency analysed these circumstances?

25. There were no formal circumstances where industrial policy would be motivated or rationalised as an effort to help domestic firms to withstand the exercise of market power by foreign firms.

3.4. Are industrial policies motivated or rationalised as a means to correct market failures in your country? If so, what types of market failures have been involved? How do you compare industrial policy or national champions with other policy approaches for correcting these market failures (such as taxes or subsidies on consumption of the product)?

26. Formally, industrial policy measures are not motivated as a means to correct market failures. Non-agricultural subsidies are gradually undergoing positive shifts – subsidies regarded as effective boosters of economic growth and development are gaining importance in the national budget (subsidies for technological development and small and medium-sized enterprises). The allocation of subsidies to recipients (especially for companies) was recently still problematic, mostly from the perspective of effectiveness of subsidies.²

3.5. Do you think that one nation engaging in industrial policy or supporting national champions attracts retaliation from other nations? To what extent are projected gains from industrial policy and national champions dependent on other nations not pursuing these policies, too? Do industrial policy and national champions constitute a “prisoners’ dilemma” situation?

27. Engaging in industrial policy or supporting national champions is certainly a two-fold problem. In case of market failures, there is no guarantee that the industrial policy measures would provide the necessary results or better results as the market itself. However, one should have in mind that there are specific situations where such measures are inevitable, but in any case these measures should be compatible with competition rules.

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² Development Report 2008
CONTRIBUTION BY SOUTH AFRICA
THE REGULATION ON RESTRICTIVE COMPETITIVE BEHAVIOUR
BY PUBLIC ENTERPRISES

--South Africa--

1. **Background**

1. The South African state, in common with most developing countries and a great many developed countries, pursued an active industrial policy in order to create the basis for industrial development. A wide range of instruments were employed as part of this industrial policy including direct state investment and ownership, tariffs and other protectionist measures, tax holidays and subsidies, procurement requirements and government supported mergers. It is probably a fair, if somewhat sweeping generalisation, to say that where basic industrial and commercial inputs were concerned the favoured instruments were direct government investment and tax subsidies, while where consumer goods were concerned tariffs were the instruments of choice. Direct government investment has underpinned dominant firms—‘national champions’—in, inter alia, steel, petro-chemicals, fertilisers, and large swathes of transport from fuel pipelines to passenger air transport. The South African state also invested in many industrial enterprises through the Industrial Development Corporation, a large industrial development finance institution established in the 1940s, that has also exercised a major influence on policy designed to support industrial development. In addition, in common with almost all countries, the state owned utilities in telecommunications and electricity.

2. We very briefly describe the evolution of state involvement in major industries before reviewing more recent debates around the role of industrial policy in South Africa and setting out the challenges that previous state support for industry poses for competition policy. Finally we sketch briefly some of the elements of what we believe are an effort to reduce the tensions which may arise between competition and industrial policy.

2. **Evolution of state involvement in major industries**

3. In the 1980’s and 1990’s, the South African government, again in common with many of its counterparts in the rest of the world, embarked on a process of economic liberalisation that included a lowering of tariffs and other barriers to international trade as well as the privatisation of important state owned enterprises, most notably those involved in petro-chemicals and steel. The first of these, Sasol Limited (“Sasol”), is now a significant multinational while the latter – Iscor Limited – has been absorbed into the ArcelorMittal South Africa Limited (“ArcelorMittal”) steel empire. Sasol and ArcelorMittal, the erstwhile state created and owned enterprises, dominate a great many of the critical domestic markets in which they participate. Other South African national champions – notably the dominant fixed line telephone company, Telkom SA Limited (“Telkom”), and the monopoly provider of electricity, Eskom Holdings, are still owned by the state.

4. The alcoholic beverages market is a clear example of a state sanctioned anti-competitive private agreement to support the creation of national champions in the beer and wine and spirits market. Here, in the 1970’s the state ignored the views of the Competition Board, a largely advisory body that preceded the contemporary competition statute and institutions, and allowed a market sharing agreement which, to this day, underpins dominant firms in each of the beer and wines and spirits markets.

3. **Recent debates around the role of industrial policy in South Africa**

5. Support for industrial policy has been maintained despite widespread dissatisfaction with the conduct of the state owned enterprises (“SOEs”) and former SOEs, those corporate entities that are justifiably characterised as South Africa’s ‘national champions’. Industrial policy over the past decade or
so has sought to pursue different objectives in the form of a more diversified and labour absorbing development path, and it has not used extended state ownership to achieve this, while there has also been far-reaching trade liberalisation. But, the established position of large former SOEs has enabled them to continue to benefit from state support such as tax holidays for major investments. At the same time, government has been largely ineffective in counteracting these interests. For example, South Africa’s telecommunication charges are generally agreed to be amongst the highest in the world and the population and the exceptionally energy intensive mining and minerals processing sectors have recently had to be bear the brunt of serious shortfalls in electricity capacity. Both entities are subject to relatively new, under-resourced and relatively weak regulatory bodies.

6. The former SOE’s, notably Sasol and ArcelorMittal SA, have been at the centre of several significant abuse of dominance investigations and several successful prosecutions. While it is wholly possible to argue that state investment was necessary for the establishment of these basic capabilities that underpinned a deep level mining and, later, a manufacturing economy, in their current incarnation these national champions are strongly associated with inefficiency and with abusive conduct, both exclusionary and exploitative. By way of example ArcelorMittal has been successfully prosecuted by a large gold mining company for contravening the excessive pricing prohibition in the Competition Act 89 of 1998, as amended (“the Competition Act” or “the Act”) and Sasol was successfully prosecuted for discriminatory pricing in contravention of the Competition Act although the latter decision was overturned by the Competition Appeal Court. Telkom’s monopoly was extended in exchange for a commitment to roll out fixed line telephone services to the rural and other low income areas – although it partly honoured the roll out commitments, it did so at prices too high for the newly connected consumers to afford and so before long the rate of disconnection exceeded the rate of new connection.

7. A product of the period of economic reforms – although with diverse roots and influences extending significantly beyond the imperatives of economic liberalisation – was a much strengthened competition policy regime, which included the promulgation of a new anti-trust statute in 1998 as well as the establishment of sector regulators in the telecommunications, energy and selected transport markets. While the reforms do evidence growing respect for market principles, the continued support for industrial policy, support which has been strengthened by the current global economic turmoil, has meant the possible tensions between these policy fields have been the subject of recent policy debates and analysis. These have highlighted the importance of dealing with the impact of anti-competitive conduct for South Africa’s economic development and, as such, the complementarities between industrial and competition policies. Sector specific policies of the Department of Trade and Industry for sectors such as metals, machinery and plastic products have also highlighted the negative impact of supra-competitive pricing of basic material inputs.

8. Support for industrial policy, specifically including national champions, is manifest in certain of the provisions of the Competition Act itself. Hence the promotion of employment, competitiveness and small and medium-sized enterprises feature alongside more orthodox consumer welfare objectives as explicitly stated ‘purposes’ of the Competition Act. The objective of supporting small and medium-sized enterprises played a significant role in the Tribunal’s decision in the matter of Nationwide Poles CC v Sasol Oil (Pty) Ltd. In this matter Sasol was found to have contravened the Act’s proscription of price discrimination. In its decision the Tribunal noted that it was required to take account of ‘an industrial policy that places the development of SMEs at the centre of attempts to improve the workings of the market mechanism.’ Although this decision was overturned on appeal, in its decision the Competition

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1 Note that the purpose of promoting international competitiveness provides that a purpose of the Act is ‘to expand opportunities for South African participation in world markets and recognise the role of foreign competition in the Republic’. (our emphasis)

2 72/CR/Dec03 - Nationwide Poles CC and Sasol Oil (Pty) Ltd
Appeal Court supported the Tribunal’s view that the Act required that the competition authorities take note of ‘the need to ensure that small and medium businesses are able to use the Act to protect their ability to compete fairly and freely’.

9. The insertion of industrial policy objectives in the Competition Act extends beyond the general purposes of the statute.

10. Section 10 of the Act provides that the Competition Commission may exempt a firm from the application of the chapter of the Act which proscribes anti-competitive agreements and abuse of dominance if the agreement or practice contributes to the promotion of exports, to the competitiveness of small businesses, to changes in productive capacity necessary to prevent the decline of an industry, or to the economic stability of an industry designated by the Minister of Trade and Industry. Note that only the Competition Commission is entitled, with a right of appeal to the Competition Tribunal, to grant an exemption. The Minister has no decision making function with regard to applications for exemption.

11. While the number of exemptions granted is small, as might be expected a number of those that have been granted do indeed promote the core industrial policy objective of international competitiveness, if not competition, although it is not immediately apparent that any of these exemptions severely compromise competition. Indeed even when granting an exemption the Commission attempts to carefully design the exemption so as to maintain competition to the greatest extent possible. However, clearly in order to have qualified for exemption the exempted conduct would have to constitute a contravention of the Act. For example, the Commission conditionally exempted a geographic market sharing agreement between Qantas (the Australian airline) and South African Airways (also a state owned ‘national champion’) on the grounds that the exemption promoted exports and allowed for a change in productive capacity necessary to stop decline in an industry.

12. The merger provisions of the Act similarly require the competition decision maker to take account of industrial policy objectives. Hence when deciding a merger the relevant competition agency – the Tribunal in the case of mergers above a specified threshold and the Commission in respect of those falling below the threshold – is required to decide whether the merger is likely to give rise to a substantial lessening of competition, and then, regardless of the outcome of the competition evaluation, to determine the transaction’s impact on a specified number of public interest grounds, which include the standard industrial policy objectives such as the transaction’s likely impact on region or sector, on the ability of small businesses to become competitive, and on the ability of national industries to compete in international markets.

13. It is important to note that the relevant competition authority is the only decision maker, including in the assessment of the public interest impact of the merger. Neither the Minister nor any other executive structure is entitled to override the competition authorities’ decisions. A ministry or department of state may make representation to the Commission and the Tribunal and, on several important occasions, have done so, but the decision making prerogative resides solely with the competition authorities. This, and the fact that the competition evaluation precedes the public interest assessment, ensures that, while the industrial policy objectives are seriously treated, they are assessed by competition professionals through the lens of the competition evaluation. This may help explain why, although the public interest assessment has occasionally resulted in the imposition of a condition (usually centred on the employment impact), they have never been dispositive in the decision whether or not to approve or prohibit a merger.

3 49/CAC/Apr05 - Sasol Oil (Pty) Ltd and Nationwide Poles CC
4 Government Gazette No. 30805, 29 February 2008
14. In short, the insertion into the competition statute of industrial policy objectives alongside orthodox consumer has not materially compromised the attainment of the core competition objectives. Nor, we believe, does this place our work outside of the mainstream of competition enforcement and adjudication. Evoking international competitiveness and scale economies in merger assessments, whether under the guise of public interest or efficiency, is standard practice in most jurisdictions with which we are familiar. The critical difference between our practice and many, if not all, other jurisdictions, is the explicit inclusion of social and industrial policy objectives in the competition statute, the transparent manner in which the public interest is weighed against the competition impact, and the fact that it is the competition authority, rather than a minister of state, that is the decision maker even on public interest matters.

15. This is not to say that the inherent tension between industrial policy and competition policy has been eliminated, particularly in those instances where industrial policy seeks to selectively promote the interests of particular enterprises. Indeed the current economic crisis has, if anything, strengthened the hand of those who support a leading role for the state in the attainment of economic objectives. Nor is this surprising – for those competition fundamentalists who have consistently denied the prevalence or impact of market failures, the financial crisis is clearly a salutary lesson. However, the financial crisis has ineluctably become the basis for demand state support and intervention in favour of national firms. Certainly in South Africa it has become the basis for demanding state support for a range of enterprises and sectors whose woes owe more to decades of state protection and its handmaiden, inefficiency, than to the impact of the economic downturn. Faced with the opportunism that underpins these demands for support, the competition authority can do little other than use its advocacy tools and its public profile to warn of the dangers inherent in undermining market processes and to warn against a conveniently distorted interpretation of the concept of market failure, one that views every unsuccessful firm or sector as the victim of market failure rather than of inferior products and supra-competitive cost structures.

4. Efforts to reduce the tension between competition policy and industrial policy

16. However, the South African authorities are attempting to take a more positive and constructive approach to industrial policy, than that of the market fundamentalist ‘nay-sayer’. We sketch briefly some of the elements of what we believe are an effort to reduce the tension between these important fields of economic policy:

17. Firstly, there are unquestionably industrial policy instruments and programmes that are, at worst, neutral with respect to the attainment of competition policy objectives. These are industrial supports that are far from market and that are directed at strengthening generic industrial capabilities as opposed to those that privilege particular firms. Human resource development and general support for research and development are clear examples of this. Where support is extended to particular enterprises it should be done as the outcome of a competitive and transparent process in which the criteria for support are clearly specified. The criteria should emphasise the prospective recipient’s prospect for future success rather than need. Furthermore, industrial policy support should always be accompanied by a clearly specified exit strategy for the provider of support. It is imperative that the competition authorities participate actively in the debate surrounding industrial policy and that they advocate for competition-friendly industrial policies.

18. Secondly, it is imperative that the competition authorities do not conduct themselves in a manner that suggests that they are anti-big business. Indeed it is important that their work evidences the incontrovertible truth that has taught generations of anti-trust enforcers that the overwhelming majority of mergers do not raise competition concern and that the merger process is an important aspect of the process of economic restructuring process. Similarly its prosecutorial strategies and decisions must give
expression to the learning that holds that many vertical agreements and, indeed, instances of unilateral conduct are efficiency enhancing.

19. Third, the credibility of the competition authorities rests on being effective in addressing anti-competitive conduct and rigorously evaluating mergers that raise competition concerns. This is particularly the case in economies with conditions for sustained cartel conduct and abuse of dominant positions. Recent cases of cartel conduct in various food products have demonstrated how the far-reaching liberalisation of government controls in 1996 was undermined by private regulation by the food processing companies. The support for market oriented economic policies requires vigorous enforcement against such conduct. In this regard, it is important to recognise that small markets are particularly vulnerable to anti-competitive unilateral conduct. Hence there is a legitimate role for the competition authorities in ensuring that entry barriers are as low as possible and that SMEs are able to survive. The ‘protection of competition not competitors’ mantra rings hollow where a great many markets are characterised by the absence of competitors and hence competition. It has been suggested that industrial policy should, wherever possible, avoid supporting dominant firms but should rather focus its attention and resources on second tier firms and new entrants. It is of course possible that second tier firms remain at that level because their offerings are inferior to the first-tier firms. But it is also highly conceivable that certain of these firms are stuck in the second tier because of the structure of the market and the conduct of its dominant participants. Where the conduct of the dominant firms is impeachable then vigorous prosecution must follow, but where the dominant firms are privileged by non-competition events and policies of the past – for example a previous history of state ownership – then there is a prima facie case for directing assistance at those that have not been beneficiaries of this historical privilege.

20. Fourthly, the competition enforcer would be well-served in this debate by a prosecutorial strategy that is clearly seen to be generating positive outcomes from an efficiency and poverty alleviation perspective. For example, the South African Competition Commission, has identified bid rigging in public tenders as an important priority area, and under that rubric, construction and civil engineering as markets that require close scrutiny. The context for this is a government economic policy that has identified public investment in infrastructure as a pillar of its growth strategy and that is committed to massive infrastructural spend in support of the 2010 FIFA World Cup. By focusing on bid rigging, the competition authorities are demonstrating the positive contribution that competition policy can make to a pillar of the state’s economic and industrial policy.
CONTRIBUTION BY SWITZERLAND
COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL LEADERS

--Switzerland--

1. Introduction

1. First of all, it is important to note that industrial policy can not only be pursued by giving state aids or subsidies. Regulatory measures such as giving monopoly rights in certain areas to certain companies that are also active in other geographical and/or product markets can create distortions that benefit or harm one or several companies. Even subtle regulations such as safety standards or other declaration requirements can influence competition in a way that one or several companies or a sector is treated preferentially in the market. So, when subsidies or state aids between countries are compared, these comparisons should always be taken with care as states with a low level of obvious financial advantages for certain companies or sectors can as well pursue an industrial policy with more subtle means.

2. The Swiss approach to industrial policy and national champions

2. Switzerland does not pursue an explicit industrial policy. Although we are aware of arguments such as the “infant industry” or “cluster” argument, we still believe that it is a risky or even unaccomplishable task for the government to select in advance certain sectors, products or companies that are supposed to be successful in a competitive market in the future. A competitive and undistorted market is probably the best way to have selected companies and sectors that are promising also in an open and internationalised market.

3. There are several reasons that accrue for the difficulties for the state to select companies and/or sectors that are successful in the future:

   - Many sectors, especially high-tech sectors, are subject to rapid technological development and innovations. These developments and innovations are unknown to the in advance to the state and even to market players. Today’s promising technologies could be worthless tomorrow – ruled out by even better new technologies or changed preferences.

   - Comparative advantages are not very well known to government and these advantages can change over time or with the opening of new markets.

   - The two bullets above amount to risks that are – to our experience – much better managed by private investors than by the government.

4. The statements above do not mean that government has no role at all in industrial policy. On the contrary, we believe that it is the State’s and especially the competition authorities’ task to work towards financing and regulations that are not distorting competition so that the most efficient companies and sectors are successful in the market.

5. Sometimes, industrial policy is mistakenly argued as an instrument to protect existent companies’ structures in rapidly changing markets. We believe that such a policy is costly and that other means are more successful in the long run to generate wealth in a globalising market. Instead of benefitting selected companies or sectors, the state should create a framework that is beneficial in general for economic activity and competition:

   - A low tax level for all companies and sectors is very beneficial for attracting new companies in strong international competition.
• A low level of administrative burden allows companies to save time and money, to adapt to new challenges and to get a competitive advantage over their competitors.

• A flexible labour market is the most important tool to allow companies and workers to adapt efficiently to new economic challenges and developments.

• Unemployment insurance combined with further training and education allows unemployed people to adjust to market needs.

• Contributing to non-sector specific research and regulations that promote innovative activity are important measures as well.

6. All the measures listed above are important tasks for the government. They can be design non-distortive to competition and if so, we believe that such a policy will usually be economically more successful than a policy that tries to pursue targeted industrial policy.

7. The same conclusions are valid for the issue of national champions. Switzerland is in open country for foreign investment and hosts dozens of large multi-national companies. Switzerland does not significantly influence its companies in merging or not merging or collaborating with selected or national companies. We believe that this strategy has contributed to creating wealth and exchange of knowledge across borders.

8. This approach is also reflected in Switzerland’s competition policy: The Swiss government has so far never used the option for a so called government exemption: It has never overruled competition agency decisions so far.

9. The Swiss cartel law does neither provide for general exemptions of competition law, with the exception for bank failures: In such a case, banking regulation prevails as systemic risks must be excluded. Exceptions such as systemic risks or special economic situations with very large employers at temporary are very rarely applied in Switzerland.
CONTRIBUTION BY CHINESE TAIPEI
COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL CHAMPIONS

--Chinese Taipei--

1. This submission briefly explains the development of Chinese Taipei industrial policy and its relationship with competition policy.

1. Industrial Policy of Chinese Taipei

2. Small and medium size enterprises (hereinafter “SMEs”) averagely accounted for above 98% of 1.2 million enterprises in Chinese Taipei in past years. The effective industrial policy implemented by the Ministry of Economic Affair, which is the competition agency of national economic development and industrial policy, is the key to ensuring economic growth and welfare of a nation. In 1980s, the business environment in Chinese Taipei changed as wages rose and the New Taiwan dollar appreciated against the US dollar. Labour and land costs increased dramatically for industrial use. At the same time, people became more aware of environmental protection issues resulted from the high-degree pollution industries. These economic challenges made the government started to promote the development of strategic industries that were characterised by a high level of technology, high value added and low energy consumption. With the establishment of the Hsinchu Science-based Industrial Park to facilitate the development of hi-tech industries, enterprises were encouraged to step up their R&D activities, improve productivity and quality, and enhance their international competitiveness.

3. When global and regional organisations became increasingly important, Chinese Taipei gradually lost its competitive advantage in labour-intensive products with low added value. The government implemented new industrial policies, including stimulating R&D by tax incentives, encouraging automation of production as well as pollution prevention, providing labour training programs so as to improve the upgrading of domestic industry in 1990s.

4. Since Chinese Taipei joined the WTO in 2002, the economic environment has become more liberalised, making it a part of the global industrialised system. The government has disclosed its intention to build Chinese Taipei into a Green Silicon Island, thus revealing its vision for national development in the new century. The project was expected to deliver economic benefits by promoting Chinese Taipei as global logistic centre, developing knowledge-based economic, stimulating conventional industries, creating R&D centres in Chinese Taipei by foreign corporations, and setting up in Chinese Taipei of local innovation and incubation centres for SMEs. The core value of the industrial policy in 2000s is to lead businesses towards a high value-added industrial era featured by innovation, invention, and R&D on the foundation of the past achievements in semi-conductor industry.

2. Policy of National Champions of Chinese Taipei

5. Apart from industrial policy of promoting the development of SMEs, Chinese Taipei has supported the policy for national champions in financial industry since 2001 financial reforms. Although Chinese Taipei was relatively unscathed during Asian financial crisis broke out in 1997, rising non-performing loans (hereinafter “NPL”) ratios and an over-banking issue increasingly became the major concerns of sector regulator, the Ministry of Finance (hereinafter the “MIF”), thus the MIF adopted financial reform project from 2001.

6. The first phase of financial reforms adopted measures to reduce NPL ratios, encouraged merger activities to prevent from over-competition in banking sector, created strong financial supervision by establishing Financial Supervision Commission (hereinafter the “FSC”), deregulated market restraints by drafting and promulgating new laws and their amendments.
7. As a result, there were 14 financial holding companies established, 58 banks engaging in trust business, and 26 merger cases involving 61 financial institutions completed to build up a favorable banking environment. Concerning the banking industry has been too fragmented, too homogenous, and overly competitive, the FSC stepped in the second phase of the reform in 2005 to further consolidate banking companies. The FSC hoped to create one or two leading domestic player in the financial service industry, or what the FSC calls "national champion" banks to play a role in the international financial market after the reform.

3. Competition Policy and Advocacy

8. At the time of the industrial policy focusing on changing industrial structure in 1990s, the government promulgated the Fair Trade Law (hereinafter the “Law”) in 1991, began to bring more attention on the merit of competition culture in industries.

9. The Fair Trade Commission (hereinafter the “Commission”) initiated a task force to review over two hundred already existing relevant laws and regulations, which might have conflicted with the competition policy in 1993 and 1996. The performance of the project in 1996 was reported to the Cabinet for further consultation with sector regulators. However, owing to a lack of sufficient support from the Council for Economic and Planning and Development under the Cabinet which is in charge of deregulation policies, the Commission then proposed an amendment to Article 46 of the Law so as to affirm the status of the Law as the fundamental economic law and as the basis for harmonising competition and industrial policies.

10. To resolve the conflicts arising between different policy measures, Article 46 of the Law was amended to state: “Where there is any other law governing the conduct of enterprises in respect of competition, such other law shall govern, provided that it does not conflict with the legislative purposes of this Law.” The purpose of this amendment is to ensure that any business conduct related to competition will adhere to the spirit of the competition law.

11. In addition to the mandate, Article 9 of the Law is the statutory foundation that calls on the Commission to cooperate with and advise other agencies regarding the impact of other policies.

12. Meanwhile, with the 1999 amendment to Article 46 of the Law, the Commission participated in the project of “Green Silicon Island Vision and Promotion Strategy” under the Cabinet and then the Commission established a task force which was referred to as the “Project for the Review of the Enforcement of the ‘Green Silicon Island Vision and Promotion Strategy’ Regulations” in July 2001.

13. The Commission providing guidance and consulting with the relevant government agencies by comprehensively reviewing laws and regulations that were impeding competition, the results were reported to the Cabinet in August 2003. At that time, more than ten different sector regulators governing more than thirty-one laws and regulations had not yet committed themselves to adopting the alternative pro-competitive laws and policies. Following further negotiations with the sector regulators in charge of such policies, 8 rules with anti-competitive effects were still pending, with half of them being related to the mandates of some professional associations to stipulate remuneration standards in charters.

14. The Commission has organised a task force to evaluate and promote the application of the OECD competition toolkit beginning with the first season of 2008. Two Commissioners of the Commission co-chair the “Competition Assessment Task Force.” The team followed the analysis process of the toolkit to evaluate the competitive effects on two selected government policies and planned to publish the cases with the major content of the toolkit in traditional Chinese for future competition advocacy purposes.
Hopefully, through the practice, the Commission based on its past experiences of regulatory reform will find out the most appropriate methodology for competition advocacy.

4. Questions for Consideration

4.1. History and Evaluation

Q5. Have merger review laws ever been suspended in your country? If so, why? Were concerns expressed either explicitly or implicitly about the way in which merger efficiencies are typically examined or in the way in which failing firms are analysed?

15. In an effort to minimise the number of exclusions at least to the extent that is still in line with the legislative purposes of the Law, the Commission adopts the most appropriate strategy to deal with each kind of “exemptions”.

16. Turning to explicit exemptions, although the Law applies to all sectors with no exception in Chinese Taipei, there are statutory exemptions applicable to mergers in the banking and insurance industries under certain circumstances:

- Article 62 of the Banking Act stipulates that if a bank is insolvent or has the risk of injuring depositors’ interests as a result of obvious adverse changes in its business or financial status, the central competent authority may order it to suspend business and take resolution measures, may suspend part of its business, may send officials to supervise or take over operations or may take other necessary actions. Article 62-4.4 further provides that if the competent authority determines that it is necessary to proceed with a transfer immediately and that there will be no serious and adverse effect on market competition, approval by the Commission under Paragraph 1, Article 11 of the Law shall not be required.

- Article 19 of the Financial Holding Company Act stipulates that if a financial holding company, a bank subsidiary, an insurance subsidiary or a securities subsidiary of a financial holding company is insolvent, or after adjustments, has a negative net worth on account of adverse changes in its financial or business conditions, and if the Ministry of Finance determines that immediate measures are necessary and that such measures will not result in unfair competition in the financial market, Article 11 of the Law shall not apply, and an application to the Commission will not be required for that financial holding company to: 1. merge with any company referred to in Paragraph 1, Subparagraph 1 or Subparagraph 2 of the preceding Article or transfer all of its rights and obligations to any said company or assume all the rights and obligations of any said company; 2. permit the same person or same concerned person to hold shares representing more than one-third (1/3) of its voting rights; or 3. be established as a result of a transfer from a financial institution.

- Article 13 of the Financial Institutions Merger Act stipulates that in the event that the business or financial status of its credit department obviously deteriorates, a farmers or fishers association cannot meet its liabilities or its net value after adjustment becomes negative, the competent authority may, if deemed necessary, and after consultation with the central competent authority in charge of farmers or fishers associations, order that association to assign its credit department and the property required for its operations to a bank. Where the competent authority deems it necessary to take emergent measures and where such measures would not have any material adverse effect on competition in the financial market, the bank is exempted from applying to the Commission for approval in accordance with Paragraph 1 of Article 11 of the Law.
Article 149-7 of the Insurance Act stipulates that when an insurance enterprise organised in the form of a limited liability company by shares assumes the operations, assets or liabilities of another insurance enterprise, where the competent authority deems that there is a need for urgent measures and there will be no material adverse impact on market competition, the requirement to report a business combination to with the Commission under Paragraph 1, Article 11 of the Law shall be waived.

Q6. Have any of your decisions ever been overridden on grounds of industrial policy? Are there any recent examples? What reasons were given? To what extent had the competition agency already considered the market characteristics or considerations that were the basis for the override? What have been the consequences of the override for consumers and competition policy?

17. There is one case illustrating that decisions of the Commission could be overridden on grounds of industrial policy.

18. The Commission had long been aware that some laws regulating professionals required that the charters of the individual trade associations set fee standards for certain practices—for example, fees professionals may charge and fee schedules applicable by type of service. In some cases, the trade associations had to submit their fee standard proposals for the regulators’ approval. Since professionals cannot practice without membership in their own trade associations, the fee standards stipulated in the trade associations’ charters in effect would decrease significantly or even eliminate the possibility of price competition in their respective markets.

19. Since these charters are authorised by relevant laws and have existed for quite a long time, to avoid the potential problems of conflict in jurisdictions and uncertainty over laws, the Commission decided to consult with the relevant regulators before taking any formal actions against those trade associations. In 1999, the Commission met with the Ministry of the Interior, the Ministry of Finance, the Ministry of Justice and the Public Construction Commission to discuss whether the price standards in the trade association charters for architects, accountants, lawyers and technicians were in violation of the Law. Soon thereafter, the Commission concluded that the trade associations had undoubtedly been engaging in concerted actions, and, as a result, it forwarded its formal opinions to the relevant regulators as well as the trade associations to clarify its position in its implementation of the Law. The Commission advised those government agencies to revise the relevant laws and required that the relevant trade associations eliminate all provisions for setting fee standards within a year.

20. In 2001, the Commission found that none of the responsible government agencies had proposed a draft to revise the relevant laws. Of the trade associations for whom the agencies were responsible, some had urged their members not to adhere to follow the fee standards stipulated in their charters, but most architects’ trade associations strongly refused to comply with the Commission’s requirements. Further communications with the architects’ trade associations were undertaken but simply to no avail. Finally, in 2003, the Commission issued the three largest architects’ trade associations orders requesting that they not only stop using fee standards but also repeal the relevant provisions in their charters at their next general meeting.

21. In the same year, the three architects’ trade associations appealed the Commission’s decision to the Cabinet, the highest administrative body, and the end result was that the Cabinet turned down the Commission’s decision. This was based on the fact that: 1) it was not clear whether the fee standards were actually affecting the market’s function; 2) the fee standards could not be effective without the regulator’s permission; in other words, the trade associations did not make the final decision; and 3) Article 9 of the Fair Trade Act stipulated that for matters provided for in the Act that concerned other authorities, the
Commission could consult with those other authorities to deal with the issue. The Commission is still considering whether there is a need to raise the issue with the Ministry of the Interior in the future.

22. This was the first time since the amendments to the Law that the Commission had tried to deploy its power against anti-competitive behaviour granted by another authority. The fact that its enforcement effort was not well received by the highest administrative body has caused the Commission to slow down its pace in trying to repeal existing laws which go against the legislative purpose of the Law.

23. The amendment to the Architects Law drafted by the Ministry of the Interior has recently been proposed to the Cabinet. The Commission has been invited to provide comments on the provisions designed to retain the power of architects’ associations to set minimum fee standards. The architects’ trade association has stated that setting a fair fee standard would possibly balance the asymmetric market position between architects and consumers, and would further ensure the quality of the resulting construction. On the other hand, since considering setting a standard service charge is not the only way of guaranteeing security, and inferior quality does not necessarily result from price competition, the Commission has proposed a draft amendment to the Architects Law that will delete the power of the association to set the fee. By so doing, the Commission asserted again that such conduct is in breach of the Law under any circumstances.

24. After the consultation held by the Cabinet, it has been decided that the new amendment will directly require the Ministry of the Interior, the sector regulator, to set the fee standard on the basis of the recommendations of consumers and stakeholders. The amendment has yet to be proposed to the legislators.

4.2. Means and Goals

Q1. Please specify any of the following are instruments of industrial policy in your country:
- Government procurement
- Exemptions from antitrust laws
- Regulatory barriers to competition
- Access to credit
- Arranged mergers and acquisitions
- Control of acquisitions of national companies by foreign investors
- Other

25. Any instruments from the above could reach the industrial policy goals in Chinese Taipei.

REFERENCES

CONTRIBUTION BY UKRAINE
COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL LEADERS

--Ukraine--

1. Introductory notes

1. The analysis of reference of competition policy to industrial policy requires, first and foremost, determination of their objectives.

2. The objectives of the competition policy, in our opinion, may be defined as formation of the product market functioning conditions to provide triple efficiency due to effect of competition mechanisms: allocative efficiency, that is efficiency of resources distribution; efficiency of resources use, or X-efficiency after Harvey Leibenstein, and dynamic efficiency or adaptive efficiency, that is efficiency of forming new resources, first of all, competence and skills.

3. In turn, the objectives of the industrial policy include provision of development of specific industries, which implies expansion of production capacity, sale of the relevant products and improvement of their quality.

4. As one of the main ways to achieve the objective of the industrial policy lies in scientific and technical progress, that is formation and use of new resources, the objectives of the industrial policy actually coincide with the objectives of the competition policy to the extent of providing adaptive efficiency by the latter.

5. At the same time, ensuring allocative efficiency implies maximal approximation of markets functioning to the model of perfect competition with the following essential features: setting prices at the level of marginal costs, dispersive market structure (low level of market concentration), absence of entrance barriers, full independence of economic agents and equal business conditions. However, according to proponents of the influential theoretical school connected first of all with the name of Joseph Schumpeter, the aforesaid perfect competition model is unable to ensure adaptive efficiency. So, there is some discrepancy not only and not just between competition policy and industrial policy, but rather between the priorities of the competition policy, depending whereon the competition model shall be determined (perfect competition versus symmetrical oligopolistic model versus asymmetrical oligopolistic model or model of national champions) to the utmost extent compliant with the needs of development of competitive economy at the specific moment.

2. Ukraine’s experience

6. In Ukraine, as at the time of recovery from the transformational crisis (at the turn of 1990s and 2000s), several types of markers were formed (from the point of view of competitive conditions): markets with high competitive structure, markets with oligopolistic structure, markets with domination features, monopolised markets.

7. At the stage of recovery from the crisis, the most successful development indicators were shown by branches with formed oligopolistic structure. This is first and foremost connected with the fact that concentration of material and staff resources in the framework of industrial and financial groups, and opportunity to pursue active protectionist policy in own interests on the part of the state, formed conditions for the branches they operated in for the fastest recovery from crisis and provide stabilisation and entire economic growth. This particularly concerned iron-and-steel industry. Markets of this branch are typically oligopolistic (in 2004, 60 per cent of ferrous metals production was covered by 5 producers, the share of the biggest one was 21 per cent). In 1995, steel production constituted only 42.4 per cent compared to the volumes of 1990, but already in 1996, the decline in production was overcome, and in 1996-1999, steel
production grew by 22.9 per cent, production of rolled ferrous metals grew by 29.8 per cent. The growth continued further: in 2000-2004, steel production grew by 12 per cent, and in general for 1995-2004, it grew 1.55 times (average growth rate: 15 per cent). Ukraine was ranked the world’s 5th steel exporter.

8. By analogy, production of motor petrol and fuel oil, which in 2000 was only 22.7 per cent compared to the volumes of 1990, in 2000-2004 grew 2.3 times upon formation of several large vertically integrated structures in the field (in 2004, the largest 5 structures covered 78 per cent of production). Production of beer, 88 per cent of which in Ukraine at the beginning of 2000 belonged to 4 business entities, from 1997 to 2001, grew in kind 2.16 times. Record growth rates in 2000-2004 were shown by the volumes of mobile communication services provided in Ukraine mainly by 2 large providers: services scope in money terms grew 6.8 times within this period.

9. It is important to note that in 2005-2007, 58.5-69.8 per cent of costs for innovation in production sector fell on 200 biggest enterprises while 54 thousands enterprises was covered only by 41.5-30.2 per cent of such costs.

10. At the same time, high rates of economic growth were observed in a number of industries, in which competitive environment was formed. The production growth rates in food industry in 2000 compared to 1999 constituted 26.1 per cent and twice exceeded the relevant general indicator of the country’s industry, in light industry: 39.0 per cent, wood processing and pulp and paper industry: 37.1 per cent. In 2002, production growth rate in meat industry 4.6 times exceeded the industry’s general indicator, in wood processing – 3.8 times, in vegetables and fruit processing – 3.5 times exceeded the industry’s average indicator.

11. Low efficient business practices were demonstrated by monopolised branches of economy. For instance, the revenue from railway cargo transportations in 2001-2003 grew more than twice, but in kind they grew only by 27.5%. Physical volume of services on production and distribution of electric energy, gas and water for the same period grew by 8.6 per cent, though the revenue from them grew by 25 per cent. In the postal area in 2001-2002, revenue for rendering of services grew more than twice, and the scope of services in kind grew only by 2.1 per cent.

12. The attempts to achieve the objectives of the industrial policy by way of granting exclusive rights and preferences to individual business entities proved to be inefficient. In particular, in automobile production, which faced deep crisis (in 1997 compared to 1990, the number of light motor vehicles produced in Ukraine reduced 78 times), under the Law of Ukraine «On stimulation of automobile production in Ukraine» adopted in 1997, individual business entities acquired exclusive preferences. As a result, actually, in 1998, production of light motor vehicles grew 12.9 times, but in the same year, the foreign investor, which acquired these exclusive rights, became bankrupt because of the East-Asian financial crisis and in 1999, production of light motor vehicles in Ukraine again reduced 2.7 times. In 2001, the main provisions of the Law of Ukraine «On stimulation of automobile production in Ukraine» to the extent of providing exclusive preferences to an individual producer was cancelled. After that, in 2002-2004, production of light motor vehicles in Ukraine was performed at high rates, and in 2004, its volume 11 per cent exceeded the indicator of 1990. In 2006, the largest national producer covered nearly a half of the internal production of light motor vehicles, the 2 following ones covered nearly a one-fourth thereof.

13. We should note that advantages shown by the markets with oligopolistic structure at the stage of recovery from the crisis, at the stage of Ukraine’s economy stabilisation (2004-2007) were to considerable extent lost. Consequently, the annual average growth rate in steel production for this period constituted only 0.11 per cent, the annual average growth rate of rolled ferrous metals and coal production: 0.43 per cent; in production of motor petrol and fuel oil aggregate reduction occurred, which constituted respectively 2.3 and 9.8 per cent a year. At the same time, a number of branches, whose markets had
competitive structure, showed in 2004-2007 stable production growth rates: for example, wood processing industry: 20.3 per cent a year, pulp and paper production and editorial activity: 14.8 per cent a year, production of meat and meat products: 14.6 per cent a year, food-taste industry: 11.5 per cent a year. In a number of cases, the Antimonopoly Committee revealed the behaviour bearing traces of monopolistic pricing in these fields. In the markets of some oil products and metallurgical industry, there were cases, when business entities simultaneously operating in external markets and facing considerable competition, and in the internal markets bearing marks of collective or individual domination, set internal prices at the level being considerably higher than external ones, thus doting promotion of their products in the external markets.

14. Export-oriented branches, for which markets with oligopolistic structure dominated, showed the lowest stability at the first stage of financial crisis of 2008: in metallurgy, in September 2008, decline in production compared to 2007 was 19.1 per cent, in coal production: 15.6 per cent, in oil processing: 20.7 per cent. At the same time, growth was observed in branches characterised by competitive market structure such as wood processing, pulp and paper production and editorial activity.

3. Preliminary conclusions

15. Experience available in Ukraine allows making the following preliminary conclusions in respect of reference of competition policy to industrial policy:

- Successful industry development implying availability of any model-based competition;
- At the stage of recovery from the structural crisis, efficient industry development may be contributed by the competition model implying symmetrically oligopolistic market structure;
- Similar competition model may be also allowed at the stage of technologic paradigm changes;
- In other cases, competition policy shall probably have the priority of approximation to the perfect competition model;
- In any case, to achieve the objectives of industrial policy, it is unfeasible to apply such measures as provision of exclusive rights to individual business entities or creation of obstacles to starting production of similar products by other entrepreneurs.
CONTRIBUTION BY UZBEKISTAN
COMPETITION POLICY, INDUSTRIAL POLICY AND NATIONAL LEADERS

--Uzbekistan--

1. Most of the state aids and subsidies in Uzbekistan are granted only to national (100% state owned companies) or to joint-ventures where state has controlling of majority stakes. Even though there is no official definition as to the nationality in this case, it would be defined as 100% of state ownership or where state possesses controlling stake. The support to the national champions is provided mainly by establishing excise-duties to imports, providing bank loans and controlling ownership.

2. The main targets of the government’s industrial policy are to foster exports and reduce unemployment. However, as the country is not a member of WTO the policy to support national champions has been stable for long period of time.

3. There are no major success or failure stories related to policies. Most of the time the support provided to national champions helps companies to grow and improve production. The state support is given for certain period of time after which the state reviews the necessity for further assistance. The success is defined as sustainable growth in production and increased efficiency as well as decreasing costs. National champions are usually but not wholly excluded from the sphere of activity covered by the best practice of competition policy standards. Currently the automobile market is supported by high import duties, which sometimes leads to high prices. Success means the total economic independence of the companies, where state eventually stops the subsidies and leaves it open to pure competition. Failure means continued subsidy of the companies without proper strategy as to the company’s future. Failure would also mean rising costs, decreasing efficiency and poor quality of the products.

4. The competition agency is not responsible for calculating the costs and benefits of the government interventions; however the agency tracks the prices of products and monitors the market access issues at those sectors. Industrial policy and competition policy in theory are different sides of the same issue. Each of the policies overlaps each other and to the point defines the priorities depending on state’s preferences. In most developing or transitional countries competition policy never realises its role and always lags behind the industrial policy, because of rationally set priorities, which sometimes may look like to have a negative long term economic impact for the economy. The competition agency constantly monitors the number of bankrupt companies and the number of insolvent companies. The benchmark to assess economic costs and benefits of government interventions is not implemented.

5. When the mergers take place based on the decrees by the Cabinet of Ministers preliminary review of merger’s effects take place by the competition authority. Mergers that have been approved by the competition agency are constantly monitored. Companies that apply for approval of the merger submit business plans on investment plans, plans of restructuring of manufacturing processes and increasing of production. These plans are reviewed by the competition agency and in cases when investors don’t take responsibility according to their business plans the competition agency reviews the case and may take a decision to reverse the merger.

6. No decision of the competition agency has been overridden on grounds of industrial policy. However, at the current level of economic development, industrial policy prevails over competition policy.

7. There is a special fund under the Academy of Science that is used to support research activities by the academic institutions in cooperation with manufacturers.
Means and Goals

8. The instruments used for industrial policy are government procurements, exemptions from antitrust laws, regulatory barriers to competition, access to credit, arranged mergers and acquisitions, control of acquisitions of national companies by foreign investors, easy access to commodity resources and products of monopolist companies.

9. In cases when national champions operate in foreign markets such as the case with the automotive producer, state is often motivated to increase the market share or protect the existent share in the foreign markets. So, such motivations are limited because not many of the national champions directly operate in foreign markets.

10. Industrial policy in Uzbekistan is often motivated to foster exports and decrease the dependence of imports, as well as creating jobs. So by those means it is not directed at correcting market failures.

11. As competition to Uzbek companies mostly comes from China, Uzbekistan is also pursuing these policies which clearly constitutes to the “prisoners’ dilemma” situation. However, big nations such as China can take more advantage from these policies because it might take a long time for all countries to adopt industrial policies to back up their manufacturers.
CONTRIBUTION BY MR. ELIE COHEN
1. Should market regulations and competition authorities be considered tools befitting periods of economic calm, while government assistance, if not industrial policies, are deemed the only tools suitable in times of crisis? As the current crisis deepens, it can be seen that the initial reflex of any government is to put the rules of competition on hold, protect domestic industry and, in some cases, even exploit the crisis by attempting to reap an illusory competitive advantage. Limiting imports by invoking dumping clauses, reserving financial guarantees for nationals alone and lending to local banks on preferential terms are all indicative of one and the same approach: when confronted by a crisis, protection is better than openness, and national identity takes precedence over territorial roots. The government assistance that it was believed could be limited to the financial industry so as to preclude systemic risk has now been extended to the motor and real estate industries, to credit-strapped SMEs, and probably before long to airlines, the chemicals industry and so on. In this way, a dynamic is taking hold which, unless care is taken, will justify protectionist measures, limitations on competition and forms of national preference. We thought the lessons of 1929 had been learned, and that there had been a clean break with the artificial havens of an administered economy, but the lure of national solutions may prove irresistible.

2. Europe, far from responding to the shock of the crisis with common policies, and far from seizing the opportunity to demonstrate the strength of the single market and of the euro area, has adopted a policy that reveals the temptation for each country to fend for itself. Clearly, what is showcased in the media would suggest just the opposite: a G4 meeting convened under the French presidency, a co-ordinated Sarkozy-Brown crisis-resolution plan, a meeting of the G20, a co-ordinated economic stimulus plan. The fact of the matter is that communication has prevailed over substance. For proof, one need only consider the policies carried out in response to the September 2008 liquidity shock and solvency crisis.

3. A shared panoply of tools of intervention was adopted: deposit guarantees, bank recapitalisation, interbank loan guarantees and in some cases the purchase of toxic assets. Yet national implementation of these measures ended up creating distortions. One example of this was the recapitalisation of banks: some countries took a punitive approach tantamount to nationalisation; others lent government funds on highly preferential terms; and the rest made recapitalisation contingent on credit expansion or dividend limitation. There were three practical outcomes to this race to fragment and renationalise financial systems. First, national competition authorities were muzzled, as was the UK Office of Fair Trading in respect of the HBOS-Lloyds-TSB merger. Second, the lack of a European mechanism for salvaging integrated financial corporations gave rise to intergovernmental joint ventures to save Fortis and Dexia, with the probable ultimate result of national dismantling of these integrated European groups. Third, the ever more numerous government bailouts and the competitive distortions they cannot help but generate made DG Competition want to apply the conventional method of *quid pro quos* for public assistance, with rapid capitulation to national demands. It was believed that Europe, being a prescriptive power, would be capable of managing the conflict between systemic risk and competitive risk generated by government assistance, but DG...
Competition’s demand for a cutback in lending by assisted businesses in the midst of a credit crunch put it in an awkward position.  

4. It can be considered that this error has since been rectified, and that DG Competition is gradually getting its bearings back, submitting national assistance plans to swift but effective review. This assumption will soon be put to the test, since we are now witnessing a second wave of recapitalisations with partial nationalisations. If the current governmental schemes were to be carried out with no harmonisation, the European financial landscape would soon be split asunder between British firms heavily recapitalised and subject to prescriptive credit policy, French firms thinly recapitalised but with no strings attached and a merged German group heavily recapitalised on scandalously preferential terms. 

5. One might attribute this relative impotence of the competition authority to the urgency of the situation and consider that when the storm has passed the Commission will resume control. The concentrations undertaken in response to the crisis will pose problems of abuse of dominant positions in some markets, and especially the one for mortgage lending; what has been authorised today can thus be dismantled tomorrow. 

6. The history of European integration may even prompt us to consider a third scenario for the course of competition policy against the backdrop of a major financial crisis: taking the high road out. Finding the European Union relatively powerless to cope with the break-up of regulatory and prudential supervisory powers may prompt amendments to the Maastricht Treaty that would invest the central bank with supervisory power to foster financial stability. Similarly, the risk of fragmentation of the single market for financial services may give rise to centralised regulation of banks of Community-wide scope. Lastly, a European financial and fiscal power may arise to deal with internal dislocation risks within the euro area should there be a deterioration of national public debts (as measured by sovereign-debt spreads between European countries). The financial crisis is having magnifying effects on the imperfections and dysfunctional aspects of European institutions. The worst is not certain, but to date the European Union has not been up to the tasks at hand. 

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1 “Brussels would like to compel all assisted banks to bolster their balance sheets, i.e. to lend less in proportion to their equity, even if that equity is strengthened with State funding” (Le Figaro, 1 December 2008); “The State is opposed to the Commission on a major issue: Brussels is making its go-ahead for the transaction contingent on limited growth in credit and in bank balance sheets” (Les Échos, 1 December 2008).
CONTRIBUTION DE M. ELIE COHEN
RISQUE SYSTÉMIQUE ET DROIT DE LA CONCURRENCE

-- Elie Cohen --

1. Faut-il considérer les régulations de marché et les autorités de concurrence comme des outils pour temps de paix économique et les aides publiques voire les politiques industrielles comme les seuls outils appropriés aux temps de crise? Avec l’approfondissement de la crise on constate que le premier réflexe de tout Gouvernement est de mettre entre parenthèses les règles de la concurrence, de protéger son industrie domestique, voire de tirer partie de la crise pour gagner un avantage concurrentiel illusoire. Limiter des importations en invoquant des clauses de dumping, réserver ses garanties financières à ses nationaux, prêter aux banques autochtones à des conditions avantageuses relève d’une seule et même logique : face à la crise la protection est supérieure à l’ouverture, l’identité nationale prime sur l’ancrage territorial. Les aides publiques qu’on croyait pouvoir limiter à l’industrie financière pour prévenir le risque systémique sont étendues à l’industrie automobile, à l’immobilier, aux PME en mal de crédit et demain sans doute aux compagnies aériennes, à l’industrie chimique ….. Ainsi se forme une dynamique qui, si on n’y prend garde, justifiera des mesures protectionnistes, des limites à la concurrence, des formes de préférence nationale. On croyait avoir tiré les leçons de 29 et rompu avec les paradis artificiels de l’économie administrée mais la tentation des solutions nationales risque de devenir irrépressible.


3. Une panoplie commune d’outils d’intervention a été adoptée : garantie des dépôts, recapitalisation des banques, garantie du crédit interbancaire, achat éventuel d’achats toxiques. Mais la mise en œuvre nationale de ses mesures a abouti à créer des distorsions. Un exemple, la recapitalisation des banques : certains pays ont adopté une logique punitive de quasi-nationalisation, d’autres prêtèrent des capitaux publics à des conditions très avantageuses, les derniers enfin conditionnèrent la recapitalisation au développement du crédit ou à la limitation des dividendes. Le résultat pratique de cette course à la fragmentation et à la renationalisation des systèmes financiers a été triple. D’une part, les autorités de concurrence nationale ont été condamnées au silence, ce fut notamment le cas de l’autorité de la Concurrence britannique pour la fusion HBOS-Lloyds-LSB. D’autre part l’absence de mécanisme européen de sauvetage des entreprises financières intégrées conduisit à des joint ventures interétaient pour sauver Fortis ou Dexia avec comme résultat ultime probable un démantèlement sur des bases nationales de ces groupes européens intégrés. Enfin, la multiplication d’aides publiques et les distorsions concurrentielles qu’elles ne pouvaient pas ne pas générer ont conduit la DG Comp à vouloir appliquer la méthode classique des contreparties aux aides publiques avec une capitulation rapide face aux demandes nationales. On croyait que l’Europe, puissance normative, saurait gérer le conflit entre risque systémique et
risque concurrentiel généré par les aides publiques mais la demande par la DG Comp de réduction du crédit par les entreprises aidées dans un contexte de credit crunch l’a mise en porte à faux.

4. On peut considérer que cette erreur a été depuis corrigée et que la DG Comp retrouve progressivement ses marques en soumettant les plans d’aides nationaux à un examen rapide mais efficace. Cette hypothèse sera rapidement testée puisqu’on assiste à un deuxième cycle de recapitalisations avec des nationalisations partielles. Si les plans gouvernementaux actuels étaient menés à bien sans harmonisation des conditions de recapitalisation, on assisterait rapidement à un éclatement du paysage financier européen entre des entreprises anglaises fortement recapitalisées et soumises à une politique du crédit directive, des entreprises françaises faiblement recapitalisées mais sans conditions attachées et un groupe allemand fusionné fortement recapitalisé à des conditions scandaleusement favorables.

5. On peut mettre cette impuissance relative de l’autorité de la concurrence sur le compte de l’urgence et estimer qu’une fois passé l’orage, la commission reprendra la main. Il est probable que les concentrations réalisées à la faveur de la crise poseront des problèmes d’abus de position dominante sur certains marchés, notamment celui du crédit immobilier ; on pourra donc défaire demain ce qu’on a autorisé aujourd’hui.

6. L’histoire de l’intégration européenne peut même nous inciter à envisager une troisième hypothèse d’évolution de la politique de la concurrence dans un contexte de crise financière majeure : la sortie par le haut. Le constat fait d’une relative impuissance de l’Union Européenne face à l’éclatement des pouvoirs de régulation et de supervision prudentielle peuvent conduire à compléter Maastricht en dotant la banque centrale d’un pouvoir de supervision au service de la stabilité financière. De même, le risque de fragmentation du marché unique de services financiers peut conduire à une régulation centralisée des banques d’envergure communautaire. Enfin, un pouvoir financier et fiscal européen pourrait naître pour traiter les risques de dislocation interne de la zone Euro en cas d’aggravation de la crise des dettes publiques nationales (mesuré par les spreads sur dette souveraine entre pays européens). La crise financière a des effets grossissants sur les imperfections et les dysfonctionnements des institutions européennes. Le pire n’est pas certain, mais l’Union Européenne n’a jusqu’ici pas été à la hauteur des enjeux.

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1 « Bruxelles voudrait imposer à toutes les banques aidées de redresser leur bilan, c’est à dire de prêter moins en proportion de leurs capitaux propres, fussent-ils renforcés par les deniers de l’Etat Le Figaro 1/12/08
« L’Etat s’oppose à la Commission sur un point majeur : Bruxelles conditionne son feu vert à l’opération à une croissance limitée du crédit et à celle de la taille du bilan des banques » Les Echos 1/12/08
SESSION II

COMPETITION POLICY AND THE INFORMAL ECONOMY
CALL FOR CONTRIBUTIONS
TO ALL GLOBAL FORUM PARTICIPANTS

RE: COMPETITION POLICY AND THE INFORMAL ECONOMY

GLOBAL FORUM ON COMPETITION (FEBRUARY 19 – 20, 2009)

SESSION II

1. The OECD Global Forum on Competition will hold a roundtable discussion on competition policy and the informal economy on February 19, 2009. The roundtable will follow the traditional format of roundtables in the Competition Committee. It is scheduled to last for 3 hours. A background paper and country contributions will be circulated. On the basis of the latter, a scenario will be prepared for the discussion, allowing contributing countries to share their views and experiences according to several themes. Presentations by several panellists will precede the general discussion.

1. Background

2. Within the economics literature the concept of the informal firm is loosely defined. At times an informal firm is defined to be an unregistered firm with 5 or fewer employees. In other situations it refers to a firm that fully or partially evades taxes or other forms of regulation such as product, labour or land regulations. In short, no common definition of an informal firm exists and consequently there is no common definition of the informal economy, either. However, regardless of the fact that informality means different things to different people, researchers and developing countries often view informality as a serious problem.

3. Recent statistics reveal that the size of the informal economy within many developing countries is large, often amounting to more than 50% of their GDP. Within industrial countries, in contrast, it is estimated to be 15% of GDP. Research findings indicate that excessively costly and stringent regulations, overly burdensome taxes, and ineffective governance help explain some of this difference, though other factors surely contribute. Excessively high taxes and costly regulations incentivize firms to operate informally because firms lower their cost structure when taxes and regulations are evaded successfully. Weak governance structures also contribute to the extent of informality as firms may rationally forecast low expected penalties from failing to comply with various regulations due to a low detection rate. In essence, firms choose to operate informally (either partially or fully) because they see profit in it.

4. Because informal firms often evade costly taxes and other regulations, many observers are concerned that the informal sector significantly affects competition in the formal sector. The reason is that the intensity of competition between informal and formal firms is related to the costs that informal firms avoid as a result of not complying with all or some of their legal obligations. If the cumulative cost of complying with a variety of regulations is high, then informal firms will have a substantial competitive advantage over formal firms. That, in turn, may prevent the entry or expansion of formal firms in the market.

5. Beyond the fact that informal firms evade the rule of law and potentially cause law abiding formal firms to exit the market, serious concerns have also been raised about the productivity of informal firms. In many industries informal firms are small, unregistered and often have no access to credit. Such firms may, nevertheless, be able to undercut large, formal firms in some markets due to the costs that they save as a result of evading taxes and regulations. When small, informal firms prevent the entry or
expansion of larger, more productive formal firms, resources are wasted. Resources are also wasted to the extent that informal firms reduce the incentives of formal firms to innovate and adopt new technologies. On the other hand, the possibility certainly exists that informal firms might be more productive than formal firms if they successively evade regulations which impede productivity enhancing investments.

6. Competition law enforcement agencies are familiar with some of these concerns. For example, some competition authorities routinely examine laws with a view towards assessing their impact on competition. But World Bank economists point out that more must be done even on fundamental regulations. For example, the Doing Business Indicators published by the World Bank reveal significant differences across countries in the speed with which companies can open a business. Such observations point out the need for advocacy by competition authorities.

7. Although moving informal firms to the formal economy is an issue in which some competition authorities may want to get involved, a more immediate one revolves around competition law enforcement actions and cases that involve firms in the informal economy. Several examples come to mind. A merger enforcement action involving formal firms might be rebuffed by the defendant’s assertions that informal producers discipline formal ones. Moreover, assigning market shares when the market definition includes informal firms could be especially difficult due to data limitations. Alternatively, laws mandating minimum prices might be enacted to help support formal firms survive competition from informal firms. Furthermore, anticompetitive action by small, informal firms may present special challenges to competition authorities.

8. The quality and utility of the roundtable will be strengthened by written contributions from participants. It will be especially helpful if you include a discussion of relevant cases from your jurisdictions. Your written contributions will complement a background paper prepared by the Secretariat.

9. To help you to prepare your contribution, a number of issues and questions are raised below that you should feel free to respond to and discuss in your submission. This is not intended to be a restrictive or comprehensive list. Participants are encouraged to raise and address other issues, as well, based on their own experience. A suggested bibliography is attached, as well.

2. Administrative Issues

10. Please advise the Secretariat by 1 December at the latest if you will be making a written contribution. Written submissions are due i) by 8 December (non-members); and ii) by 5 January 2009 (members and observers to the Competition Committee). Failure to meet that deadline could result in a contribution not being distributed in a timely fashion in advance of the meeting.

11. All communications regarding documentation for this roundtable should be sent to Jennah Huxley, Telephone – 33 (0)1 45 24 85 55; Fax – 33 (0)1 45 24 96 95; E-mail – Jennah.huxley@oecd.org. Ken Danger would be pleased to answer any substantive questions you may have about the roundtable. His phone number and e-mail address are: 33 (0)1 45 24 82 50, ken.danger@oecd.org.
3. Some Suggested Issues and Questions for Consideration in Country Contributions

1. Definition of informal economy. What is an appropriate definition of the informal economy? Are some measures better than others?

2. Causes, characteristics and size. What factors contribute to the formation of informal firms? Do some factors appear to be more important than others? What types of products or services are frequently produced within the informal economy? How large is the informal economy in your jurisdiction? Is the informal economy stable, growing or reducing in size?

3. Level playing field and productivity. Does the informal economy impact competition in the formal economy? If so, is the formal sector affected generally or only in specific industries or by firm size? Do informal and formal firms collaborate? Does a large informal economy impede the entry or expansion of foreign firms? Are informal firms less productive than formal firms per se? Alternatively, are they ever more productive? Why or why not? Does regulation and taxation evasion by informal firms keep larger, more productive formal firms from entering the market or expanding in some instances? Does informal production appear to hamper economic growth – or does it enhance it?

4. Competition law enforcement. Are small firms operating within the informal economy outside the reach of competition authorities? If so, what alternative strategies could be used to deal with competition problems in the informal sector? What competition cases in your jurisdiction have involved aspects of the informal economy? How can the informal economy affect market definition and the calculation of market shares? What methods should be used to estimate the possible effect on competition from a merger in the formal economy when there is a concern about substitution by consumers to informal firms?

5. Advocacy. In what ways can competition authorities contribute to solving the informality problem? What methods have been used in your jurisdiction to move informal firms to the formal economy? What methods seem to be especially pro competitive?
SUGGESTED BIBLIOGRAPHY


APPEL À CONTRIBUTIONS
TOUS LES PARTICIPANTS AU FORUM MONDIAL

Objet : La politique de la concurrence et l’économie informelle

Forum mondial sur la concurrence (19-20 février 2009)

Session II

Cher Participant,


Dans la littérature économique, la notion d’entreprise informelle n’est pas définie de manière précise. Parfois, une entreprise informelle est définie comme une entreprise non immatriculée ne comportant pas plus de 5 salariés. Dans d’autres cas, il est fait mention d’une entreprise qui échappe totalement ou partiellement aux impôts ou à d’autres formes de réglementations régissant notamment les produits, la main-d’œuvre ou les terrains. En résumé, il n’existe pas de définition commune de l’entreprise informelle et, par conséquent, il n’y a pas non plus de définition commune de l’économie informelle. Toutefois, indépendamment du fait que chacun interprète différemment le caractère informel, les chercheurs et les pays en développement considèrent souvent l’économie informelle comme posant de graves problèmes.

Des statistiques récentes montrent que la taille de l’économie informelle dans de nombreux pays en développement est importante, et représente souvent plus de 50 % de leur PIB. En revanche, au sein des pays industrialisés, elle est estimée à 15 % du PIB. Des résultats de recherches montrent que des réglementations excessivement coûteuses et contraignantes, une fiscalité trop lourde et une gouvernance inefficace contribuent à expliquer en partie cette différence, bien qu’elle soit certainement due aussi à d’autres facteurs. Des impôts excessivement élevés et des réglementations coûteuses incitent les entreprises à fonctionner d’une manière informelle, dans la mesure où les entreprises qui réussissent à frauder sur le plan fiscal et sur le plan des réglementations parviennent à abaisser la structure de leurs coûts. Des structures administratives peu efficaces contribuent aussi au développement de l’économie informelle, dans la mesure où les entreprises peuvent prévoir rationnellement que le fait de ne pas se conformer aux différentes réglementations ne les expose pas à d’importantes pénalités en raison d’un faible taux de détection. En fait, les entreprises choisissent de fonctionner de manière informelle (partiellement ou totalement) parce qu’elles en tirent un bénéfice.

Comme les entreprises informelles échappent souvent aux impôts coûteux et à d’autres réglementations, beaucoup d’observateurs sont préoccupés par le fait que l’économie informelle a une incidence importante sur la concurrence dans l’économie formelle. En effet, l’intensité de la concurrence entre les entreprises informelles et les entreprises formelles est liée aux coûts auxquels les entreprises informelles échappent du fait qu’elles transgressent la totalité ou une partie de leurs obligations légales. Si le coût cumulé du respect de diverses réglementations est élevé, les entreprises informelles disposeront d’un avantage concurrentiel considérable sur les entreprises formelles. Cela peut empêcher l’accès aux marchés ou le développement d’entreprises formelles.
Au-delà du fait que les entreprises informelles échappent à la règle de droit et sont susceptibles d’amener les entreprises formelles qui respectent la loi à sortir du marché, de vives inquiétudes se sont exprimées quant à la productivité des entreprises informelles. Dans de nombreux secteurs, les entreprises informelles sont petites, non immatriculées et n’ont souvent pas d’accès au crédit. Ces entreprises peuvent néanmoins être en mesure d’être plus compétitives que les grandes entreprises formelles sur certains marchés en raison des coûts auxquels elles échappent en fraudant le fisc et en ne respectant pas les réglementations. Lorsque de petites entreprises informelles empêchent l’accès au marché ou l’expansion d’entreprises formelles plus importantes et plus productives, il en résulte un gaspillage de ressources. Les ressources sont également gaspillées, dans la mesure où les entreprises informelles réduisent les incitations, pour les entreprises formelles, à innover et à adopter de nouvelles technologies. En revanche, il est certainement possible que les entreprises informelles soient plus productives que les entreprises formelles si elles réussissent à échapper aux réglementations qui entravent les investissements permettant d’accroître la productivité.

Certaines de ces préoccupations sont familières aux administrations chargées de faire appliquer le droit de la concurrence. Par exemple, certaines autorités de la concurrence examinent systématiquement les lois en vue d’évaluer leur impact sur la concurrence. Toutefois, les économistes de la Banque mondiale soulignent la nécessité de progresser encore dans ce domaine même en ce qui concerne les réglementations fondamentales. Par exemple, les indicateurs Doing Business publiés par la Banque mondiale font apparaître des différences importantes entre les pays en ce qui concerne les délais dans lesquels des entreprises peuvent être créées. Ces constatations font apparaître la nécessité, pour les autorités de la concurrence, de mener des actions de sensibilisation.

Si certaines autorités de la concurrence peuvent souhaiter participer aux actions menées pour orienter les entreprises informelles vers l’économie formelle, un problème plus immédiat porte sur les actions d’application du droit de la concurrence et les affaires qui font intervenir des entreprises de l’économie informelle. Plusieurs exemples viennent à l’esprit. Une action judiciaire concernant une fusion entre entreprises formelles peut être contestée par des affirmations du défendeur selon lesquelles les producteurs informels pénalisent les producteurs formels. De plus, l’attribution de parts de marché lorsque la définition du marché inclut des entreprises informelles peut être particulièrement difficile en raison des limites concernant les données disponibles. En revanche, des lois fixant des prix minimums peuvent être adoptées pour aider les entreprises formelles à faire face à la concurrence des entreprises informelles. De plus, les manoeuvres anticoncurrentielles des petites entreprises informelles peuvent poser des problèmes spécifiques aux autorités de la concurrence.

La qualité et l’utilité de la table ronde se trouveront renforcées par des contributions écrites des participants. Il serait particulièrement utile que vous puissiez inclure un examen de cas pertinents par vos juridictions. Vos contributions écrites compléteront une note thématique établie par le Secrétariat. En outre, vous êtes priés de noter que Mme Taimoon Stewart et M. Bill Lewis ont accepté de participer avec nous à cette table ronde.

Afin de vous aider à préparer votre communication, vous trouverez ci-joint un certain nombre de questions auxquelles vous pourrez répondre librement et que vous pourrez développer dans votre contribution. Cette liste n’a pas pour objet d’être restrictive ni exhaustive. Les participants sont invités à évoquer et à traiter également d’autres questions, sur la base de leur propre expérience. Une bibliographie proposée se trouve également jointe.

Si vous envisagez de présenter une contribution écrite, vous êtes prié d’en aviser le Secrétariat d’ici le 1er décembre au plus tard. Les contributions écrites devront parvenir d’ici le 8 décembre. En cas de dépassement de cette date limite, votre communication risque de ne pas être diffusée en temps voulu avant la réunion.
Toutes les communications concernant la documentation établie en vue de cette table ronde doivent être envoyées à Jennah Huxley, téléphone – 33 (0)1 45 24 85 55 ; fax – 33 (0)1 45 24 96 95 ; adresse électronique – jennah.huxley@oecd.org. Ken Danger se fera un plaisir de répondre aux questions de fond que vous pourriez avoir à poser concernant la table ronde. Son numéro de téléphone et son adresse électronique sont les suivants : 33 (0)1 45 24 82 50 ; ken.danger@oecd.org.
Questions dont l’étude est suggérée dans les contributions des pays

- **Définition de l’économie informelle.** Quelle est la définition appropriée de l’économie informelle ? Certains indicateurs sont-ils préférables à d’autres ?

- **Causes, caractéristiques et taille.** Quels sont les facteurs qui contribuent à la constitution d’entreprises informelles ? Certains facteurs apparaissent-ils plus importants que d’autres ? Quels sont les types de biens ou de services qui sont souvent produits dans le cadre de l’économie informelle ? Quelle est l’importance de l’économie informelle dans votre juridiction ? L’économie informelle est-elle stable, en croissance ou en régression ?


- **Application du droit de la concurrence.** Les petites entreprises qui opèrent au sein de l’économie informelle échappent-elles au contrôle des autorités de la concurrence ? Dans l’affirmative, quelles sont les autres stratégies qui pourraient être utilisées pour traiter des problèmes de concurrence dans le secteur informel ? Quelles sont, dans votre juridiction, les affaires concernant la concurrence dont certains aspects étaient liés à l’économie informelle ? Comment l’économie informelle peut-elle affecter la définition du marché et le calcul des parts de marché ? Quelles sont les méthodes à utiliser pour estimer l’effet que pourrait avoir une fusion dans l’économie formelle sur la concurrence lorsqu’il existe un risque de substitution de la part des consommateurs au profit des entreprises informelles ?

- **Sensibilisation.** De quelle manière les autorités de contrôle de la concurrence peuvent-elles contribuer à résoudre les problèmes posés par l’économie informelle ? Quelles sont les méthodes qui ont été utilisées dans votre juridiction pour orienter les entreprises informelles vers l’économie formelle ? Quelles sont les méthodes qui semblent particulièrement favorables à la concurrence ?
BIBLIOGRAPHIE PROPOSÉE


CONTRIBUTION BY BULGARIA
COMPETITION POLICY AND THE INFORMAL ECONOMY IN BULGARIA

-- Bulgaria --

1. The Informal Economy in Bulgaria

1. The grey economy is one of the main constraints to investment and growth in Bulgaria. Lower tax and social security rates and increased control intensity introduced by the Bulgarian government since 2003 and continued credit and FDI-based economic growth have reduced the share of the grey economy by some 30% between 2002 and 2008.

2. The grey economy has emerged as a top concern to businesses operating in Bulgaria prompting an increasing number of proposed corrective policy actions on the side of the government, the business community, trade unions and think-tanks. Recent tax and social security contribution cuts and increased government control intensity have resulted in a de-shadowing of some parts of the grey economy.

2. Size and Scope of the Grey Economy in Bulgaria

3. Although grey economy is notoriously difficult to measure and understand it is easily identifiable by businesses when they face partners and competitors who operate outside the law by not paying taxes, social security and health contributions, hiding actual employment, circumventing product quality, safety or environment regulations, infringing copyrights, etc. According to the latest Enterprise Survey of Bulgarian firms performed by the World Bank in 2007 informal practices have topped the list of constraints to firm investment in Bulgaria.

4. Notwithstanding differences in concepts and methodology, estimates of the size of the grey economy in Bulgaria since 1990 have ranged from 16% to 38% of GDP, which has consistently ranked the country among the “top” new EU member-states. According to different estimates the size of the grey economy in Bulgaria in 2007/2008 ranges between 20% and 35% of GDP, with some sectors, such as construction and real estate, reporting less than 50% of the actual value of transactions. While the National Statistical Institute imputes and adds part of the grey economy into national accounts and these numbers need to be interpreted with great caution when making conclusions about policy actions, they send a clear signal to policy makers that grey economy is a sizable challenge to Bulgaria’s economic development. The most hardly hit sectors are the labour intensive construction, tourism, agriculture and services (e.g. repairs, private education and healthcare, etc.) but research has also shown that there are also considerable grey pockets in manufacturing, in particular in excise industries (alcohol and cigarette production and fuels), textiles and transport.

3. Dynamics of the grey economy

5. In response to business concerns and initiated policy action to reduce the level and scope of the grey economy in Bulgaria, the Center for the Study of Democracy and Vitosha Research constructed a Hidden Economy Index in 2002. The index, published annually since 2002, aims to track the dynamics of the hidden economy in Bulgaria. It is important to note that the index does not measure the size of the grey economy but its dynamics, giving important feedback to the policy makers and the business community on the effectiveness of measures to curb grey economy. According to the index there has been a rebound in the grey economy in Bulgaria in the first year of EU accession. This might reflect both reform fatigue on the side of the Bulgarian government following intensive efforts in 2006 to join the EU, but also the rising concern of the business community in the country over unfair competition from the grey economy as international competitive pressure squeezes down its margins.
4. Measures to reduce the level of grey economy

6. Since 2003 the Bulgarian government has undertaken a number of economic incentive measures and increased control intensity to reduce the level of grey economy in the country, such as the sizable reduction in corporate and personal income taxes, as well as social security contributions, the integration and modernisation of tax collection under the National Revenue Agency, the introduction of compulsory labour contract registration, etc. These measures to improve the business environment compounded by sustained high economic growth have resulted in a gradual reduction in the share of grey economy in the country. According to CSD estimates based on the Informal Economy Index the hidden turnover of companies in Bulgaria decreased from 29% in 2002 to 17% in 2007.

5. Competition law enforcement

7. The Bulgarian Competition Law is applied to all undertakings and natural persons and consequently small firms operating within the informal economy do not remain outside the scope of competition enforcement.

6. Examples of CPC practice:

1. In 2005 the Commission approved the sectoral analysis of three related markets: production of and trade in milling wheat, wheat flour and wheat bread for mass consumption.

   An inquiry into the bread sector revealed that the huge “grey economy” in the bread production and distribution market is the most frequently outlined problem by the market operators. Part of bread manufacturers, mainly small bakeries, produce and sell bread without having registered their firms and consequently have no obligations to the State budget and the insurance funds. They buy flour and grain without the proper documentation and invest no resources to improve working conditions. Their cost price is 20 – 30% lower than that of legitimate bread producers. The manufacturing process of illegitimate bakeries is done in poor sanitary conditions and through under-reporting of income. These firms undercut product costs which hinders sector development and creates market chaos.

   A conclusion was made that the “grey economy” in the sectors for production and trade in wheat flour and wheat bread for mass consumption stemmed from the VAT-free trade in wheat and that the relatively strong “grey” economy in the sector generated unfair competition.

   As a result of the initiated inquiry, the CPC came out with some recommendations:

   • A suggestion to develop, with the help of branch organisations, an effective control system to fight unfair competition in the sector. The aim was to restrict the informal economy by prohibiting grain trade without the proper documentation resulting in under-reporting of turnover, tax and insurance evasion, and harm to the State budget.

   • The CPC advised the State to introduce mandatory registration under the VAT law of all flour producers. The objective was to place market participants in an equal position and “de-shadow” illegitimate producers.

   • The CPC advised market participants to diminish the silent or explicit prevention, restriction or distortion of competition on the relevant market, namely the unfair attraction of customers by selling flour at prices below the actual production and realisation costs, as well as the direct or indirect fixation of prices and allocation of markets and supply sources.
The CPC called for joining the efforts of State bodies and branch organisation to enforce the rules of fair business and market behaviour.

2. In 2008 the Commission on Protection of Competition approved the concentration between Holsim Bulgaria AD and Remos Beton OOD. The assessment of the concentration in the market of ready-mixed concrete suggested evaluating the size of the market. The Commission had reasonable grounds to believe that part of the production of concrete is made without the necessary documentation at lower prices or without regular and accurate accounting. The existence of “grey sector” was indicated by the Association of producers of concrete in Bulgaria as well as by independent producers.

The lack of official statistics on regional markets in the concrete production and the existence of unregistered transactions raised serious doubt about the accuracy of the assessment based on individual reports from participants in the market, since there is no certainty about the market players and the completeness of the accounting documents. All this called for an alternative indirect assessment through tracking shipments of materials for concrete production, namely cement and inert materials.

The indirect assessment of the regional market of ready-mixed concrete, on the basis of consumption of inert materials, is not sufficiently accurate due to the existence of grey sector in the delivery of inert materials: many companies produce inert materials without authorisation and sell them at low prices without documents. The statistical reporting of transactions is seriously hindered by the presence of unregistered sales, illicit mining and the related difficulties in actual control of the yields available on municipal concessions.

Regarding the assessment of the regional market volume of concrete, based on the consumption of cement as the main ingredient used in concrete production, information on sales of the national producers of cement to the concrete producers in the region provided relatively detailed information on the total consumption of cement in concrete production in the region. At the same time, additional information from national statistics on the imports of grey cement in the country can not refer to consumption in a given geographical area, but should be viewed as an indication that the designated market volumes may be higher.

3. In 2007, the Commission on Protection of Competition reviewed a proposal made by the taxi associations to the Ministry of Transport for the introduction of minimum uniform tariff of the taxi service, determined through a coordination of the legitimate branch representatives and the local authorities, valid for the territory of each municipality.

The CPC opposed to any form of fare regulation. Nevertheless the Commission proposed measures to decrease the informal economy in the sector. The CPC reckons that the municipal councils should exercise their powers envisaged in the Law for the road transport to determine the number of the taxi automobiles, working on the territory of the municipality, as well as the conditions and the order for their distribution between the carriers. Although this restricts the entry in the market, at the moment this is the most suitable way for balancing the interests of the consumers and of the carriers. These powers should be exercised after consultations with the taxi associations. The entering of new participants in the market without any control is connected with risk of disregarding technical requirements. The determination of the number of taxis should go together with enhanced control with regard to the requirements and severe sanctions in cases of infringements. The number of the taxis should be reviewed every year on the basis of the changes in circumstances and the needs of the population. Thus there will not be market
foreclosure for a long period and the potential competition will continue to play its disciplining role.
CONTRIBUTION BY CHILE
THE INFORMAL SECTOR AND COMPETITION POLICY: 
THE CHILEAN FNE’S EXPERIENCE 
--Chile--

1. The concept of ‘informal sector’

1. The expression “informal sector” – or sometimes ‘informal economy’ - has no single meaning in the economic and social theory. One of its fields of application is the labour market, where it identifies people working in an unofficial way, i.e. under no contract, hence not covered by the social security system or by an established social protection net. This first meaning, along with some precisions needed for a formal definition, is the one used by the United Nations International Labour Organisation (ILO)\(^1\). But this is not the connotation important to us in what follows.

2. The expression also stands for agents and businesses operating outside the legal and regulatory framework – such as, for instance, health care, property rights or the tax system. It can readily be seen that this concept can depict as many informal markets as there are agents and businesses in an economy. In other words, an informal sector can be observed in each economic activity and sector, although informality is predominant is some of these, as is the case of small and medium enterprises.


2. The informal sector’s economic impact

4. According to the literature, Latin American countries exhibit a large incidence of the informal sector, which contributes to a high rate of black labour (informal employment) and to a low rate of tax compliance. Estimates for the Argentinean economy in 2004, for example, show the relative tax charge in its formal and informal sectors: “According to the Foundation for Latin American Research, the firms that pay their taxes on time and register their employees have a tax incidence of 37.3% of GDP, more than twice the informal sector’s, all of which clearly bears negatively on the former’s competitiveness. In some cases this can be deemed as unfair competition, able to push formal firms out of the market.”

5. Tax considerations are far from being the sole concern caused by the informal sector, since local trade is also harmed. In order to increase and improve to informal sector’s regulation, in 2007 the government sponsored a bill\(^2\) on the grounds that “illegal trade is a serious national problem as long as it generates assorted costs and social damage. On the one hand, mention must be made of tax evasion. Besides, in many cases that illicit activity breaks the law of intellectual property thus affecting the claimants of involved rights, along with perverting the copyright system. Third, there is the distortion introduced in the illegal trade’s product market, which translates into unfair competition to legitimate businesses. In the tax, sanitary, criminal, and copyright laws, and also in the municipal environment, measures have been taken to fight illegal trade and its harmful effects, to no avail. Defences adopted so far with the purpose of weakening illegal trade have consisted mainly in sanctioning the retailer, that is, they

\(^1\) ILO introduced the concept of ‘informal sector’ for the first time in the early 70s, not without controversy, grounded on the complexity, dynamism and diversity of informal activities around the world. Only in 1993 ILO produced a statistically harmonised definition, based on the characteristics of activities and businesses related to the sector. Later on, in 2002, ILO acknowledged that workers and informal activities are not concentrated in one sector (or economic activity) alone, changing the concept to a wider one, from ‘informal sector’ to ‘informal economy’.

\(^2\) Senate’s Bulletin N° 5069-03
aim at the final link in the productive chain and hence do not reach producers, managers or supervisors of the organisations behind this illicit activity. This bill intends… to prosecute the organisations and associations devoted to illegal trade, as a way of hindering its origins”.

3. The informal sector in Chile

6. The regular measurement of said sector in Chile is made by the National Statistics Institute, which measures levels and rates of monthly employment and unemployment in the country. The source of its figures is the National Employment Survey, in application since 1986. According to it, the local informal sector accounts for nearly 40% of total employment.

7. A further estimation of the informal economy’s size and characteristics was developed by Sánchez and Labbé, following the ILO methodology and the CASEN survey for 2002. The researchers credited the informal sector with a 46% share, whereas ILO’s data pointed at a 36% share. Finally, a World Bank’s document for 2003 reported that the Chilean informal economy represented a 20% share of GNP, far below the regional average (41%).

8. All these figures betray the fact that the informal economy has not been thoroughly examined in Chile so far. Considering this issue’s importance, the Ministry of Economic Affairs is setting up a research to assess and estimate the informal economy incidence and evolution, based on a household panel data. The outcome from the first instrument is expected for April 2009.

4. The Informal Sector and Competition Policy

9. The Chilean Competition Law’s target is “to promote and defend free competition in markets”. In subsequent articles it states that “the anticompetitive illicit are any deed, act or contract that prevents, restrict or obstruct free competition, or that tends to produce these effects” in a wide sense. The following literals illustrate anticompetitive behaviour, like collusive agreements and abuses of dominant position. The Chilean statute does not consider anticompetitive conducts per se, but analyses the transgression by means of the rule of reason. In this sense the case analysis always includes the definition of the relevant market and the identification of a market power used or obtained in a wrongful way, or—in forward-looking rulings—, whose acquisition generates significant risks of abuses or of coordination in the future market scenario.

10. Due to all this, in Chile the relation between the informal economy and the competition policy is not necessarily clear and straightforward, mainly because the informal economy and informal activities seldom have a market share large enough to result in a dominant position. This is all the more true since 2007, when the Unfair Competition Law was enacted.

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4 National Socio-Economic Characterisation Survey (CASEN), used to diagnose and assess the impact of government programmes on households. This survey is carried out by Chile’s Planning Ministry.
6 This framework led to the early dismissal of a number of cases where no background for defining markets or evidence of market power was available.
11. Despite this market power concern, a review of the competition authorities’ rulings leads to identify two main issues between the informal economy and competition policy:

- an informal activity harms formal competitors directly by means of unfair practices; and
- informal agents are considered as economic agents, and included in the definition of the relevant market

12. The following cases are empirical examples of both situations:

i) Travel agency case (2000)\(^8\)

Koriana Travel was accused by the FNE of selling air tickets with a substantial discount, allegedly financed by tax evasion. The Commission regarded this conduct as unfair competition and punished the defendant with a fine.


In this case, concerning the cigarette distribution market, Philip Morris (subsidiary of the Altria Group) accused Chiletabacos (the dominant firm in Chile with more than a 90% market participation and a subsidiary of British American Tobacco) of abusing its dominant position through a series of vertical restraints, such as dealing and exclusivity contracts.

According to Chiletabacos, the ‘black market cigarette sales’ added up to around 7% or 8% of its market. The Competition Court dismissed the black market figure as an argument for diminishing Chiletabacos’ market power. This is the sole case in Chile in which the informal economy has been seen as outlining the relevant market in a competition case.

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\(^8\) Ruling n° 568 / 2000
CONTRIBUTION BY COLOMBIA
COMPETITION POLICY AND THE INFORMAL ECONOMY

--Colombia--

1. Definition of the informal economy

1. “The term “informal sector” was first coined by a British economist, Keith Hart, in a study of economic activities in urban Ghana (Hart, 973). Today, the concept of an “informal sector” seems to be replaced by “informal economy”, which includes all economic activities by workers and economic units that are—in law or in practice—not covered or insufficiently covered by formal arrangements, directing both enterprise and work relationships”

2. Several authors have developed the study of informal economies around the world for developing countries. The usual sense given to the term is brought from the Anglo-Saxon current (United States and Occidental Europe), which describes the informal as the group of economic activities that are carried out lawfully inside a market, but the resultant transactions are not counted in the national statistics and accounts, due to the fact that such activities escape from the formal registration, with the purpose of evading the control of the State either partially or totally. This definition does not include illegal undesirable activities and productive activities destined to self consumption. In order to make our contribution, this is the meaning that we choose for the figure exposed, in application to the Colombian economy and the effects generated in the market.

2. Causes, characteristics and size

3. The informal economies are generally associated with developing countries, which is the case of Latin American nations, but is not strange to developed countries either. For the first scenario, developing countries, one of the predominant factors for informality is unemployment in the formal sector, accompanied by other ones such as tax and law evasion.

4. There is a large range of causes for the increasing extension of the informal economies pointed in the study of this topic, however, we would like to aim some of them because of their significance towards this analysis in developing economies such as the Colombian one.

5. The migration of population from the country to the urban centres is one of the fundamental origins of informality. As known, the migration produced internally in a State, entails to disproportionate growth of the cities, as well as marginalised strataums and unemployment because of the impossibility to absorb the increasing offer of able work force. When these factors are congregated in the major cities, the unoccupied population might decide to produce or commercialise products and services informally, as said in the definition proposed, this production or commercialisation and the resultant products and render services are legal, but the transactions generated in the process flee out of registration, which ends up in evading a serious number of requirements, such as proper accounts and books, taxes, labour law, social security law among other serious effects.

6. On the other hand, even though at the beginnings the notion of informal economy was placed in a marginal place, not linked to the formal sector, and expected to disappear when the nations achieved sufficient levels of economic growth and industrial development, now a days is clear that the informality can not be longer considered as a temporal event. From this point, the theory of the economic cycle has

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been applied by some authors, exposing that it constitutes another visible cause for this phenomenon. In
general terms, the exposed hypothesis establishes that the successive stages that develop the formal
economy influence the informal economy. In this sense, when the formal sector is in crisis, the informal
one experiments an increment and vice versa. As seen, the relation between the two economies would be
indirectly proportional. “Furthermore, the informal economy has been observed to have more of a fixed
character in countries where incomes and assets are not equitably distributed. It seems that if economic
growth is not accompanied by improvements in employment levels and income distribution, the informal
economy does not shrink. The situation is, therefore, that the informal economy is continuously increasing
in most developing countries, even in rural areas. In all developing countries, self-employment comprises a
greater share of informal employment than wage employment”.

7. In Colombia the informal economy is subdivided depending on the activity, product or service
which is developed. For instance, we can discern informality in commerce, industry or services.

8. In commerce, informality is mostly observed in street vendors, an activity which is practiced
commonly along Latin American cities from which Colombian cities are not excluded. All kind of
products are commercialised, perhaps the only requirement is that they are easily transportable because of
the conditions of the business.

9. Informal industry, in the other hand, is mainly underground in comparison to informal commerce,
which is generally visible. “There are two kinds of informal industrialists in Latin America, one is the
formal industrialist who informalises part of his production as a result of the high cost of regulation or
taxes. Even though he may conceal part of his production, he belongs to the community of established
industrialists. In many cases the high cost of legality in Latin America has forced him to move part of his
production to the informal sector.” For the Colombian case the informality is present on both manners
mentioned above.

10. Regarding services, the usual example in developing countries is public transportation, activity
that goes hand in hand with the fact that the government is unable to cover all the needs in this field. In our
country, public transportation prices are regulated by the administration, so that the offer from the
transporters whom escape from regulation normally consists in charging less for the same service.

11. The last official statistic analysis concerning informal economies covered the thirteen (13)
principal Colombian cities during years 2001 – 2006 from April to June, and was prepared by the
Administrative National Statistic Department (Departamento Administrativo Nacional de Estadística –
DANE). This Department includes for the given study, domestic and independent workers, excluding
professionals or technicians.

12. It can be said that in Colombia an important percentage of the labour occupation is informal. In
the 90’s, the informal occupation inside the major cities was ranged close to the 54 %, from the year 1996
and ahead, this proportion rose constantly until year 2001, when the percentage is pointed in 61%. From
2001 to 2003, this participation decreased in 7 points. The last statistic revealed in 2006, showed that in the
thirteen principal cities in the country the informal employment achieves the 58.5 % of the labour
occupation. The statistics reveal an indirectly proportional relation between the increasing of formal work

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and decreasing of informal jobs, as well as frames that a 14% contributes to social security, while 76% have health insurance both paid and subsidised³.

13. The Gross Domestic Product behaviour is one of the most relevant sources of the fluctuation between formal and informal economies. Evidence points to the fact that in front of a sustainable, continued growth in the economy, a correlative reduction in the range of informality is shown.

14. However, lately a tendency has taken place in Colombian economy, constituting a paradox: meanwhile the economy is growing, unemployment increases or at least it does not decrease. This has been exposed by the Administrative National Statistic Department (Departamento Administrativo Nacional de Estadística – DANE) when comparing the increment in the Gross Domestic Product (GDP) with the raise in the unemployment rate⁴.

15. An hypothesis might be deducted from the exposed above; even though formal economy is the principal and direct source of the GDP, informal economy income indirectly fortifies this indicator, beginning with the increase in consumption power from those that accrue working informally. This track shows how GDP increment does not necessary reflects in the decrement of unemployment and can, as suggested, grow in an opposite way: while unemployment in the formal economy rises, translating hand work to the informal sector, the last one expands and contributes to the GDP.

16. “Estimates have been made of the contribution of the informal sector (i.e. not the informal economy as whole, only informal enterprises) to the GDP. These estimates indicate that the contribution of informal enterprises to non-agricultural GDP is significant. The average share of the informal enterprise sector in non-agricultural official GDP varies from a low of 27% in Northern Africa to a high of 41% in Sub-Saharan Africa. The fact that such a large number of countries in Sub-Saharan Africa have such estimates reflects recognition of the importance of the informal sector in total GDP. The contribution of the informal sector to GDP is 29% for Latin America and 41% for Asia”⁵.

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<table>
<thead>
<tr>
<th>Country (year)</th>
<th>Informal sector GDP as percentage (%) of non-agricultural GDP</th>
</tr>
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<tbody>
<tr>
<td>Northern Africa (2002)</td>
<td>27</td>
</tr>
<tr>
<td>Sub-Saharan Africa (2002)</td>
<td>41</td>
</tr>
<tr>
<td>Benin (1993)</td>
<td>43</td>
</tr>
<tr>
<td>Cameroon (1995–96)</td>
<td>42</td>
</tr>
<tr>
<td>Kenya (1999)</td>
<td>25</td>
</tr>
<tr>
<td>Mozambique (1994)</td>
<td>39</td>
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<tr>
<td>Tanzania (1991)</td>
<td>43</td>
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<tr>
<td>Latin America (2002)</td>
<td>29</td>
</tr>
<tr>
<td>Colombia (2002)</td>
<td>25</td>
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<tr>
<td>Mexico (1998)</td>
<td>13</td>
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<tr>
<td>Peru (1979)</td>
<td>49</td>
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<tr>
<td>Asia (2002)</td>
<td>31</td>
</tr>
<tr>
<td>India (1990–91)</td>
<td>45</td>
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<tr>
<td>Indonesia (1998)</td>
<td>31</td>
</tr>
<tr>
<td>Philippines (1995)</td>
<td>17</td>
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</tbody>
</table>

Source: ILO, Women and men in the informal economy – a statistical picture 2002

17. Towards the activity, the statistics show that the informality in Colombia concentrates in commerce and services, and in a minor level in industry. The first two (2) categories represent the 70% percent of the informal economy, mean while industry corresponds to the rest. In the industry, qualified work force and a minimum of capital are required, in opposition to the first classifications.

18. There are other indicators studied, such as the level of education. The population that integrates the informal sector is mostly composed by unskilled population. This participation, added to the population with primary degree education, conforms the 83% of the informal occupation.

2. Level playing field and productivity

19. As a characteristic of capitalist developing economies, the expansion in work demand does not come entailed to the same amount of work offer in the formal sector. In consequence, a huge part of the population is enforced to secure their living by producing or commercialising products or services in a small scale, with low resources, limited organisation and non entry barriers. The result of this scenery supposes insignificant productive levels, with absence of technique and accumulation, which means that both, the perspectives of real competition and the possibilities of saving, are minimum or non existent. In this frame, binding to law and all types of regulation represents enormous difficulties for this part of the population. Normally the population described dedicates to informal commerce and services rather than to informal industry.

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Informal economy constitutes a problem for the population that is affected in their minimum rights, as well as for the government because the tax income is reduced parallel to the highly inversion that has to be made to minimise the damage due to the evasion mainly towards the defenceless workers.

In diverse sceneries, the International Labour Organization (ILO) has pronounce it self about informal labour, pointing that half of the world’s workers do not earn enough to lift themselves and their families, noting an overlap of informality and poverty. “The reality is that workers all over the world face degrees of informality, the most formal of which have multiple forms of protection, the least formal none at all”

For informal industry the scenery is different; it refers to a sector of the population that might have the capital and the knowledge to participate of the formal sector, but decides to exclude itself from the regulation in order to expand their income margin or to commercialise at lower prices in the way to increase a market share or to eliminate competitors. In this panorama must been included the firms that do make part of the formal sector but leave partially informal a section of their business.

Even though informal industry represents a lower proportion than commerce and services in the informal economy in Colombia, it constitutes an important obstacle to the economic development of the country. From the moment the tax evasion begins, the measure employed by the government is raising the tributes to the formal firms, in such way that the inequality between the transaction costs for these firms and the informal ones is unsustainable. Competition, as a result, grounds on the basis of disparity.

“The effect of the informal economy on productivity and economic growth is discussed in a recent McKinsey study. Companies around the world underreport employment, avoid certain taxes, ignore product quality and worker safety regulations, violate copyright and intellectual-property laws, or even fail to register as legal entities. The problem is particularly acute in developing countries, where companies that operate informally produce as much as 80 percent of the output in some industries. Few policy makers are concerned, but they should be. By avoiding taxes and regulatory obligations, informal companies gain a substantial cost advantage that allows them to stay in business despite their small scale and low productivity. This prevents more productive, formal companies from gaining market share. The result is slower economic growth and job creation”

This lack of transparent competition affects the possibility of growth of the formal firms that, additionally, offer quality work conditions. The productivity of the country is also affected because generally the formal firms are more prolific than the informal ones, but the existence of the last ones reduce sells from the first ones, implying a raise in unused installed capacity and stock. However, is possible that informal firms become more productive, this as a result of the savings that constitute the serial evasion to law, regulation and taxes. Due to this situation, the margin might be invested in technology, which can promote efficiency. Even though, this outcome, as positive as can be seen, can’t be promoted or encouraged; to achieve this condition many sacrifices are made along the way including, as said before, the minimum rights for the workers that belong to this class of market, as well as the common interest and the solidarity that characterises the purpose of the taxation, the public order when breaking the law and the equality between equals, when competing in profuse different conditions towards the firms that fulfil all the legal pertinent requirements.

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4. **Competition law enforcement**

26. Small firms operating within informal economy are most certainly outside of the reach of the Colombian competition authority, or at least on a direct manner. A possible solution given by the competition authority would be through competition advocacy.

27. Market definition allows establishing the products that are part of a same market and between which competition appears, as well as those products that are substitutes. When a firm is part of the informal economy, it is not possible to take it into account to realise the market definition making it difficult to have a real market structure. Additionally, due to the possibility that informal firms tend to evade taxes and regulations, it is possible that they may sell products to prices under those given by formal competitors, in this way disabling formal firms to have a major market participation and preventing the competition agency to have a suitable control of the competition in a certain market.

5. **Advocacy**

28. The importance of analysing informal economies has been subject of our attention. The Superintendency is aware of the global tendency to implement remedies on this area.

29. What the Superintendency may do being a technical organism created to inspect, control and supervise, is to advice the government regarding the importance of attending the needs of these phenomenon, fulfilling the need and the obligation of this agency to stress the importance of turning the economies into a formal scenario. These kinds of matters are a State policy issue in our country. The government should, through institutions structured with this kind of faculty, adopt the needed measures.
CONTRIBUTION BY EGYPT
COMPETITION POLICY AND THE INFORMAL ECONOMY

--Egypt--
The Egyptian Competition Authority (ECA)

1. Overview

For the sake of this report, informal sector in Egypt is defined as enterprises that lack any of the following three conditions: license, registration and regular bookkeeping.

The main characteristics of the informal sector in Egypt are [1]:

- The ratio of informal enterprises to total small private sector enterprises in Egypt is 82%. This percentage is the same as 1988!

- Respectively, Trade and Services account for 38.32% and 30.74% (total 69.06%) of the economic activities in the informal sector. Manufacturing, by contrast, accounts only for 19.04%.

- Compared to formal enterprises, informal enterprises are poorer in terms of capital, employ fewer workers, and have very limited access to formal finance.

2. Causes and Concerns on Competition

- Government Regulations: Egypt applies cumbersome business entry procedures; the World Bank [1] ranks Egypt as 114 (out of 181 economies). The lengthy and taxing steps of setting/running a business provide potential opportunities of corruption, hinder investment, and push small entrepreneurs into the informal economy. The effect on competition cases is the absence of potentially important data when identifying market structure or determining market power of companies. For example, the ECA is currently conducting a study on the edible oil sector in Egypt, where we estimate that the informal sector accounts for about 11% of the market, but we have no tangible access to the specific data of that sector. However, we do know for sure that practices in this sector are largely illegal and result in the production of inedible/carcinogenic types of oil. Thus, there is also a concern on the effects of informal sector on consumers’ health.

- Lack of entrepreneurship support: Existing government’s credit programs for small business seem ineffective. The main sources of finance remain predominantly through personal/spouse’s savings (50%) and Inheritance (27.4%). Also these programs stop short from adequate training on business expansion, setting business plans, and prediction of market growth. The effect on competition is a stagnant informal sector, as indicated above. In other words, lost opportunities of new entrants that can compete more efficiently, improve products’ quality or lower prices.

- Cultural and Economic Factors: Based on [4], Egyptians prefer to act as members of a life-long group or organisation, favour rules and structured circumstances, and accept/respect
paternalistic/autocratic relationships to others based on where they are situated in formal and hierarchical positions. Also unemployment rate is about 9%, but it is highest among high educated sections (20%) than among illiterate or below intermediate (1%) [2]. This negative rate-of-return on education indicates migration of educated entrepreneurs to informal sector. Taking cultural consideration into account, these entrepreneurs would rather minimise future risks of their business by lowering their cost structures and avoiding registration with formal societal institutions. Also, they would keep their business small, funded by family and relatives and serving their local communities. The consequence on competition is, again, lost opportunities of growth which in turn could stimulate the market dynamics with new competitive entrants. Finally, the cultural dimension of “appreciating hierarchical relationship” poses a problem in acquiring qualitative data. In researching the Oil Sector in Egypt, we encountered claims of informal sector that buys frying oil from factories to later pack it and resell it for small restaurants or household consumption. Since the ECA is associated with the government it was quite difficult to verify these data from restaurant owners; the image and affiliation of the ECA was just too intimidating. To circumvent this obstacle, our investigators resorted to informal discussions with friends and those conversant with the subject. The “group” dimension of Egyptian culture, together with informal atmosphere, has paid off and the ECA could eventually acquire the needed information.

3. Methodologies and Recommendations

For qualitative data that cannot be reached through formal means, the ECA would consider alternative means of informal interviews and [seemingly] casual focus groups with relative stakeholders. For quantitative data, and economic analysis, the ECA usually adopts the information gathered from the formal sector as representative for the whole market. The justification here is that, as indicated by the discussion above, the informal sector in Egypt is fragmented, stagnant, and inefficient. Thus it poses no tangible threats on existing market powers or potential formal entrants. If anything, the informal sector represents a wasted opportunity for strengthening the competition in the Egyptian market.

In order to attract the informal sector into the mainstream business community, the ECA envisage a stronger role for the media, namely public education campaigns. The effect of such campaigns has already been felt in the Egyptian monetary sector. In 2005, Egypt has launched a nation-wide media campaign to increase public awareness of societal benefits of tax, change the attitude of tax evading persons towards the Egyptian Tax Authority. As a result, two million Egyptians filed taxes in 2005, doubling the corresponding number in 2004. Also, the tax revenue of 2006 has increased to 9% of the country’s GDP, compared to 7% in 2005. Thus, much like individuals evading taxes, we believe that cost-minimising informal sector can be swayed to join civic institutions if provided with the proper awareness and long-term benefits of such an action, e.g. access to capital, sources of finance, and power to enforce contracts.
References


ANNEX

DIFFICULTIES FACING THE EGYPTIAN COMPETITION AUTHORITY WHEN DEALING WITH THE INFORMAL SECTOR (MILK CASE)

- Lack of data/information about informal sector traders, producers and manufacturers, their relationship nature, cost structures, amounts of production, assets, distribution channels, and other needed information in order to conduct a milk market study.
- Difficulties in understanding the informal sector behaviour as the sector’s knowledge about the market isn’t at the same level of the registered formal farms, in terms of market structure, legal framework, prices of inputs, necessary administrative facilities needed as well as essential hygienic requirements.
- The informal sector does not have the culture of cooperation due to the lack of trust in the government bodies. Some of the formal sector farms or companies do not have this cooperation spirit, regarding the informal sector; the situation is even worse.
- Difficulties of sector analysis, around 80% of the drinking milk market is informal. This figure is based on estimates of the formal sector and needs further assurance.
- The perception of the unfairness of the competition law, having the formal sector claiming unfairness “are you enforcing your power against us and leaving the informal sector deregulated?” They consider this as an unfair environment.

The benefits of turning informal sector into formal:

- being under veterinary supervision will result in good quality of feeding, therefore good quality of output (milk);
- having records about the number of firms, animals, will result in reliable figures and analysis;
- increase in supply of healthy milk and dairy products;
- increase in the supply of milk will increase the competition among the market players to the benefit of end consumers.

Some advantages of the informal sector:

- there are no entry/exit barriers to the market at any period of time; given a low cost of entry (one cow is sufficient), resulting a less concentrated market (millions of producers and thousands of manufacturers);
- create numerous jobs;
- low overhead expenses and transportation costs, i.e. they distribute their products in the surrounding neighbourhood. This enables most of the informal producers to distribute their products to a big number of customers at the lowest possible cost;
- lower prices of products that a large number of the Egyptian society favours over quality.
CONTRIBUTION BY GABON
COMPETITION POLICY AND THE INFORMAL ECONOMY

--Gabon--

1. Definition

1. From a purely economic standpoint, the informal economy can be defined as all economic activities not subject to regulation and open to competition. These markets fall outside the scope of economic and social rules, as well as State intervention, and go untaxed.

2. The informal economy takes many forms, but the absence of “entry barriers” remains one of its leading features.

3. Administrative formalities and a heavy fiscal burden are the factors behind the expansion of the informal sector, which has developed to such an extent that it now competes with the formal sector.

2. Importance of the informal economy in the Gabonese economy as a whole

4. The informal economy is playing an increasingly major role and contributes substantially to the livelihood of a good share of the population in Gabon. This informal fabric of the economy covers a whole range of activities run by small craftspeople/traders, from Gabon and elsewhere in western and central African, offering goods and services at “reasonable” prices, to suit the obviously limited resources of their clientele.

5. The informal economy therefore comprises productive activities, family micro-businesses and individual initiatives.

6. The informal economy is largely dominated by commercial activities where the main players are economically independent.

7. In terms of competition, many small individual or family firms have emerged with the growth of the urban population, as opportunities arise.

8. At the same time, this expansion in the underground economy has awakened a singular taste for fraud among some of its shadier characters, particularly importers who fail to provide full invoices for the containerloads of goods they bring into the country without paying customs duties. This fraud is said to be highly detrimental to the inland revenue, but also to local producers because it gives rise to far more unfair competition than informal trade/crafts could ever do.

3. Competition in the informal sector

9. The opening up of the market and the entire economy to free competition has led to many informal economic activities, and the introduction of illegal business practices. The informal sector encompasses virtually every field of activity relating to commodities. Besides trade (wholesale and retail), the activities hardest hit by the scourge of the informal economy are “fruit and vegetables, apparel, services, crafts, passenger/freight transport and production, in particular forestry”. The most common illegal practices in the informal sector includes “uninvoiced sales”, “false invoices” and “hiring out business licences”, as well as “fronting” which is common in the pharmacy sector.
4. Application of competition law to the informal economy

10. Faced with the surge in the informal sector now affecting the Gabonese economy, the government is having to come up with answers to a host of questions that remain of great concern to experts in structural adjustment planning. A central issue here is whether or not to adopt a laissez-faire attitude, to what, and to what extent.

11. Some pundits view the emergence of the informal sector as a healthy reaction by the “market” to the interventionism prevalent in African states.

12. They also see it as a real breeding-ground for small entrepreneurs who, thanks to the support they receive and to their competitive prices, will eventually make their way into the global economy.

13. The informal sector is therefore perceived to be a vehicle for economic development, and efforts should be made to ensure that its businesses become more “formal”.

14. In short, the informal economy can be viewed as a necessary evil in developing countries like Gabon, provided there is an economic and institutional environment favourable to that sector so that it will increase its contribution to employment, production, human resource development and the social integration of those it employs.

- **Strategy No. 1**
  Adapt the legal and institutional framework to boost spontaneous development and promote free competition, as well as access to physical, financial, technical and educational resources on terms that are as beneficial to informal micro-businesses as they are to modern firms.

- **Strategy No. 2**
  Rigorously monitor the informal sector, which involves scheduling one-off inspections in sectors which are detrimental to both the formal sector and consumer health and which, by their very nature, distort free competition.

- **Strategy No. 3**
  Support for self-organisation, i.e. the gradual “incorporation” of the informal into the formal sector; this involves training for entrepreneurs in management techniques, competition and the market economy and is aimed at promoting access to the funding required to help enhance techniques and raise productivity.
CONTRIBUTION DU GABON
LA POLITIQUE DE LA CONCURRENCE ET L’ÉCONOMIE INFORMELLE

--Gabon--

1. Définition

1. Sur le plan purement économique, l’économie informelle se définit comme étant l’ensemble des activités économiques échappant à tout règlement et qui sont ouverts à la concurrence. Ces marchés échappent aux règles économiques et sociales et à l’intervention de l’État et ne font pas l’objet de prélèvement fiscal obligatoire.

2. L’économie informelle est multiforme, cependant, l’inexistence des « barrières à l’entrée » reste une de ses principales caractéristiques.

3. Le formalisme administratif et la forte pression fiscale sont à l’origine de l’expansion du secteur informel qui s’est développé au point de concurrencer le secteur formel.

2. L’importance de l’économie informelle dans l’économie gabonaise

4. Elle joue un rôle de plus en plus important et contribue de manière substantielle à la satisfaction des besoins quotidiens d’une bonne partie de la population gabonaise. Ce tissu informel de l’économie englobe une diversité de petits métiers exercés par des artisans ou petits commerçants gabonais mais aussi immigrés originaires de l’Afrique de l’Ouest et du Centre qui offrent des produits et des services à des prix “raisonnables” adaptés aux ressources par essence limitées de leur clientèle.

5. L’économie informelle est donc composée d’activités de production, de micro entreprises familiales et d’initiatives individuelles.

6. Le secteur de l’économie informelle est largement dominé par les activités commerciales dont le rôle principal est joué par les personnes économiquement indépendantes.

7. Sur le plan de la concurrence, on assiste à une éclosion de plusieurs petites entreprises individuelles ou familiales en rapport avec la croissance démographique dans les grandes villes et au gré des opportunités.

8. Parallèlement, la croissance de cette économie souterraine fait naître chez ses acteurs les plus vêteux un goût prononcé pour la fraude et notamment, chez les importateurs qui, en procédant à des sous facturations, font entrer par conteneurs entiers des marchandises sans payer de droits de douane. Cette fraude porterait un très lourd préjudice aux recettes de l’État, mais aussi aux producteurs locaux en les concurrençant déloyalement et bien plus fortement que ne pourrait le faire le secteur informel de l’artisanat et du commerce.

3. L’état de la concurrence dans le secteur informel

9. L’ouverture du marché et de l’économie nationale au libre jeu de la concurrence a favorisé plusieurs activités économiques informelles ainsi que la mise en œuvre de pratiques commerciales illégales. Le secteur informel couvre pratiquement tous les domaines d’activités productives et de services marchands. Outre le commerce (gros et détail), les activités les plus touchées par le fléau de l’informel sont « le secteur des fruits et légumes, l’habillement, les prestations de service, l’artisanat, le transport des voyageurs et des marchandises ainsi que les entreprises de production notamment dans l’exploitation forestière ». Parmi les pratiques illégales les plus courantes dans le secteur informel, on note « les ventes...
sans factures », « les fausses factures » et la « location des agréments du commerce », le phénomène de prête-noms est aussi monnaie courante dans le secteur des pharmacies.

4. **L’application du droit de la concurrence à l’économie informelle**

10. Actuellement, et devant la montée en puissance du secteur informel dans l’économie gabonaise les pouvoirs publics doivent apporter des réponses, à une kyrielle de questions qui restent des préoccupations majeures des experts des plans d'ajustements structurels. Au centre, la grande question du laisser-faire ou non, qui laisser-faire, dans quelle mesure.


12. Ils y voient aussi une véritable « pépinière » de petits entrepreneurs qui, à condition d’être soutenus, pourront, grâce à leur prix compétitifs, prendre place dans l’économie internationale.

13. Le secteur informel est donc perçu comme un vecteur de développement économique, dont il faut s’employer à « formaliser » les activités.

14. En somme, le secteur informel peut être considéré comme un mal nécessaire dans les PVD, à l’instar du Gabon à condition toutefois, qu’il soit le gage de la promotion d'un environnement économique et institutionnel favorable au secteur informel afin d'accroître sa contribution à l'emploi, à la production et à la valorisation des ressources humaines, à l'intégration sociale de ses membres.

- **Première stratégie**

  Aménager le cadre juridique et institutionnel pour stimuler le développement spontané et favoriser le libre jeu de la concurrence ainsi que l'accès aux ressources matérielles, financières, techniques et éducatives dans des conditions aussi avantageuses pour les micros entreprises informelles que celles ouvertes aux entreprises modernes.

- **Deuxième stratégie**

  Contrôler rigoureusement, le secteur non structuré ce qui consisterait en la programmation des interventions ponctuelles dans les secteurs qui portent un préjudice tant au secteur structuré qu’à la santé et à la sécurité des consommateurs et qui sont de nature à fausser le libre jeu de la concurrence.

- **Troisième stratégie**

  L’appui à l'auto organisation : il s’agit d’une « incorporation » progressive du secteur informel au secteur formel, celle-ci passe par la formation des « entrepreneurs » aux techniques de gestion, à la concurrence, à l'économie de marché et vise à favoriser l’accès au crédit qui permettra d’améliorer les techniques et entraînera un gain de productivité.
CONTRIBUTION BY JORDAN
COMPETITIVE POLICY AND THE INFORMAL ECONOMY

--Jordan--

By: Hetham Abu Karky
Legal Researcher

1. Introduction

1. Economic is the study of what we do with the things we have in order to get the most of what we want.

2. The end economic activity is to satisfy the final consumer. The greatest economic system is the one that provides more goods and services at less cost. The consumer wants to get the best possible quality of products or services and pay the least possible prices.

3. Many people, perhaps most, do not notice or care whether the product is of formal or informal economy.

4. So the informal economy is there, and it always will be, everywhere. It is wider in some countries than other countries.

2. What the informal economy is

5. We will use the example of a wool weaver, who buys the wool from a well-known and registered shop, then weave the wool to make a pullover. He paid 5 JDs for the wool and sold the pullover for 15 JDs. So the 5 JD are part of the GNP, then it is part of the formal economy. But the 10 JDs are not part of the GNP, so they are part of the informal economy.

(GNP - Gross National Products - is the total value of all goods and services produced during a year.)

6. Therefore, all illegal transactions that create products and services, all imported products secretly and contrary to law without payment of legally required duties, smuggling, all these deeds and many similar are part of the informal economy.

3. Why there is an informal economy

7. Some or all of the following, cause the informal economy:

- Poverty: The condition of being poor makes some people approach any activity that help to earn money.

- Unemployment, especially if the unemployed are left without compensation or help.

- Greed for wealth, desire for possessing or having more than one needs.

- Scarcity of goods, consumer demands, high prices, and inflation.

1 Complaints and Consultations Division, Competition Directorate, Ministry of Industry & Trade, Amman, Jordan
• High level of taxation.
• When the monopoly power is not controlled by law.
• When the competition laws are not in exercise.

4. Informal economy and Competition

8. We do not live in purely competitive economy. We will never be. We must assume a purely competitive situation in order to understand the important relationship between Supply, Demand, and the influence of these two forces on Price.

9. Adam Smith said: (If members of society are left alone to follow their own selfish interests, each person will be directed as if by an invisible hand to contribute toward the material welfare of the commonweal in ways desired by society.)

10. Many prices are controlled by influences other than competition. Government controls some prices. Business men, manufacturers, whole sellers, and retailers, all control prices too.

11. The theory of pure competition is not presented as an accurate description of our economy, but as a major influence on it. There is no seller who does not face some kind of competition, either actual or potential.

12. In competitive society, there would be problems and conflicts. For example, demand rises for an expensive kind of cigarettes. If prices made these products profitable, the result is either more factories to produce these cigarettes or more smuggling.

13. Some members of the society would be getting what they wanted but the majority of members of society would probably not benefit from such an allocation of resources.

14. Then pure competition would hardly be described in such a case as operating for the good of the wealth of the society.

15. There has never been a world in which pure competition controlled the production and sale of all products.

16. In every economy, in Jordan too, governments have been important in deciding the uses of resources. There have always been certain industries large enough to influence supply.

17. According to "Size and Measurement of the informal economy in 110 countries around the world" work paper by Friedrich Schneider, the informal economy percent in Jordan is around 19.4% of the Jordanian GNP.

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2 The paper was presented at a Workshop of Australian National Tax Centre, ANU, Canberra, Australia, July 17, 2002.
Table 1: The size of the informal (and official) economy of 26 Asian countries

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5. **The Informal Economy Effects**

18. The informal economy has a negative effect on the economic growth; it also has some positive effects as well.

   **Positive effects:**
   - Reducing unemployment rate and poverty incidence through creating job opportunities.
   - Employment in this sector is considered as a reserve for the formal sector during periods of economic recovery; store of excess employment during downturn.
   - Supplying the formal sector with many necessary goods and services.
   - Reducing the cost of living for the poor through providing goods and services at low prices.

   **Negative effects:**
   - The informal sector could be used as a venue for money laundering.
   - This sector deprives the government from an important source of revenue because the activities in this sector are not taxed.
   - The activities of this economy are not reflected in the GDP/GNP, which gives inaccurate estimation on the size of the economy and on the developments in the economy, including rates of economic growth.
   - Unjust competition due to the fact that the good and services produced in the informal economy are exempted from all taxes and fees.

6. **Government regulations**

19. The government encourages competition and protect it by means of antitrust legislation, on the other side of the coin the government is discouraging competition by such devices as tariffs, patents, fair trade laws and labour legislation.

20. Some time governments abolished enterprise and had taken over management of firms within action when they believe competition within an industry to be either impossible or contrary to the public interest.

21. As a result, when ever the government encourages competition, the informal economy decrease, and when discourses competition the informal economy increase.

22. The informal economy will be always the unknown part of the GNP, it is up to government and people to decrease it or increase it.

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3 Labor Rights in Jordan, By Dr. Mohammad Shawabkeh, [www.undp-jordan.org](http://www.undp-jordan.org)
7. Competition and the informal economy in Jordan

23. The informal economy in Jordan affects the competition in the formal economy in specific industries.

24. The informal sector usually comprises individual activities and small enterprises which are subject to the regulations of labour, including agricultural activities, household activities, maintenance, transportation, real estate brokerage, peddler’s activities, the activities of the family members who work collectively on various activities and they are not paid on regular basis as well as the small businesses which are not covered by the regulations of the Social Security Corporation. In most cases, the activities of this sector have small capital, use primitive production and marketing methods and employ unskilled workers. Therefore, we can assume that the competition could be effect in these sectors.

25. Sometimes we can notice that the formal firms and informal traders collaborate. Some formal firms use the informal traders to market goods their specially when it clause to expire date or when they are looking to effect other firms activities.

8. Competition Law Enforcement

26. There are several methods to be use to estimate the possible effect on competition from a merger in the formal economy when there is a concern about substitution by consumers to informal firms for example:

- Organise the formal sector to grant high quality of product by using a good raw material according to the national standards.

- Use machinery to save wages and time "product more cost less".

- Let the consumer realises that the quality slandered is very important and the unofficial products mostly not good even though it was cheaper than official products e.g. the informal product could not be covered by seller warranty.

- The competition authorities can contribute to solving the informality problem by lunched awareness campaign and exchange information with other authorities.

- Try to control the informal goods by cooperate with the interested authorities.

- Control markets and check the necessary licenses and permeations to practice economic activities.
CONTRIBUTION BY KENYA
COMPETITION POLICY AND THE INFORMAL ECONOMY IN KENYA

1. Introduction

1. A 1972 landmark ILO study in Kenya confirmed the existence of this parallel economy dominated by small and micro businesses that absorb a large number of persons that would otherwise be recorded as unemployed by Economic Surveys. This sector that has been referred to as the informal sector to distinguish it from the modern sector is described as consisting of "... all small-scale activities that are normally semi-organised and unregulated, and use simple labour-intensive technology... undertaken by artisans, traders and operators in work-sites such as open yards, market stalls, undeveloped plots, residential houses and street pavements. They are not registered with the Registrar of Companies and may or may not have licenses from local authorities for carrying out a variety of businesses." The informal sector has been efficient at utilizing waste materials such as old tires, scrap metal, etc. to produce goods and provide services that otherwise would have been imported or would be too expensive for low income sectors.

2. These small businesses are often started by individuals with little capital and with virtually no support from the government or Non Governmental Organisations. A government report attributes the notable growth of the informal sector to "... ease of entry into and exit from the sector and little capital investment... absence of registration and other legal formalities, and gradual shift of labour from subsistence farming to informal sector as the economy increasingly becomes market oriented". Unemployment and underemployment is another particularly strong reason to go into self-employment in the informal sector.

3. While the government and the NGOs have been satisfied at the ability of the informal sector to absorb excess labour force in the country, there has been concern regarding how most of these enterprises stagnate at the bottom and do not show signs of growing into medium and large scale enterprises. Some of the difficulties that small and informal businesses face are associated with the country’s legal structure; unavailability of capital to develop businesses, while others are related to the lack of appropriate business skills.

4. The concept of an informal economy, micro and small enterprises (MSEs) and Jua Kali
txt

are often used interchangeably. The sector is a major source of employment and income as it accounts for 72% of total wage employment and 81% of private sector employment. Its’ contribution is therefore greater than that of the medium and large manufacturing sector.

5. A majority of MSEs are micro-enterprises with fewer than 10 employees, while 70% of them are one person, own account workers. This infers that majority of MSE enterprises are operating at the bottom of the economy, with a significant percentage falling among the 53% of Kenyans living below the poverty line.

1 The views expressed herein are those of Mr. Francis W. Kariuki, the Acting Commissioner/CEO of the Monopolies and Prices Commission of Kenya and Ms. Beldine Omolo, Head of Enforcement. They do not necessarily represent the position of the Commission.

2 Jua Kali means hot sun. It depicts operations by informal businesses in the open, sometimes under the scorching sun.
2. The Dairy sector: A case study of milk vendors

6. The informal dairy sector of Kenya is one of the most dynamic sectors in the economy, creating more jobs than the formal dairy sector. In cognisance of the above, new research has been conducted with the aim of demystifying the myth that milk sold through informal channels pose public health risks. The Government has been urged to recognise the existence of the informal sector and license its players. About 55% of all milk marketed by some 600,000 small-scale farmers is actually sold directly by farmers to neighbouring consumers and institutions. Raw milk traders are estimated to handle about 1/3 of the total marketed milk, with only 8% sold directly to processors.

7. Because the informal milk sector is creating employment in the often-forgotten rural areas, as well as urban areas, the implication of this research is that the government should redesign the rules of the game to enable the sector to create even more jobs. The jobs are being created in the mobile milk trace (bicycle delivery – exclusively for young men mostly of age 20-35), in milk bars, shops/kiosks and small processors.

8. Issues of public health in the informal milk markets came to the fore after a study conducted by the Ministry of Agriculture and Livestock Development, Kenya Agriculture Research Institute (KARI) and the International Livestock Research Institute (ILRI) in 2000. The findings showed that up to 96% of households in Kenya boil milk prior to its consumption, which when likened to pasteurisation, ensures that all harmful bacteria are destroyed hence making the milk safe for consumption.

9. The report acknowledges that although there is some degree of adulteration of milk supplied through the informal channels, there was no obvious link between milk quality and the type of market agent, and there may not be serious harmful effects in the milk that eventually reaches the consumers. “Adulteration of milk through addition of water may introduce chemical and microbial health hazards as well as reduce the nutritional quality, palatability and market value of milk,” says the report. Overall, only 10 percent of all milk tested was found to be adulterated, most cases occurring in the dry season when there is milk shortage.

10. Another major health risk is the large number (up to 15%) of both pasteurised and raw milk samples that contain antibiotic residues. The negative implications of this are that over time, there is the possibility of patients developing of drug resistance, which then would call for more expensive antibiotics and place a strain on the national budget. This requires training particularly of dairy farmers and veterinary assistants as well as drug suppliers. Training of all milk traders in quality control, including use of proven hygienic handling methods, is the main pre-condition for licensing.

11. The formal and the informal dairy sector relies to a very large extent on marketed surplus from the smallholder dairy producers which in 1997 was estimated at 1,093 million litres, says the report. Of this amount only 12 percent passed through pasteurisation and “formal” marketing while the remainder – about 88 per cent – was sold raw through direct sales to consumers and hotels through co-operatives, self-help groups and small traders.

12. The small-scale market agents include milk bars, shop/kiosks and mobile/itinerant traders, sold, on average sell 50-120 litres a day. The agents pay farmers prices that are 7 to 65% higher than those paid by the processors and charge the consumers 20-50 % less per litre for raw milk compared to what consumers of packaged milk pay.

13. The consumer preference for raw milk is reflected in Nairobi as well as other urban centres. This trend is spurred by the inefficiencies associated with the formal milk processors. Even when the sector was under the monopoly of Kenya Co-operative Creameries, the organisation accounted for only 25 per cent of
the marketed milk. The formal dairy sector is less vibrant because of stringent regulations on quality control and packaging. There is also the large capital outlay needed to set up processing and cooling plants. The informal dairy sector also thrives on the fact that vendors make prompt payments for milk at the farm gate and they also sell at competitive prices.

3. Public Transport- the case of Matatu Transport Providers

Public transport in urban Kenya is dominated by Matatu vehicles. The term Matatu, which means “thirty cents” in local vernacular, was a standard charge for every trip made in the early 1960s. In 1973, the Government in response to lobbying from Matatu operators declared that Matatus were a legal mode of transport and could operate without obtaining Public Service Vehicles (PSV) licenses except to comply with existing insurance and traffic regulations. Initially, the Kenya Bus Service - which was jointly owned by the United Transport Overseas Ltd (75%) and the Nairobi City Council (25%) - existed since 1934 as the sole legal provider of public transport services in the five major towns. It was, however, not able to cope with the increase in demand for transport services and this encouraged the growth of the Matatus from 17,600 in 1990 to 40,000 in 2003. The vehicles comprise mini-buses with sitting capacities ranging from 14 to 40 passengers. They provide employment and generate revenue for the Government in the form of license charges, duty, VAT and other taxes. In addition, the industry plays a leading part in transportation of both persons and goods in rural and urban areas.

Unfortunately, the industry’s vast growth has been accompanied by increasing road traffic accidents which are caused by among other factors, reckless driving, unroad worthy vehicles, poor road conditions, laxity of law enforcement, vested interests, poor driving skills and poor working conditions. Road accidents are the third leading cause of death after malaria and HIV/AIDS and are at present a major public health problem in terms of morbidity, disability and associated health care costs.

The Matatu sector has 4 trade associations each furthering different interests of its members. The Matatu Vehicle Owners Association (MVOA) or MOA was formed in 1973 to allow owners the control of operations of the sector. The formation of the Matatu Welfare Association (MWA) in 2001 and the Matatu Stage Welfare Association serve the interests of drivers, conductors and other stage workers. Route-based Savings and Credit Cooperative Societies (Saccos) serve as welfare organisations that pool resources and redistribute them through credit schemes, organise route operations and address members’ welfare concerns. Most of these Saccos were affiliated to larger organisations like MWA and MOA. The route-based organisations are generally stronger than the national bodies like MWA and MOA in articulating the concerns of the industry.

At the competition level, the Monopolies Department has had few problems with the sector associated mainly with fare fixing and route allocations. Some of their activities e.g. extorting goodwill charges from unsuspecting matatu owners in order to be allocated a route to operate in, are predatory in nature. Most of the players including their Associations have no fixed abode and therefore Department finds it difficult to serve notices on them.

The informal matatu business has thrived on the fragmented nature of the institutional and organisational structure of the transport industry. The Kenya Roads Board (KRB) which is the main institution responsible for the national road infrastructure network in Kenya, the Transport Licensing Board (TLB), Motor Vehicle Inspection Unit, Registrar of Motor Vehicles, Driving Test Center, Traffic Police and Local Authorities are under different ministries hence the lack of harmony in policy implementation.

In 2002/3, the government undertook two measures to correct the situation. First, it developed the integrated national transport policy and secondly, it introduced reforms in the operation of public service
vehicles. These measures are for the purposes of reducing accidents, enhancing safety of commuters, ensuring responsibility, accountability and competence of drivers and conductors; eliminating illegal drivers, conductors and criminals that had infiltrated the industry; and facilitating the identification of vehicles and restricting their operation to authorised routes. The following provisions were provided:

- installing speed governors to control speed to 80 Kph for vehicles whose weight exceed 3,048 Kilos;
- fitting seat belts on all public, commercial and private vehicles;
- employing drivers and conductors on permanent basis;
- issuing badges and uniforms to PSV drivers and conductors;
- indicating route details and painting of yellow band on Matatus for easy identification;
- re-testing of drivers after every two years;
- prominent display of driver’s photograph together with their identity card details;
- regular inspection of motor vehicle for tests and certification.

20. The provisions have not been effective because of:

- lack of proper enforcement by traffic police;
- discriminatory nature of rules which target only Matatus;
- high expenses of institute the safety measures;
- reduction of income for the operators owing to the fact that the seating capacity of the vehicles was reduced from 18 to 14 passengers;
- additional costs owing to inspection charges by the Vehicle Inspection Unit;
- the enhanced regulatory requirements increased the possibility of extortion for bribery by the principal enforcement agencies.

21. However some progress has been noted after the implementation of the reforms:

- most Matatus have been issued with compliance certificates;
- MOTC in collaboration with the National Road Safety Agency has been conducting the National Roads Safety Awareness campaign on radio, TV and newspapers as well as using billboards;
- reduction in accidents by about 73% in the first six months of implementation of the legal notice;
- restoration of sanity and order in the Matatu industry;
- defective vehicles have been eliminated;
- cartels have been eliminated or reduced by disbanding illegal groups and placing management of PSVs in the hands of their owners;
- the government has further directed all local authorities to take over management of bus parks within their areas to help remove cartels from the routes;
- two new insurance companies have started providing insurance cover to Matatus;
• crime rate has reduced owing to the requirement that all PSV drivers and conductors must possess certificates of good conduct from the police. The same requirement has also led to elimination of unqualified drivers who were major causers of accidents;
• interest is now being shown in the sub-sector by NGOs and private sector players such as insurance firms that are sponsoring seminars and workshops in safe driving for owners and workers.

4. Street Trade

22. Street traders are a sub sector of the MSEs that dominate the Kenyan economy. Recent Baseline Survey indicates that there are over 1.3 million MSEs which contribute 18 per cent of Kenya’s Gross Domestic Product [GDP]. The survey states that about 64 per cent of the MSEs are in trade, under which street vendors fall. This sub sector is engaged in buying and selling of goods. Income from the trade sub-sector is ranked lowest among the MSE sector, but they are vital to the livelihoods of many urban and rural poor. These micro trade activities are sometimes referred to as ‘survivalist’ enterprises - they allow entrepreneurs to survive with hardly any savings. The sector is a major source of employment and income and about 48 per cent of the operators are women.

23. The Kenya Labour Force Survey Report of 1998/99 indicates that the sector covers all semi organised and unregulated activities that are small scale in terms of employment. The report notes that the activities are largely undertaken by self-employed persons or employees with few workers in the open markets, in market stalls, in both developed and undeveloped premises, in residential houses or on street pavements [Labour Force Survey, 2003].

24. One outstanding feature of street trade in Kenya is that it is viewed as anti competitive, even predatory because vendors block entrances to shops and sell similar merchandise and at lower prices than the shopkeepers. The low prices are partly attributed to the fact that the vendors do not pay taxes, neither are they obligated to pay rent and other overheads costs that the formal traders incur.

25. The Local Government Reform Programme [LGRP] of 1999 focused on a key policy areas such as reduction of poverty and unemployment, and promoting higher rates of economic growth. The reforms had three components:
• improving local service delivery;
• enhancing economic governance; and
• alleviating poverty through increasing efficiency, accountability, transparency and citizen ownership.

26. Its immediate policy focus is the removal of unnecessary regulatory barriers and the reduction of costs of doing business. In particular, the government initiated two nation-wide reform efforts, namely: the Single Business Permit [SBP] and The Local Authority Transfer Fund [LATF]. The SBP in relation to small businesses is a response to business licensing problems faced by MSEs. Business licensing is aimed at protecting consumers from exploitation, health and safety hazards and control of business activities.

27. Business licensing imposes costs on businesses that are often out of proportion to the benefits delivered. Further, in practice, the regulatory provisions are abused and have become merely income earning opportunities for those charged with enforcing the regulations [Devas and Kelly 2001]. While the move to have a SBP is appreciated, it has largely benefited the small and medium firms and not micro firms where the street traders fall. The micro firms have had ad hoc policy responses from both the central
and local government levels. These responses have included relocation of street traders and affirming

government commitment to the sector.

28. On the issue of policies and regulations, most urban authorities in Kenya operate on colonial by-

laws that have yet to be reviewed. The policies are deficient and the urban authorities have not only failed
to enforce them, but in reality, given their form and coverage, they have not been possible to enforce.
While the basic idea is that licensing which is intended to enable entrepreneurs to conduct their businesses
productively and profitably, it has become a stumbling block. In spite of the number of people who can be
licensed being limited, once the license is given, it is shrouded with many other outdated restrictive
requirements relating to public health, building requirements, and other regulations outlined in the Local
Government Act. This has resulted in most traders evading licenses, and therefore flouting most
regulations laid down by authorities. There is need for local authorities to put in place relevant policy
frameworks and reviews of the existing by- laws if they have to conform to government policy of
enhancing the performance of MSEs. A few urban councils have reviewed the by- laws relating to street
trade. Other councils continue to put emphasis on enforcement without clarity on policies and regulations.
The councils have not hit a balance between order, and promoting the activities and performance of
informal sector operators such as street traders. Some view street traders as a temporary problem, bound to
disappear, although experience has shown the contrary. The inability to address the issues is intensified by
lack of effective organisation among street traders, especially in the area of representation and advocacy on
issues affecting them.

29. The 2002 - 2008 Kenya Development Plan indicates measures aimed at ensuring control and
regulation of hawking within the Central Business District. Most urban local authorities have begun
implementing this policy with due to lack of adequate space for all street vendors within the CBD. For
instance in the case of the CBD of the capital city of Nairobi, where over fifty thousand street traders
operate, the city has only managed to set aside sites that can accommodate about 7,000 traders. This move
is positive, although the tenure remains unclear, with the urban authorities viewing the sites as temporary
while the vendors view them as permanent. Although the urban authority had a plan to charge some fees,
this has not been possible due to a mix up in allocation. There were cases of double allocations, infiltration
by those not allocated sites and hostility directed at the City Council Authorities. This has resulted in a
stand off situation that can only be solved through dialogue and negotiation. Most of these sites lack
infrastructure and services and are congested. The congestion is due in part to infiltration by vendors not
allocated sites, and also by vendors allocated unfavourable sites where there is insecurity and fewer
customers. These are aspects that should have been taken into consideration before relocation. Past
experience of ad hoc street traders relocation indicate that without critical consideration of access to
customers and security, relocation efforts will continue to be resisted.

30. In the relocation process, associations have not been effectively used, partly due to their
fragmentation and weakness. The city authorities opted to use representatives of street traders drawn from
different areas of the CBD. The role of these representatives was largely to listen to the packages being
offered by the authorities, as opposed to negotiation and dialogue. Their ‘listening’ role and failure to
negotiate for appropriate relocation sites and an efficient allocation process made most street traders feel
betrayed. The relocation policy would have been more successful, if the street traders had a unifying body
advocating and negotiating on their behalf. Ensuring a dynamic MSE sector requires functioning
associations that support entrepreneurs, lobby and dialogue with authorities for enabling MSE policies and
programmes. Associations are useful for purchasing raw materials, marketing, bulk transport, sharing tools
and equipment, guaranteeing loans, providing market information and linking up with training and
business service providers.
5. Sector Reforms

31. The Sessional Paper No. 2 of 1992 notes that the role of Government in the development of the sector will be one of facilitator rather than that of interventionist. This is due to the fact that there has been concern that in attempting to intervene to help it “grow” its dynamism, ruggedness and innovativeness may be affected. The enabling environment the government has already established or proposes to establish includes investment allowances for starting new factories outside the major cities, duty exemptions for the purchase of capital machinery for small enterprises located in rural areas, support for technological assessment of innovation, developing market incentives to encourage subcontracting to small enterprises and reducing the harassment of the entrepreneurs operating on public land or sites, setting up vocational training centres for apprenticeships etc. Several NGOs and local banks have also attempted to assist small sector entrepreneurs to access credit for start ups and expansion of their businesses.

32. Over the years, the Government has continually recognised the role of the informal economy in several policy documents. Under the Development Plan of 2002, various rules and regulations that affect the operation and growth of the sector were reviewed. Other policy responses have included: elimination of trade licensing at Central government level; harmonizing, rationalisation and implementation of Single Business Permit (SBP); and on-going review of labour laws; relaxation of business regulations; broadening access to finance; the enactment of MSE Act; and measures aimed at ensuring control and regulation of hawking within the Central Business Districts of major towns. Under the Economic Strategy for Wealth and Employment Creation (2003-2007), the government committed itself to address factors responsible for the poor performance of productive sectors, which include: high cost of engaging in productive activities, high cost of capital particularly for MSEs and lack of supportive and weak institutions. The initiative was to be achieved by removing various regulatory impediments that increase the cost of doing business, promoting MSEs by finalizing and implementing a Sessional paper on the sector, focusing on employment creation and formalisation of informal activities.

33. The strategy paper further states that the formal and informal sectors in Kenya are basically the same, and the only difference being size. The latter are however denied essential services as well as infrastructure as they do not pay taxes. The Paper proposed to eliminate this dichotomy by providing infrastructure and services, particularly financial, to small and medium enterprises and by ensuring that they pay taxes.

34. In the past, the emphasis on the formal private sector has exposed the private informal sector to the vagaries of bad governance, dominated by inefficiency and rent seeking bureaucrats and policy makers. Such officers have been more concerned with rent seeking rather than ensuring the formalisation of adequate policies and efficient implementation of policy provisions. The Policy concern therefore has been how to provide equal opportunities to both the informal and formal sectors of the economy as their integration would lead to one vibrant economy.

35. Under Vision 2030, Kenya’ aims to be a newly industrializing “middle income Country providing high quality life for all of its citizens”, the government has therefore committed itself to “raise the market share of products sold through formal channels (e.g. supermarkets) from the current 5% to 30% by 2012…..this will also contribute an additional Kshs.50 billion to the GDP. At producer level, the plan aims at building “Producer Business Group” (PBGs) which will in turn feed large wholesale hubs principally in the rural areas. These hubs will be “Tier 1” retail markets which will provide the primary producer with better value than at present when markets are heavily fragmented.”
CONTRIBUTION BY LITHUANIA
COMPETITION POLICY AND THE INFORMAL ECONOMY

--Lithuania--

1. In 2005, the Competition Council of the Republic of Lithuania (further – CCRL) conducted an investigation of a cartel agreement in the taxi passenger carriage service market in Vilnius. The entities operating in the market were established to have been engaged in practice which could be assessed from the point of view of “informal” economy. The CCRL conducted the investigation within the limits of its competence, i.e. exclusively on the basis of the provisions of the Law on Competition (LCRL) therefore the provisions and some of the considerations presented below concerning the informal economy may be considered as assumptions only, rather than as facts or an a priori evidence.

2. The investigation was started by the CCRL ex officio after, in September 2004, representatives of the Vilnius Association of Taxi Service Providers (VATSP) through mass media were publicly urging carriers of taxi companies to increase the taxi fares. The CCRL issued a written warning to the heads of the Association to the effect that such incitements contradicted provisions of the LCRL. Despite the warning, the passenger taxi fares were simultaneously and equally raised (the investigation established that the decisions to simultaneously increase the fares were passed in the meetings of the VATSP).

3. At the close of 2004, there were 60 taxi companies operating in Vilnius under the licence issued by Vilnius Municipality. At the time the companies were fiercely competing for passengers and as a result, many of them were charging fares below cost (taxi fares in Vilnius at that time were among the lowest in Europe). This could primarily be accounted for by their informal operations seeking to disguise the actual revenues thus avoiding paying the State taxes. In reality, very few of all legitimately operating companies were behaving in a “civilised” way, i.e. were in an orderly manner paying taxes to the State. The market leader UAB Martono Taksi had over 100 own vehicles complying with the relevant international standards in 2004, it was employing drivers, paying them regular salaries and was properly managing its accounting records. UAB Martono Taksi was among the founders of the VATSP. Surprisingly, it was this company that acted as an initiator of the cartel agreement. In its explanations to the Competition Council the company pointed out that the public inducement to increase the passenger carriage fares was a means to draw the attention of the respective institutions to the illegal operations of most of the taxi companies in Vilnius that do not pay the respective taxes to the State or salaries to the drivers they employ, i.e. are involved in informal activity.

4. In this respect it is notable that according to the then effective laws and the procedure governing the operations of passenger carriers that are assigned to the area of municipal regulation, taxi companies were still not subject to the requirements in compliance with the European Union standards. For instance, a taxi company holding an appropriate operating licence and registered as a private company (UAB) was not required to have own vehicles, i.e. the company could hire private carriers with their own vehicles. The make of vehicles and their manufacturing year (depreciation degree) were virtually not regulated. Such taxi drivers were required to pay to the private company a small (token) fee and could retain the balance of the fees received from the passengers without declaring the actual income. According to the Law on Value Added Tax effective at the time to acquire the status of a VAT payer the annual income of an operator must be not less than LTL 100,000 (EUR 28,962). Thus when approaching the threshold some informal taxi companies would wind up their operations and establish a new (subsidiary) company. Under the circumstances the initiator of the cartel agreement – UAB Martono Taksi was not in a position to compete on equal terms with other taxi firms acting informally.

5. Having completed the investigation in February 2005, the CCRL concluded that the Association of taxi service providers and some of the companies providing taxi services in Vilnius had infringed the
requirements of Article 5 of the LCRL – having concerted their actions in the beginning of October 2004 unanimously increased the passenger carriage fares, i.e. committed concerted actions that contradict the provisions of Article 5 of the LCRL. A total of ten taxi companies of Vilnius were acknowledged as having infringed the LCRL and were subject to fines for the committed prohibited actions – conclusion of agreements which aim to restrict competition or which may restrict competition including the agreements to directly or indirectly fix prices of goods (services) and fix other purchase or sale conditions. UAB Martono Taksi was acknowledged to have acted as an initiator of the prohibited agreement and was subjected to the largest fine.

6. The companies – members of the Association of Taxi Service Providers, in disagreement with the Resolution of the CCRL, appealed the Resolution to the court. The Supreme Administrative Court of the Republic of Lithuania that passed the final decision in the case ruled that the companies providing taxi services in Vilnius concluded, by means of concerted actions, a prohibited agreement concerning the service fares that distorted competition in the taxi service market and were damaging consumer interests.
CONTRIBUTION BY MONGOLIA
INFORMAL ECONOMY EFFECT ON COMPETITION IN MONGOLIA

--Mongolia--

1. There are statistical evidences showing an increasing role of informal economy since 1990 where Mongolia transferred from centralised economy to market economy. For instance, during middle of 1990-s informal economy comprised less than 5% of GDP whereas according to the statistical data 2004, it reached 11.3%. However, some informal reports confirm that it was more than 11.3% and might have reached even 40%.

2. Therefore, we would like to briefly discuss meat market as meat is mostly supplied by informal sector to the market.

   Meat market:

3. Our country consumes about 250 tons of meat yearly, 12.7% of which is prepared and supplied by formal sector, i.e. enterprises, and the rest (87.3%) is by informal sector which means hand prepared. In other words, meat market is a unique market that is basically occupied by the informal sector.

4. Product market of the product is not limited by one another, as they can replace each other (cow, horse, goat, sheep, and camel meat) and therefore can make up a common market. In the market research, geographical market of them defined to be Ulaanbaatar as a whole one market.

5. Hand preparing process belongs to informal sector for it includes mainly not registered, part time workers who don’t pay tax, social insurance, and middle men or ‘profit reseller’.

6. Meat preparing process for the meat to consume by Ulaanbaatar contains following stages:

<table>
<thead>
<tr>
<th>Stage</th>
<th>Hand prepared/Informal sector</th>
<th>Prepared by industrial method (manufactured)/ formal sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stage 1</td>
<td>Negotiate with local herdsman /in countryside/ on price and buy livestocks from him/her</td>
<td>Negotiate with local herdsman /in countryside/ on price and buy livestocks from him/her</td>
</tr>
<tr>
<td>Stage 2</td>
<td>Supply to and butcher in stocks from central and western provinces the wholesale market at west edge of Ulaanbaatar, and stocks from eastern province to ‘Nalaih’ wholesale centre at the west edge of the city.</td>
<td>Prepare/ butcher stocks, and supply to relevant shops.</td>
</tr>
<tr>
<td>Stage 3</td>
<td>- Between 9 and 10 middle men at wholesale markets such as Nalaih, Huchit shonhor and Emeelt resell their products they bought early in the morning, to salespersons of Huchit shonhor or salespersons of other city markets and retail shops. - or they personally transport them to retail shops.</td>
<td></td>
</tr>
<tr>
<td>Stage 4</td>
<td>- Salespersons from retail food shops purchase meat graded/ sorted and prepared in Huchit shonhor - Middle men personally transport the meat to shops and sell it.</td>
<td></td>
</tr>
</tbody>
</table>
7. In the first stage, herdsmen prefer to sell their stocks to middle men /informal sector/ as to manufacturer for number of reasons such as many kinds of documents they asked to provide.

8. Cost per 1 kilogram meat shown in the table. /As an example, average price for sheep and beef is displayed/: /as of 1.12.2008 1USD=1165¥/

<table>
<thead>
<tr>
<th></th>
<th>Hand prepared</th>
<th>Manufactured</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Sheep</td>
<td>Beef</td>
</tr>
<tr>
<td><strong>Stage 1</strong></td>
<td>3000</td>
<td>3500</td>
</tr>
<tr>
<td><strong>Stage 2</strong></td>
<td>3150</td>
<td>3800</td>
</tr>
<tr>
<td><strong>Stage 3</strong></td>
<td>3650</td>
<td>4300</td>
</tr>
<tr>
<td><strong>Stage 4</strong></td>
<td>3770</td>
<td>4500</td>
</tr>
</tbody>
</table>

9. Based on the data above, we can see that manufactured meat cost more than hand prepared meat. Although in terms of quality and hygiene, manufactured meat is far better, customers tend to buy more from hand prepared meat.

10. Moreover, the fact that they can hand prepare meat and supply them on less price than otherwise is a leverage in competition to others and encourages therefore to run a ‘unregistered’ business.

11. For reasons above mentioned, tax, social insurance structure and standardisation requirements individuals tend to run an informal business. Thus, manufacturing method is not still prominent. By providing services and products that meet consumer immediate need Middle men and Profit reseller /business men in informal sector/ make their living. Although that is a source for living for many people, government is putting more importance in transforming informal into formal sector.
CONTRIBUTION BY PAPUA NEW GUINEA
COMPETITIVE POLICY AND INFORMAL ECONOMY

--Papua New Guinea--

1. **Introduction**

1. Papua New Guinea (PNG) has a relatively small dual economy, comprising a formal and informal economy.

2. The formal economy is dominated by large-scale resource projects, particularly in mining and petroleum, and through tax and royalties provides a large proportion of government revenue.

3. The informal economy supports 85% of the people through semi-subsistence agriculture. The formal sector employs around 15% of the workforce.

4. PNG has an abundance of natural resources including:
   - Large reserves of minerals
   - Extensive forestry and fishery assets
   - Significant potential for agricultural expansion

5. The informal economy is characterised by local trade stores, market gardeners and other small agriculture operations, fisherman and local markets.

6. Village-based agriculture supports over 70% of the population, and domestic trading of fresh produce is a very important source of cash income.

7. By far the most important crops in PNG are sweet potato, bananas, yams and taro which comprise the dominant staple food for over 75% of the rural population.

8. The main agricultural export commodities are timber, oil palm, coffee, cocoa and coconuts. Forestry is PNG's third largest revenue earner and a major contributor to economic and social development. Much of this production is undertaken by small landholders within the informal economy, trading with local intermediaries who then deal with the larger factories and production houses in the formal economy. There is also a significant trade in betel-nut (a stimulant which is widely used in PNG) which operates only in the informal market, through street vendors.

9. PNG has several significant competitive advantages in relation to the production of timber - available land, good soils and climate, and a long history of successful incorporation of trees into agro-forestry systems.

10. The forestry and mining sectors are export oriented and are dominated by international or multinational enterprises. While there have been many instances reported where traditional landowners’ interests are said to have been ignored or environmental and other regulations have been disregarded by mining and forestry operators, those issues are not relevant to the discussion in this paper.

11. The PNG fisheries zone of 2.4 million square kilometres is the largest in the South Pacific. The fisheries zone includes an extended reef system, numerous islands and an extensive coastline. These create huge opportunity but also present an enormous challenge for monitoring and control. The total market
value of the PNG catch is estimated at $A140-160 million, a significant proportion of which is traded through the informal economy, rather than being supplied to fish canneries or otherwise going into the formal economy.

12. Pigs and poultry are important village animals within the informal economy and there are some live exports of cattle from PNG from larger producers within the formal economy.

13. There is particular need to develop the informal sector (including those involved in village level production and marketing of root and horticultural crops, small livestock), to improve the productivity of major tree crops (increase production and exports, lower production costs), and to support research and development that assists in diversification of the agricultural export product base.

2. PNG Competition law

14. PNG has been an independent nation since 1975. For many years it was thought that the economy had not developed enough to warrant competition law.

15. Furthermore it was felt that part of this lack of development stemmed from the fact that the informal economy was so large and that that economy did not warrant or need such regulation.

16. There was some limited consumer protection law and price control. Furthermore with most utilities being provided by the national Government, time was not ripe for competition law. Industry was largely Government run or controlled.

17. However with the move to privatisation of some utilities and the development of the PNG formal economy, competition law was introduced. That process commenced in 1996.

18. Competition Policy and Industrial Policy became part of the same goal, economic efficiency and consumer welfare.

19. The policy was to open up markets to imports, foster exports and generally encourage competition. Further, industries that lacked competition, often through the small size of the market creating natural monopolies, were subject to regulation by the competition regulator, including price control in some limited circumstances.


21. The competition provisions, referred to as the Market Conduct Rules, are based on those in the New Zealand Commerce Act and are similar to the competition provisions applying in most developed economies. Broadly speaking, the Market Conduct Rules prohibit arrangements which substantially lessen competition (with a per se prohibition of price fixing); resale price maintenance; exclusionary conduct (primary boycotts); and misuse of market power (abuse of dominant position). Anti-competitive mergers or acquisitions are also prohibited. Authorisation by the ICCC on public benefit grounds can be applied for – a small number of authorisations on public benefit grounds have been approved by the ICCC since 2003 for business acquisitions or anti-competitive arrangements.

22. The law is tailored to meet PNG needs. In particular there are provisions regulating PNG monopoly (government owned) utilities. There is also provision for price control, though the number of products which are currently subject to price control or price monitoring is very few.
23. In effect the ICCC Act has an overall competition and consumer protection mix. In addition the Act has extensive and some unique provisions relating to essential utilities which affect the bulk of PNG consumers.

3. **Competition policy and the informal economy**

24. Generally the PNG informal economy ignores economic regulation such as the competition and consumer law. One principal reason for this is geography; PNG is one of the least urbanised countries in the world, with upward of 80% of the population living in non-urban areas. It is in those localities that the informal economy mainly operates. Many of these localities are in remote areas where access is difficult, frequently with no road access and no telephones or other ready means of communication. In such places it is not possible for the ICCC, as the competition and prices regulator, to operate, nor are commercial goods and services readily available.

25. Thus while in PNG there is still some price control, it has been very difficult to police such law in the informal economy. For instance, the wholesale and retail margin for petrol is price controlled and in local areas trade stores sell petrol, rather than service stations, but their cost structures, freight costs and other factors make the imposition of maximum margins irrelevant and impossible to enforce anyway.

26. We see the informal economy as having only a limited impact on the formal economy. The informal economy is critical on the one hand for feeding the PNG population in both rural and urban areas, and on the other hand for providing the source of much of the products for export.

27. As a competition regulator the ICCC does not ignore the informal economy. However we see little reason or opportunity to enforce competition laws in that economy, even though our law covers all PNG commerce. Much of what happens in the informal economy is guided by traditional culture and not competition dictates.

28. We do however seek to inform the informal economy about our roles and how competition law may assist the informal economy *vis-à-vis* the formal economy.

29. Some of the informal economy has formed itself into co-operatives, in areas such as growing coffee, oil palm, vanilla and other similar agricultural products for export, and these bridge both economies. It is at this intersection of the informal and formal economies that the ICCC has potential competition issues with co-operatives as distinct from the members of the co-operative. For example, some processing co-operatives tend to rely, in their dealings with individual growers, on market sharing, price fixing and other anti-competitive arrangements between processors, to the potential detriment of the growers. However, growers with limited education or knowledge of their rights are often happy to receive a fixed price from one processor for their product, notwithstanding that they may well be able to get a better price if processors were competing to purchase their raw products.

30. We expect over time that the gap between the two economies will diminish as more of the informal economy will either feed into the formal or create corporate structures that move into the formal. There have been examples in the last two years where participants in the informal economy have been moving towards the formal. Street vendors who in the past have been selling food and handicrafts have, since the introduction of competition in mobile telephone networks, begun selling pre-paid telephone cards, which have now become a high proportion, by value, of those street vendors’ business. This has caused those vendors, and their customers, to become more aware of the existence of regulation in the formal economy.

31. We at the ICCC will assist in that transition, including ensuring that anti-competitive conduct does not impede the transition of the informal sector or hamper it in any way.
32. In many ways the informal sector is the cultural backbone of PNG and a competition and consumer agency has to assist to foster the country’s economic culture towards the international, globalised economy in which we all now operate.
CONTRIBUTION BY PERU
COMPETITION POLICY AND THE INFORMAL ECONOMY

--Peru--

1. Introduction

The Political Constitution of Peru (1993) rules that the State promote and guarantees to firms and consumers their participation in the market governed by the principle of free competition and free private initiative.

Under an economy of social market model, the role of the State is not reduced, but oriented to supervise and promote the investment, taking part only in the provision of goods and services when the private sector is not able to supply them and or to mach the demand of basic needs (health services, education, basic infrastructure, and the likes).

The constitutional frame guarantees the free competition and protects consumers, and it allows design policies and practices as instruments to reach these economic and social objectives.

In effect, academics argue that in a competitive market, the consumers will benefit from low-price goods and services, better quality and product diversity. The competitive process allows consumers to choose the product according to their needs and budget restriction.

On the other hand, the companies may obtain benefits because the market forces them to be more efficient. In competition, the companies will reduce their total costs of production (productive efficiency), increase the quality and diversity of their products or services and provide to the consumers products with prices near their costs. As a result, competitiveness of the companies will increase with the possibility of successfully taking advantage of a process of economic integration (e.g. Free Trade Agreement).

Finally, the government will also be benefited. The competition will expand the national product because of the increase in tax collection, or the availability of more budget resources. This will make possible for the government to be in better position to finance the provision of public goods and services, allowing citizens to access to these ones and improving their living conditions.

Theoretically, in order that an economy may work close to a competitive market and, therefore, obtain more efficient results, the following conditions are necessary:

(i) the existence of many suppliers in such a way that can not influence negatively in some commercial conditions;
(ii) goods are the most homogenous possible;
(iii) consumers have enough information so that they can make their better consumption election; and
(iv) there are few trade barriers in the market.

Nevertheless, markets are imperfect, on the contrary, they have failures (i.e. natural information asymmetries, monopolies, anticompetitive behavior, high entrance barriers, product heterogeneous), which prevent that market agents reach their objectives with efficiency. For these reasons, the state may intervene establishing and executing policies that allow obtaining efficient results in a competitive market.

1 Juan A. Candela Gómez de la Torre, Presidente de la Sala 1 del Tribunal de Defensa, de la Competencia y Propiedad Intelectual (INDECOPI), Lima, 16 February 2009
In addition, competition and practice policies have as objective to contribute with markets in which competition is possible and desirable, assigning economic resources for the benefit of consumers, companies and the government. It also generates social efficiency.

In Peru, at the beginning of the 90s, the government created a legal framework to protect and promote the market competition, and to protect consumers and intellectual rights. The leading institution INDECOPI appears as an administrative agency within a national system. It roles is to arbitrate and promote the market development, applying competition policies with the objective of correcting some of the failures that can be observed in the market working against the normal development of the competitive process. Thus, for example:

- It applies the free competition regulation to prevent the anticompetitive behaviour that produces an artificial deviation of the competition market, by the arbitrary agents who abuse of their position of dominion.

- The information asymmetries that increase the costs of transaction in the consumption relations, which fought by the Commission of Consumer Protection

- The Commission of Bureaucratic Barriers Elimination fights the trade barriers imposed by the State thought acts or normative devices that constitute an irrational or illegal barrier to access to the market.

- The lack of products and services homogeneity is object of the Control and Standardisation Commission of no Tariff Commercial Barriers.

As it is mentioned previously, we will analyse how the informal economy existence affects the application of Competition Policies by the Competition Authority.

2. What is the Informal Economy?

It is true that there is not an exact definition or concept to define and conceptualise the phenomenon. Usually, the concept use depends of the aim and scope of the study.

The modern and accepted definition is that the informal economy is part of everybody’s daily life. In fact, it is a reality of the world, exists everywhere and gets larger everyday. It exists in less development countries as development ones.

The economic development theory tries to explain the causes of underdevelopment by using the dual analysis of the economy. For instance, rural and urban sectors have also been divided into formal and informal sectors. This designation was not intent to contribute to an academic proliferation of labels; was merely an analytical terminology to describe a duality that avoids the bias against the low-income sector inherent in the traditional-modern dichotomy. Both sectors were qualified as modern; both were the consequence of the urbanisation process that has been take place in different LDC’s. Academics used the terms “large-scale” and “small-scale”, but those terms were purely descriptive and no saying anything about why one sector is large-scale and the other is small-scale.

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It was added that

“one important characteristic of the formal sector is its relationship to the Government. Economic activities formally and officially recognised and fostered by the Government enjoy considerable advantages. First, they obtain the direct benefits of access to credit, foreign exchange concessions, work permits for foreign technicians, and a formidable list of benefits that reduce the cost of capital in relation to that of labour. Indirectly, establishments in the formal sector benefit immeasurably from the restriction of competition through tariffs, quotas, trade licensing and product and construction standards drawn from the rich countries or based on their criteria. Partly because of its privileged access to resources, the formal sector is characterised by large enterprise, sophisticated technology, high wage rates, high average profits and foreign ownership.

In addition, it was written that

“The formal-informal analysis applies equally well to the agricultural sector. The parallels are obvious and striking. The division between operators with licenses and those who does not have licenses in urban areas is reproduced in agriculture between those who grow tea and coffee with official punishment and those who do it illegally. Their similarity to urban squatters is obvious – both are irresistibly drawn to real or perceived sources of wealth, despite legal restrictions of access.

Some authors said that this concept is related to illicit activities in general (e.g. illicit traffic and drug production, smuggler, and the likes) and illicit

### Picture 1

<table>
<thead>
<tr>
<th>TYPES OF ACTIVITIES OF THE INFORMAL ECONOMY</th>
</tr>
</thead>
<tbody>
<tr>
<td>TYPE OF ACTIVITY</td>
</tr>
<tr>
<td>Illicit activities</td>
</tr>
<tr>
<td>Tax’s Evasion</td>
</tr>
<tr>
<td>Tax’s Elusion</td>
</tr>
<tr>
<td>Illicit activities</td>
</tr>
</tbody>
</table>

Source: Schneider, F and D. Enste (2002), “Hiding itself in the shades, the growth of the underground economy” Subjects of Economy the IMF. Peruvian Institute of Economy.

But, from the institutional theory point of view, it is understood that institutions are those forms to think, to act and to feel, that members of a society share, and that allow them to interact under more or less predictable rules. Under this concept, the role of the institutions is to reduce the costs of transaction in the social and economic relationship. In this sense, Douglas North has stated that “institutions would be the rules of game in a society; or formally talking, they are the human restrictions that model human
interaction”

On a first stage of the society, when social relations were less complex, the coexistence norms that rule the behavior between the members of the locality were based on consuetudinary rules. When the society relationship became more complex, it was needed the creation of rules that established how the market behavior should be, and, mainly how to make them effective, in order to be able to avoid social conflicts between the market agents. In this scenario, the State was born thought its power in order to create rules that will govern the economic and social relations, monopolising its execution based on the law regimen.

From this point of view, the informal economy can be defined as those:

“activities that are based on illicit acts to be carried out (...) they are activities that intrinsically do not have a criminal content, but , in spite of being allowed activities in a country, have to use an illicit behavior to be carried out”.  

Moreover, on an interview given by the anthropologist Jaris Mujica, who lived in one of the poorest and marginal districts of Lima, in order to analyse the informal market of cellular phones, he defined as:

“The word Informal means all those practices, systems and orderings of local, economic and familiar structures that do not work within the structural legal formality, nor within the legal processes and either within the correct process of an Ethic’s Codes.”

It is possible to affirm that as a whole the word “informal” means that in a society there are activities which exist outside of the law. Thus, for example, the case of the “pirate taxi drivers”, whom without being registered offer a transport service to the public. As it is possible, its purpose is allowed as a way of living, and with their work simultaneously they are offering a public service; however, the ways they are using are illicit because they do not count on the respective license, probably without paying taxes and without following environmental regulations. Therefore, in spite of the allowed purpose, the activity as a whole is illicit because is unprotected by the law.

In the informal economy, economic agents can be observed from the supply side or the demand side. The formality for companies could mean a high cost that will reduce competitiveness to them, reason why it turns out more beneficial to stay in the parallel market. In addition, all supply responds to a demand, therefore, if an informal supply exists is because a group of consumers who buy at this market exists, probably because it is less expensive for them.

In this respect, Jaris Mujica says:

“When these informal practices are no longer controllable or when the cost of the control is greater than the benefits the company receives, the let fight itself. As a consequence the interrelation between the informal and the formal begin to coexist until the point that some companies cannot subsist in the formality if they are not supported by informal practices”.

6 Interview published in El Comercio on September 27th, 2008
7 Ibid
In that sense, the informality is not a problem that is exclusive of the developing countries, but also, of the developed countries. As an example, is only enough walking by the streets of Miami, Rome or Madrid where the informal ambulatory commerce is for immigrants a way of living.

2.1. The cost of formality and informality

According to Doing Business 2009 studies, in countries where it has been observed a more onerous regulation for the economic agents, and where the trade barriers are, the informality levels increased. In that sense, it has been affirmed that:

“The investigations generally reveal that in countries with an overwhelming regulation display, an informal sector of high dimensions, higher unemployment rates and a slower economic growth.”

In that sense, the policies that the State rules in order to insert measurement to the economic agents at the formal sector will depend on their efficiency, but at the same time of giving legal norms that will govern the economic relations. For that reason, it has been indicated that the informality is not other thing that the inefficiency of the law.

“The origin of the informality (...) is found in the inefficiency of the Law. In technical terms, we are informal by the cost of the legality. The politicians, the legislators, and much less, the lawyers do not understand that the law costs like any other thing (...) a prosperous country has a low law cost in comparison with the income of the population; a country that is not prosperous has a low cost.”

Following the classic economic theory, if we begin with the premise that the economic agents are rational in taking their decisions, making a cost-benefit analysis; then, it is possible to affirm that in an excessively onerous legal frame, the election of the agents to remain in the informal sector is rational, because it is less expensive for them, even if they take into consideration the possible fines and sanctions that the authority can impose to them if they are detected in the informality.

Therefore, Ghersi argues that the informality is not -as it is implicitly affirmed in some texts of sociology- part of the idiosyncrasy and Latin American towns’ inheritance that comes from our indigenous and colonial past. In other words, the problem of informality existence does not have its foundation in a cultural problem, a religious dogma or an ethnic origin. The problem of the informality has its origin in the inefficiency of its own legal ordering and, finally, in the State that not creates an efficient normative frame that stimulates the companies to act and to operate within a frame of formality.

2.2. The cost of formality

The costs of the formality are divided in two (2) groups: the costs of the formal sector access and the costs of permanence.

In relation to the access costs usually it is mainly related to the bureaucratic barriers that the own administration imposes. An example will allow us to illustrate it. In 1983, the economist Hernando De Soto made a study taking as a model a dressing factory at an industrial zone of Lima. With this purpose, a work group was hired to begin and complete all the necessary legal proceedings without paying the bribe.

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8 Doing Business 2009. World Bank
10 Ibid
unless this was necessary to continue with the experiment. Results of the study showed that the whole process took ten (10) months and employees were asked for bribes in ten (10) opportunities, and in two (2) of them, they had to pay the bribe in order to get the licenses.

Additionally, a total of US$ 194,400 payments among rates and other requirements had to be done. The legal cost of registry was equivalent to thirty two (32) times a vital minimum wage. In comparison, another group was in charge to do the same procedure in New York and Florida, which took between 3 and 4 hours, respectively.\textsuperscript{12}

Consequently, it is possible to argue that the costs of the formality depends on the normative frame, and also implies the following concepts: (i) the incurred expenses to obtain the qualifying titles to operate in the market; and (II) the cost of opportunity translated in the time and allocation of resources for the fulfilment of the legal exigencies.

On the other hand, once an economic agent has accessed to the formal market, its relation with the state regulations does not end there, it follows with a great number of norms and costs of remaining in the formality.

According to De Soto, the term, in a broad sense, includes the costs imposed directly by the legislation such as the taxes, the payment of labour rights, the accomplishment of certain administrative proceedings, and the likes. In addition, there are costs indirectly imposed by the legal institutions as the instability of the legal system and the inefficiency of the Justice System to solve the possible conflicts that happen between the economic agents. The permanence costs have been divided in groups: tax burden and tax bureaucratic regulations and bureaucratic or administrative processes requirements.

As it is known, taxes that a formal firm must pay are the main income source for developing countries. The control of the tax authority is easier when a formal firm is registered, but it does not happen with economic agents who operate informally. For that reason, the informal firms or firms that develop part of their activities informally have a competitive advantage forehead the companies that fulfil their taxes obligations.

According to the Doing Business study in 2009, in countries where the taxes are high and the benefits come from their taxes, the informality tends to be increased. For the economic agents, the decision of following or not tax regulations do not only depend on what onerous is the level of the tax rates, but also how complex are the administrative procedures for the fulfilment of the tax obligations.

\textit{“The economies that are in the first level, and offered taxes facilities usually count on lower business taxes. In addition, they have simple administrative taxes processes for a tax declaration”}.\textsuperscript{13}

For that reason, in order to struggle the informality stimulating the fulfilment of the tax obligations, the State must give an integral reform establishing low tax scales and the best legal frame.

On the other hand, there is another type of regulation that affects the costs of the permanence of the economic agents in the formal sector that is related to the labour costs.

In effect, in countries where the labour norms impose strong limitations for dismissals or work schedules, the companies are going to avoid completely the minimum labour norms, operating in the informality. In that sense, governments must look for equilibrium between norms that offer certain

\textsuperscript{12} Ibid
\textsuperscript{13} Doing Business (2009) World Bank
protection to the workers avoiding social conflicts and those that allow the flexibility in the labour market with the objective of reducing the competitiveness at the formal companies and stimulate the growth of the informal sector.

In this regard, the study Doing Business 2009 says:

“at the developing countries, it is frequent that the regulators are mistaken towards an end, the excessively regulations contribute to increase the informal sector. This model is evident in Venezuela and Bolivia: both have laws that prohibit the dismissal of workers by economic causes and both are between the five economies with a big percent of informal sectors...”

The high labour costs, especially in the developing countries, cause formal firms to be less intensive in the use of the work factor for their production and, on the contrary, induce the agents who have capital assets to use it in an intensive way.

Finally, these costs of permanence could determine that the economic agents assign their resources to have a better knowledge of how following the regulations, which finally could give as a result that the permanence of the companies in the market depends not as much on the efficiency of its productive process, but how efficient is their relationship with the government”.

2.3. The informality cost

There are two groups of costs for being informal. The first one is about the costs from the punishment that is imposed when the authority detects an informal activity, and the second one is referred to the impossibility of being benefited with the goods and services provided by the State.  

In effect, the informal agents provide certain amount of resources with the object of not being detected, and not being punished by the State. Generally, these punishments are hard enough and imply in most of the cases a considerable part of what they own (e.g. the informal manufacturers of pyrotechnics), reason why many agents destine part of their patrimony in bribes, which also stimulates the government corruption. Additionally, with the purpose of making up or attenuating their existence in the market, the companies reduce their efficient production for not being detected.

On the other hand, the informal agents are disabled to benefit from the services that the government offers in the market, specially, the services of the judicial and legal system and from security forces. In effect, considering that the informal activities are outside of the legal frame, the informal industrialists cannot completely have their own property rights. In that sense, in the informal sector, the transaction cost is increased due to the uncertainty of its execution.

In addition, other cost of the informality considered refers to the reduction in the internal investment and that originating one of the markets of capitals. In effect, according to an study made by De Soto, the families, who lacked a property title or had a unstable title in Peru, did not invested much in the construction of its own house until the property of the land -where they lived- was adjudged to them legally.

In relation to the reduction of the market’s investment, this one was pronounced in the following inefficiencies: i) the high interest rates that the informal economic agents paid; ii) the low value of appraisal destined to the informal activity, and iii) the difficulty to transfer the property and to create

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3. Impact of the informality in Peru

According to the arguments that have been said, the magnitude of the informal sector in Peru would be equivalent to a 35% of the PBI (GDP); whereas a 60% of the working hours are developed in the informal market.

From the social and economic point of view, Ghersi has concluded that the informality in Peru is high. If 60% of the toiled hour-men are in the informal sector, then the government only controlled four of every 10 hours that the Peruvians worked; this means that the Peruvians worked 6 hours outside the Law. In addition, in spite of its quantitative importance, of the preceding data, it is concluded that the informal sector has a low productivity, since 60% of the work only make 35% of the production.

4. Origin of the informal economy in Peru: The migratory phenomenon

De Soto, argues that the economic and social changes that have taken place in Peru, began with different migratory events that determined that the population of the country began itself to concentrate in the cities, whereas the rural areas were remained vacated virtually. In a period of almost 40 years, from 1940 to 1981, it is observed that almost 2.4 to 11.6 million of the urban population have been increased whereas the rural populations only increased in a third (4.7 to 6.2 million). This means that in 1940 two (2) of each three (3) Peruvians were living in rural areas, whereas in 1981 the figure is reversed and two (2) of each three (3) live in the city. It comes off from next chart:

<table>
<thead>
<tr>
<th>Year</th>
<th>Urban Population (%)</th>
<th>Rural Population (%)</th>
<th>Total Population (Millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1940</td>
<td>35,4</td>
<td>64,6</td>
<td>7,1</td>
</tr>
<tr>
<td>1961</td>
<td>47,4</td>
<td>52,6</td>
<td>10,4</td>
</tr>
<tr>
<td>1972</td>
<td>59,5</td>
<td>40,5</td>
<td>14,1</td>
</tr>
<tr>
<td>1981</td>
<td>62,2</td>
<td>34,8</td>
<td>17,8</td>
</tr>
<tr>
<td>1993</td>
<td>70,1</td>
<td>29,9</td>
<td>22,6</td>
</tr>
<tr>
<td>2005</td>
<td>72,6</td>
<td>27,4</td>
<td>27,9</td>
</tr>
</tbody>
</table>

These migratory surges were stimulated by the deep differences that have existed between the city and the rural area, mainly in the provision of basic services and the opportunities of better life conditions. Thus, for example, in the study of De Soto, it is mentioned that the migrations were stimulated by the low rates of infantile mortality that existed in Lima, because of the improvement of the services and medical covers in the city.

Another factor that has been mentioned is the opportunity of a better salary, thus for example, it is mentioned that in 1970, a worker who left the rural area to be used as worker in the city received a high salary.

Another factor that explains the migratory phenomenon is the high degree of centralism that has

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existed in Peru during its republican history. In effect, the growth of the Public Administration, were an attractive reason for the countryside settlers who looked for being close to the political decisions; as well as looking for opportunities to work like private sector or government employees.

Finally, according to De Soto, the most important factor that increases the migratory phenomenon is the difference in the educational level that existed between rural and the urban areas.

Nevertheless, the migration was not an easy change for the settlers who moved from rural areas, because they would find a hostile reality. In the first place, they had to face negative feedbacks for the traditional high class, that in the facts were translated in a social and racial segregation.

Perhaps, the most important obstacle that was faced by the immigrants was that the enterprise sector was not able to create the sufficient jobs for the increasing supply of manual labour of the rural immigrants. At the present time, the enterprise sector has the same problem for immigrants, the urbanisation-industrialisation matrix have not let work as a factor of attraction for the immigrants, who see in the city as an opportunity of integration to the modernity or as a way to have better jobs in order to improve the quality of life.

Nevertheless, not all the people have been able to have a job in the city, as an example, the following he has pointed:

“In certain cases, it is common that the companies do not resort to the work market to contract workers, because they prefer to hire people “recommended” by their own workers, in order “to place” relatives, friends, countrymen, or others.”

This determined that the marginalised immigrants of the formal labour market, by the incapacity of the state and the enterprise class, saw themselves in the necessity to auto generate their own entrance through the informal economic activities such as the ambulatory commerce, (e.g. pirate transport), etc.; which did not require of a specialised and described knowledge, but a lot of effort and sacrifice.

The phenomenon was denominated “the marginal pole of the economy” that includes economic activities made by immigrants whom not had the opportunity to be inserted satisfactorily to the layers of the labour and social formality. This is the group of people that it has been able to generate a deep change in the social, labour and economic relations in the conservative and traditional cities.\textsuperscript{18}

From another point of view, informal sector appeared in Peru because the economic grow model that focused into exploit natural resources to export raw material likes minerals. Big corporations concentrated their activities in certain rural areas almost without linkages with other local activities. On the other hand, main manufacture and trade firms began to develop their production activities (60%) mainly in Lima, the capital of the country. This was the main cause of the migratory process and the origin of the informal sector in Peru.

5. **Policies adopted for reducing the informal economy**

The government has taken a set of policies to reduce the informal activities. These include legal measures to reduce burden tax, administrative tax procedures, labour and product regulations and administrative processes for setting and operating firms.

Decrease of informality does not need the establishment of a strict punitive system because it will be

fruitless if Public Administration does not additionally count on an adequate and effective supervision system that timely detects the violation to law. In addition, besides that, a merely repressive system could give to the informal economic agents an incentive to invest in sophisticated mechanism for covering up and increase the corruption of public officials.

The Administration should foster the passing of policies in order to insert informal agents to formal sector by reducing access and permanence costs.

The last Peruvian Administrations have made important steps. For example, in tax policy, The Government enacted the Legislative Decree 771 by means of it was created the named Unique Simplified Regime (RUS) which had as a general objective to simplify the fulfilment of taxing duties in favour of the citizens and make it easier its management for Tax Administration. The principal objective was to expand the number of taxpayers by incorporating into formality to persons and small business that were performing economic activities in the informal sector. The mechanism used was to establish a unique and flat payment for considering accomplished the obligations related to income tax and value added tax without needing the presentation of tax declaration neither registration of accountant books.

In the field of land property, the Government has created the Bureau for The Formalisation of the Informal Property – COFOPRI as public decentralised entity in charge of designing and enforcing (in an integral, comprehensive and fast way) a program for the formalisation of land property (land possession in state land property) and their permanence in the formality. In fact, is not only important to grant titles of property to the precarious holders as COFOPRI has done in the last years, but additionally it should be established necessary mechanisms in order to avoid formalised real states go back to informality. For instance, many programs in Africa for grating titles have been fruitless because new owners started to informally buy and transfer real states, because costs for transfer mean almost 10% of the value of the property and it takes ninety (90) days to get the registration. Besides that, the register publicity system granted little security to the property. The policy of formalisation allows as a first step to access to the legal property but it also makes possible that many people can register an asset that permit to register and organise companies which can obtain loans from financial institutions.

In the labour market, the Government has passed the Law 28015, Law for the Promotion and Formalisation of Micro and Small Business, which seeks formalising this kind of enterprises by establishing a Special Labour Regime, which in principle has an objective to reduce some labour costs, the number of paid vacations, the value of indemnity for arbitrary firing, etc. The following table shows a comparison between the Special Labour Regime and The General Labour Regime:

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Table N 3

<table>
<thead>
<tr>
<th>REFERENCE</th>
<th>GENERAL REGIME</th>
<th>SPECIAL REGIME</th>
</tr>
</thead>
<tbody>
<tr>
<td>REMUNERATION</td>
<td>S/. 500.00</td>
<td>S/. 500.00</td>
</tr>
<tr>
<td>WORKING DAY</td>
<td>8 daily hours or 48 hours weekly</td>
<td>Same</td>
</tr>
<tr>
<td>WORKING AT EVENING</td>
<td>Minimum Vital Remuneration + extra 35%. Form remuneration over S/. 675 the extra is not applied.</td>
<td>If it were habitual, it would not be applied.</td>
</tr>
<tr>
<td>DAY OFFS AND HOLYDAYS</td>
<td>24 hours and payment for overtime.</td>
<td>Same</td>
</tr>
<tr>
<td>VACATIONS</td>
<td>30 days, reduction to 15 days for &quot;buying of vacations&quot;.</td>
<td>15 days, reduction to 7 days.</td>
</tr>
<tr>
<td>ARBITRARY FIRING</td>
<td>1 and 1/2 remuneration per working year. Limit of 12 remunerations. Fractions are paid in twelfth and thirtieth.</td>
<td>2 remunerations per working year. Limit 6 remunerations. Fractions are paid in twelfth.</td>
</tr>
<tr>
<td>SPECIAL INDEMNITY</td>
<td>2 remunerations per year. Fractions are paid in twelfth and thirtieth. This is only for workers of the General Regime that are retired and replaced for workers of the Special Labour Regime (article 57 of Law 28015).</td>
<td>This is not.</td>
</tr>
<tr>
<td>SOCIAL SECURITY</td>
<td>Worker is a regular</td>
<td>Worker and manager are regular.</td>
</tr>
<tr>
<td>PENSIONS</td>
<td>The workers decide the pension system.</td>
<td>Worker and manager additionally decide if they pay to pension system.</td>
</tr>
</tbody>
</table>


Taking as a base the Minimum Vital Remuneration, the new Special Labour Regime will mean a saving of costs for micro business, such as it could be observed in the following table:

Table N 4

<table>
<thead>
<tr>
<th>Issue</th>
<th>General Labour Regime</th>
<th>Special Labour Regime S/. Month</th>
</tr>
</thead>
<tbody>
<tr>
<td>Minimum Vital Remuneration</td>
<td>500.00</td>
<td>500.00</td>
</tr>
<tr>
<td>Familiar Assignation</td>
<td>50.00</td>
<td></td>
</tr>
<tr>
<td>Gratification July &amp; December</td>
<td>91.66</td>
<td></td>
</tr>
<tr>
<td>CTS 8.33 %</td>
<td>53.47</td>
<td></td>
</tr>
<tr>
<td>Vacations (1/12)</td>
<td>45.83</td>
<td>20.83</td>
</tr>
<tr>
<td>Social Security 9%</td>
<td>61.87</td>
<td>43.87</td>
</tr>
<tr>
<td>TOTAL</td>
<td>802.83</td>
<td>567.70</td>
</tr>
</tbody>
</table>
Finally, in the field of administrative simplification of bureaucratic procedures, the Government has made advances by passing the following regulations:

- **The Law of General Administrative Procedures – Law 27444** – which stipulates the following:
  (i) the principle of simplicity as an authority’s duty to establish easy proceedings and ask only for rational and proportional requirements; (ii) the obligation for passing a Unique Text of the Administrative Proceeding which contains all the proceedings before an entity; (iii) a proceeding of automatic approving subject to post supervision; (iv) a prohibition of requiring some determined documents such as one that the entity already obtained in a precedent proceeding; (v) the establishment of a limit for fixing fees of the proceedings that can not be superior to the real costs of the service.

- **The Law of the Administrative Silence – Law 29060** – establishes a regime of positive administrative silence for:

  (a) requirements in order to exercise pre-existing rights or develop economic activities that require previous authorisation from the Administration, subject to that public interests are not negative affected (e.g. public health, environment, natural resources, public safety, etc.)
  (b) appeal for questioning the denying of a request or administrative acts, unless the cases described before; and
  (c) proceeding in which the significance of the final decision does not have an impact on third parties.

### Informality, consumer protection, competition defense and protection of intellectual property

As it was appointed, Indecopi, as competition authority, acts in its role of arbitrator and promoter of the free market economy model, helping to correct the market failures (by *ex post* and *ex ante* intervention) that are able to restrict the functioning of the competitive process.

In that sense, in the following sections it will be analysed how Indecopi intervene in the markets from the perspective of its respective functions, keeping in mind the premise that both the formal agents and informal ones are under the scope of Indecopi’s competences.

**Consumer Protection**

According to the Legislative Decree 716 – Protection of Consumer Act, a consumer is

> a natural person that, in acquiring, using and enjoying a good or contracting a service, acts in a field different to a professional and business activity; and, exceptionally, a micro enterprise that shows a situation of asymmetry of information with respect of its provider related to services and products not concerning with its object of business.

In that sense, the problems related to the commercial relations established by the consumer with the providers (retailers) are focused on information asymmetries and, consequently, lack of suitability of the product. Indeed, in a consumption relation, the provider of a specific product has major and better information about its qualities and characteristics, and if that product is suitable in order to satisfy the consumer’s expectations. Through many modalities, the provider can hide relevant information to consumers, so it can produce a risk that sub-optimum commercial relations appear in the market, which would not have existed with adequate information. The inefficient result of this kind of transactions means that consumers will not allocate their limited resources for a better value in order to satisfy their unlimited needs.
As it can be inferred, the central issue is to form well-informed consumers and providers that believe in the advantage of acting with correction in the market by following the rules of loyal and free competition. This becomes particularly difficult if it is taken into account that there are a group of activities and agents that act in the informal sector; however, this does not mean that Indecopi does have competence to resolve conflicts arising from informal consumptions relations or on the fringes of the institutional (which does not include criminal offences).

Nonetheless, the Indecopi’s main difficulty to solve conflicts derived from no formal transactions lies on proving the consumption relationship. In those transactions generally a proof of payment or any other document is not issued, so consumers are not able to prove they contracted a service or acquired a good from an specific supplier (even when it is informal). In general, these kind of transactions are closed by word or based in confidence when there have been previous operations.

Finally, it is important to point at the case of informal transactions, which consumers generally have the capacity to know about the risks derived from them, and even so, those consumers decide to assume them because of the lower price. Under this concept, the consumer could assume that any intention of complaining before Indecopi could be more burdensome in terms of money and time in comparison with the price that has paid for the good or service.

**Defence of Free Competition**

When there are cases that affect the competitive process through conducts of abuse of dominance and collusive practices, the competition authority will investigate and, eventually, punish, independently if the accused economic agent has activities in the formal or informal sector.

It is important to mention, as we did before, that an informal firm does not take advantage of scale economies because it precisely attempts to stay small in order to avoid of being detected and punished. Therefore, it is unlikely to observe in the market an informal agent that has dominance position. In the same way, because of the size of informal firms and the magnitude of their transactions, it is unlikely the incentive to engage in a collusive practice.

However, it is a paradox that in some cases it is possible to observe the presence of informal firms that have discouraged and made it failed the execution of anticompetitive conducts.

Indeed, in a case between the Chamber of Commerce of Lima vs. the Transporters Owners of Trucks Union (UNT Peru) and other trade transportation groups. The Technical Secretariat of the Commission observed that in the market of inter-cities transportation of persons and cargo was unlikely the existence of a collusion by the imputed formal transportation enterprises, because fixing a high concerted formal price would be discouraged by the lower informal price.

Therefore, there was a significant presence of informal suppliers so the formal ones would have the following options:

(i) To try to establish collusive agreements and mechanism of supervision including everybody or the great majority of providers (informal or formal);
(ii) If the previous option is not possible because of the intervention of the Administration or the high presence of informal, the formal agents resort to make lobby between the authorities looking for a protectionist regulation.
(iii) If the previous option is not possible because the intervention of the Administration is declared unconstitutional by the Constitutional Tribunal or another reason, then it will be more beneficial for the formal agents moving to informal sector.
As it could be inferred, the markets with a significant presence of informal agents are those where generally, the barriers to entry are low and the supply side is atomised. Therefore, the Competition Authority should not worry about monitoring these markets since it is unlikely the existence of anticompetitive conducts.

Finally, it is important to appoint that we could not deny the importance of informal sector inside the market economy in Peru. In that sense, when a specific anticompetitive conduct is analysed, the authority of competition should not leave out the presence of informal agents, first, when it determines the relevant market and, consequently, the market power that let them cause a major injury for the general economic interest.

Supervision of the Loyal Competition

The special Commission is in charge of enforcing the Law of Repression of Disloyal Competition – Legislative Decree 1044 – that punishes the business and trading practices (including those from advertising activities) against the good faith that has to guide the free competition in the competitive markets.

As in the last section, the Commission has competence to resolve cases of disloyal competition, independently if the parts execute activities in the informal sector.

A conduct that is punished under this Act is the modality described in the article 14 of the Legislative Decree 1044 that refers to the acts in violation of law. This modality of act of disloyal competition punishes to the economic agents that gain a competitive advantage by breaking any imperative regulation; for instance, a specific rule that orders to obtain a certification to operate. Therefore, this supposition is directly applied to the economic agents that act in the informal sector and by virtue of that, they obtain a competitive advantage.

The repression of conducts of disloyal competition in the modality of acts in violation of law helps to discourage informality since competitors injured with that conduct are able to bring charges against the offender. And, it discourages that injured competitors reply by breaking the law, too.

In 2005, a case involved enterprises of GLP (LPG) commercialisation in cylinders. The Tribunal of Indecopi punished to Alfa Gas because it obtained an anticompetitive advantage breaking the Regulation for GLP Commercialisation, passed by Supreme Decree 01-94- EM. In this case, the regulation established that enterprises of GLP commercialisation were banned of trading their own products using the cylinders that belong to their competitors, unless that (i) they have subscribed an agreement of “co-responsibility” and (ii) the agreement have been put into knowledge of the Minister of Energy and Mines. In this case, it was proved that Alfa Gas would be using the distinctive cylinders of its competitors for the commercialisation of its own product.

Supervision of Dumping

A Commission is in charge of correcting distortions on competition because of importation with a price under dumping. If national producers considered that are injured with the importation of similar products with dumping prices, they could ask the Commission for an evaluation of the market in order to determine the existence of the practice and a damage that causes to national production, and then, to impose antidumping rights.

By means of the action of the Commission, it could be avoided that the national producers has the incentive to operate part of their activities in a no-formal way, in other words, breaking labour,
environmental, tax regulations in order to reduce their production costs and, doing so, to be able to compete with the low prices of the imported products.

By the imposition of antidumping rights, the imported products will enter to the country in the same competitive conditions than goods produced in Peru by formal enterprises.

**Elimination of Bureaucratic Barriers**

There is a Commission which is in charge of monitoring acts and dispositions issued by the Public Administration that do not constitute an illegal barrier or an irrational barrier to the access or permanence in the market for private agents. These barriers are related to the demand of requirements and charging; or impediments and limitations to the performance of the economic agents.

In that sense, it is evident the importance of the functions of the Commission for the purpose of removing bureaucratic barriers that are able to constitute an obstacle for making the economic agents get into the market.

For example, there is a study about Rates of Access to Market 2007 – 2008 elaborated by the Technical Secretariat of the Commission and the Department of Economic Studies of Indecopi. In this study, it was observed that in relation to the passing of a TUPA only the 50% of a group of local governments had accomplished all the legal obligations related to this administrative tool (the first place was obtained by the Municipality of Callao).

Likewise, it was observed that 58,3% of the local governments fulfilled with creating the proceeding for the license of operation by issuing a municipal regulation, as it is established in the Law 27444. However, it was verified that the 70,8% of them had included that proceeding in their TUPA’s. This means that 12,5% municipalities had not fulfilled with creating that proceeding according to law, but they had included it anyway. Finally, the 47,9% of the municipalities approved the tax for the right of licence proceeding by issuing a regulation; however, the 75% of them had already included in their TUPA’s which means that 27,1% had included that tax without having approved it according to law.

To summarise, through resolving and monitoring actions, the Commission has taken care that the costs of access and permanence in the formal sector do not increase by actions of the Public Administration. In that sense, it has to be more beneficial for economic agents to keep themselves in the formality.

**Intellectual property and informality**

Indecopi has three (3) Directions of Intellectual Property: (i) The Direction of Distinctive Signs; (ii) The Direction of Investigation and New Technologies; and (iii) The Direction of Author Rights.

In the Peruvian market, it is possible to observe that a high number of no-formal transactions are related to the infringing of Author Rights, mostly, by reproduction of DVD’s and CD’s in audio and video called “pirate products”.

For instance, in the following table it is possible to observe statistics estimations of piracy made by Department of Economic Studies of Indecopi in the report called “The phonographic industry and piracy in the Peruvian Market: 1999 – 2003”:
Table Nº 4

<table>
<thead>
<tr>
<th>AÑO</th>
<th>CD (Unidades)</th>
<th>KCT (Unidades)</th>
<th>INDICE DE PIRATERIA</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Mb</td>
<td>V</td>
<td>d</td>
</tr>
<tr>
<td>1999</td>
<td>2 314 506</td>
<td>2 458 082</td>
<td>nd</td>
</tr>
<tr>
<td>2000</td>
<td>6 607 176</td>
<td>1 364 271</td>
<td>382 235</td>
</tr>
<tr>
<td>2001</td>
<td>22 903 180</td>
<td>2 366 828</td>
<td>2 294 325</td>
</tr>
<tr>
<td>2002</td>
<td>50 946 262</td>
<td>888 549</td>
<td>1 638 389</td>
</tr>
<tr>
<td>2003</td>
<td>81 625 301</td>
<td>826 606</td>
<td>2 525 560</td>
</tr>
</tbody>
</table>

Where: “Mb” represents the total imports of CD’s and/or cassettes unrecorded; “V” represents legal sales of CD’s and/or cassettes which recorded in the national market; “d” represents the total of confiscated stuff by the authorities; “c” represents the percentage of unrecorded CD’s that were used to carry out reproductions different to musical purposes. In that sense, it can be inferred from previous data that by 2003 it existed a level of piracy between 98.5% and 98.7%.

The Direction of Author Rights is in permanent work in order to reduce commercialisation of informal audio and video pirate copies. Thus, during 2004, that Direction executed almost 40 operations in different places where pirate products were sold illegally for an amount of US$ 21 million.

However, the task for eliminating the informality in this sector goes on, but it is complicated because the network of production and distribution of this illegal business has high levels of sophistication, so they are able to reach a great mass of consumers. This has motivated that formal Peruvian enterprises use the same ways of distribution in order to spread their “original” products to a lower price so they can attract part of the consumers of piracy.

Finally, it is important to stress on the efforts of Indecopi in fostering some campaigns which have had the objective of catching the consumer’s interest about damage of piracy in authors and the State. Examples of these campaigns are “Antipiracy Crusade” and “The Movie Theater Day”.

Made by Department of Economic Studies of Indecopi
CONTRIBUTION BY ROMANIA
COMPETITION POLICY AND THE INFORMAL ECONOMY

--Romania--

1. Definition of informal economy

1. Most authors trying to measure the informal economy (or underground economy) face the difficulty of how to define it. One commonly used working definition is: “all currently unregistered economic activities which contribute to the officially calculated (or observed) Gross National Product”.

2. These very diverse sectors and kinds of informal economies in Romania can be grouped in four types (R. Neef, 2004):

1) Informal dependent activities. The people and households involved in such activities live in poverty, engage in informal activities - mostly subsistence farming and occasional labour, day work, transport or construction, but also some small handicrafts or street trading - and their main source of income is survival-level.

2) Informal supplementary activities. These activities are far less obvious, but are part of the strategies applied by the population as far back as the time of the “shortage economy”. They are informal supplementary activities, practiced within households that are not poor, in order to complement their formal incomes, or improve their standard of living. The activities in this category are much more numerous than those in the first category. These include farming and the sale of products thereof, qualified trades, professional services and temporary work abroad. Most of these households have at least one formal jobholder, some using for personal gain the resources at their place of employment, such as materials, equipment, working time, infrastructure, or clients. Few of these benefit from stable social transfers, in most cases pensions. They receive supplementary income from agriculture (or land they own), qualified trades or even small businesses.

3) Informal enterprises. Most of the people in this group lack adequate material and financial capital, and are therefore unable to officially start up a business. They are mostly active in labour-intensive industries, such as trade, professional services (computer operation, accounting, tutoring) etc. Most of these are family businesses, and the formal jobholders in the household provide the basic liquidity for the firm. A great deal of energy and time at work is the substitute for little capital. Others, to our knowledge, a minority, have available basic assets and property, excellent qualifications and a network of well-placed relations. They know “who needs to be known” to establish modern farms, transportation companies, micro-construction or specialised production companies. There is no data on these small, informal enterprises (evading taxes and using unregistered workers) to allow for a quantitative or typological estimation. The line between informal enterprises and formal ones engaging in a limited number of informal practices fluctuates and is impossible to approximate. It is more a difference of intensity than one of form.

4) Criminal economic activities. They are active in the most diverse fields and have a variety of forms, (these include theft, drug producing and dealing, and finance criminality). Some are just distributive, tapping resources from the economy. Others manufacture illegal products or use illegal distribution chains. Their profits do not depend on the number of working hours spent or on their own accumulation, but rather on risk-taking, blackmail or violence. Illegality is the core of criminal economic activity, and constitutes its difference from other types of informal economies that may include many illegal elements or manipulations, but which be put aside if other legal resources were substituted.
2. Causes, characteristics and size

3. The informal sector is a critical component of many economies in Eastern Europe, considered by some as the “shock absorber of transition”. The economic, social and political re-engineering which characterises transition to a market economy and western style democracy creates many uncertainties as well as many opportunities; a large part of this process has actually happened outside of official channels through informal relations and activities.

4. In this context, many problems emerge, since it is widely believed that high tax rates and ineffective tax collection by the government are the main causes contributing to the rise of the underground economy. The economists have already established a relationship between tax rates and the amount of tax evasion or the size of the underground economy: the higher the level of taxation, the greater the incentive to participate in underground economic activities and escape taxes. However, corruption is an important factor that can not be neglected. Moral issues, related to the fairness and the asymmetry of the relationship between the individual and the State, and structural flaws in the legislation are also considered as catalysts for economic fraud.

5. General wisdom says that the sectors in which underground activities mainly occur are: repair and maintenance of vehicles and domestic appliances; clothing and footwear production (including repairs); construction; agriculture; transport; wholesale and retail trade; tourism, hotels and restaurants; real estate; education; health; business and personal services.

6. At the macroeconomic level there are several so-called indirect methods used to estimate the size and dynamics of the underground economy, reported in literature as “Monetary Approach”, “Implicit Labor Supply Method”, “National Accountancy”, “Energy Consumption Method”, etc. Unfortunately, many times there are large differences among the estimated shares of informal or underground economy obtained by various methods. For instance, a study published by L. Albu\textsuperscript{1} shows that: “the figures range between about 20% of GDP, obtained on the basis of the energy consumption method (Enste and Schneider, 2000) and more than 45% computed using the monetary approach (French, Balaita, and Ticsa, 1999). Also, the figures (based on the national accounts methodology) reported by the National Institute for Statistics (NIS) increased (mainly due to changes in methodology); from about 5% in 1992, to 18% in 1997 and to 20-21% in 2000-2001. Adding to these figures about 7% of GDP, representing the estimated average level of self-consumption in the case of a rural household, legally non-registered but informal, it results that during the last years the informal economy accounted for 25 - 28% of the national economy”.

7. Many transition economies have experienced a surging business activity in the informal sector. Some of this activity is illegal (criminal), for example arms trafficking. Such activity will not become formal, regardless of improvements in the business climate. Other activities, like mom-and-pop retail trade or small production units operate merely for the subsistence of their owners and do not generate enough revenue to make their inclusion in the tax base meaningful. However, there exists a considerable share of business activity that is semiformal, e.g., the company is registered but most employees are not etc.

8. Unofficial enterprises can be medium or even large enterprises with sophisticated activities. This happens because an enterprise is able to keep activities ‘blended’ i.e. part formal and part informal or unofficial.

\textsuperscript{1}“A Model to Estimate Informal Economy at Regional Level: Theoretical and Empirical Investigation” - Lucian-Liviu Albu, Institute for Economic Forecasting, Romanian Academy, Paper prepared for the International Conference on Regional and Urban Modeling, Free University of Brussels, June 1-2, 2007
9. Businesses in the subsistence end of the informal sector spectrum hold little potential for “graduating” to the next levels. Business failure rates are high because of high localised competition and lack of information or access to other markets. Moreover, many of these enterprises are short-lived until the household finds other sources of income that enables it to recover or surpass its living standards.

10. Unofficial enterprises in the small and medium end of the informal sector whose owners and employees are highly educated and have sophisticated skills hold the greatest potential to ‘breakthrough’ to the formal sector. This sub-sector is where there is a great deal of mixed activity, enterprises that may be formally registered, but some of their activities or employees are not officially reported. Improvements to the business and regulatory environment may provide incentives for these potentially dynamic enterprises to go formal. However, many authors believe that such businesses structure their supply and customer relationships in ways that make it difficult to go “legal” later; also opportunities to modernise are often dismissed and productivity of informal companies stays below half the average of legitimate companies.

3. Level playing field and productivity

11. The expansion of the underground economy relative to GDP has important consequences for public finances. Businesses in the underground economy escape taxation, so that the transfer of scarce resources to the underground economy undermines the tax collection and consequently reduces the supply of essential public goods, such as macroeconomic stability, public order or law enforcement. Furthermore, a vicious cycle may emerge since budgetary concerns generated by low tax collections may generate increased tax rates imposed on formal businesses. In addition to exaggerating the unearned cost advantage of informal ones, higher taxes eat up revenues that formal companies would otherwise invest in R&D.

12. Informality stifles economic growth and productivity in two ways. First, the powerful incentives and dynamics that tie companies to the grey economy keep them subscale and unproductive. Second, the cost advantages of avoiding taxes and regulations help informal companies take market shares from bigger, more productive formal competitors.

13. In many sectors of the economy entire informal value chains have a substantial cost advantage over their formal counterparts. In addition, customers of an informal business expect low prices, and many would go elsewhere if it transformed itself into a formal company and had to raise them.

4. Competition enforcement

14. A sector where the Competition Council was very recently faced with a substantial underground economy is the cereals market and its downstream markets.

15. In 2007, upon receiving signals from the market and the press, the Competition Council opened an ex-officio investigation on the general bakery market regarding potential price agreements between producers. Subsequently, RCC opened a sectoral enquiry on the upstream market, respectively on the market of cereals used for the production of general bakery products. Both actions are still ongoing, although in their final stages of completion.

16. The analysis of both markets revealed a high percentage of underground activity. In the first investigation, even if formal players interviewed accused large portions of the market being affected by informal players, evidence showed that the informal players were small operators, in villages and the peripheral area of small cities. Difficulties in the assessment of the market and market shares of formal players, affected by lack of figures from the informal side, were not detrimental to the case since RCC was investigating a per se infringement. The large number of small informal operators, though, has a large influence on the price of bread.
17. Apparently such operators are part of an informal distribution chain, so cost advantages that create pressures on formal competitors result not only from tax evasion, but also from lower costs in raw materials, storage etc.

18. Data from the sectoral enquiry on the market of cereals used as raw material in the market of the initial investigation confirmed the spillover effect of underground activity in all downstream markets onto the final product market, affecting the behaviour and pricing policy of formal bread producers.

19. Most of the bread producers declared that they are forced to keep their profit margins very low to stay on the market. Oddly enough, the ordinary bread consumer may find an apparent positive aspect of the pressure of the underground economy on the formal one: without the tax evaders, the price of bread would soar.

20. However, for the more trained eye, large bread producers do not seem to be in any threat of exiting the market. Bread is a basic food product and therefore demand for bread is highly inelastic. Moreover, the lack in sophistication of the customers and low level of income per capita of the Romanian general population as opposed to more developed economies may mean that an increase in prices for bread would paradoxically generate an increase in the quantity demanded (the Giffen effect). The size of the informal bread producers makes it impossible to believe a scenario where consumers, especially those from the big cities where most of the bread produced in large factories is distributed, would shift their buying habits so much as to travel large distances to seek for cheaper bread.

21. Baking is not a capital intensive industry. It manufactures generally low-cost goods from product components. It is however true that a low profit margin will keep companies from investing in quality improvements or brand diversification and thus generate cost efficiencies that would make them more competitive on the market.

22. Evaluating the size of the informal economy in the grain market proved to be an almost impossible task, since statistical data available from various institutions was incompatible due to different methods of estimation. The mechanism for granting subsidies for agriculture could have provided also a good approximation of internal production of grain; however, certain subsidy beneficiaries tend to declare fictitious figures for their production, accusing unfavourable weather for low levels of productivity and selling the undeclared grains on the black market. Also, according to information received, large quantities of cereals were imported and exported illegally. Players on the market placed the size of the “black market” at 40%.

23. Financial Guard controls on these markets revealed losses for the State budget of almost 21 million EUR only from bread producers investigated in 2007. 8 out of 10 undertakings investigated were evading taxes. Total figures for tax evasion from all markets using cereals are impossible to estimate.

24. The Competition Council will communicate the findings of the investigation reports to the relevant authorities that have the necessary tools to get these markets back to a certain degree of normality.

5. Advocacy

25. All types of informal activities have something in common: the entrepreneurs who pursue them believe the benefits of informality outweigh their costs. Some activities will always stay informal: illegal activities like drug trafficking is one example; house-cleaning is another example. No improvement in the regulatory environment will change their status. Fortunately, such activities account for a small share of GDP. Many activities that now take place in the informal or semi-formal economy may be legalised if the costs of staying informal would rise and its benefits would fall.
26. Several changes need to take place in order to improve the environment for operating a formal business.

- Reducing barriers to entry on markets.
- Streamlining administrative process.
- Adequate fiscal policy, assisted by efficient tax collection and control instruments/organisms.
- Eradicating corruption.
- Enhancing access to capital.

27. Most of these actions are beyond the attributions and mission of the competition authority, but rather fall under the responsibility of other governmental institutions.

28. Advocating removal of excessive regulations that create high barriers to entry is however a task that a competition authority can and should perform in order to promote and preserve free competition on the markets.

29. A good example on this topic is the taxi services market. Although the case was extensively presented in a previous submission of the Romanian Competition Council for OECD’s Competition Committee Roundtable on taxi services in 2007\(^2\), recent and relevant evolutions justify an additional brief presentation.

30. Until 2002, in Romania taxi services were regulated at local level by each local public authority, by means of decisions of the local councils. At the end of 2002, the Parliament adopted a law regarding taxi and for-hire services; this law established the general rules of functioning for these services, enforced at national level. Local authorities were now empowered both to define the dimension of the market by establishing a maximum number of licenses and to issue regulations regarding minimum and maximum tariffs for taxi services. Moreover, these decisions were to be made upon consulting the respective professional associations.

31. RCC led a sustained advocacy activity, informing the Government, the Parliament and the General Council of Bucharest about the anti-competitive aspects in the law and proposing\(^3\) their elimination. Our position was also presented publicly, in several articles, press releases and interviews in the mass-media, underlying each time the negative effects of the restrictions existing in the taxi law.

32. Discussions took place also with the professional associations in the field and with the legislators for finding less harmful solutions from the competition standpoint. RCC insisted on eliminating minimum tariffs and refraining from consulting the professional associations on tariffs and number of licenses.

33. Regarding the limitation imposed to the number of licenses, it was suggested that the limitation should be eliminated in two years time, in order to give stakeholders the possibility to adapt/ prepare themselves to face up to the competition on a free market, without such entry barriers. If necessary, such limitation might only be maintained in big cities where heavy traffic might justify it; as soon as traffic

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\(^3\) The competition law in Romania allows the competition authority to propose modifications of the normative acts which contain provisions with an anti-competitive effect
issues are addressed, this limitation should be also eliminated. This opinion was upheld by local authorities in small towns that considered limiting the number of licenses not justified.

34. Several draft laws regulating the taxi services that incorporated our comments were submitted to the Commissions of the Parliament and extensively debated. In 2007, the Romanian legislator issued a new law regarding local public transportation, which included taxi and for-hire services. The new law contained several provisions that were supposed and may have been indeed a disincentive for the informal economy in the sector and most certainly contributed to the welfare of the consumers.

35. However the restriction regarding the maximum number of licenses was maintained along with other anticompetitive provisions that are not relevant for this topic.

36. At present a maximum number of four authorisations per 1,000 people are issued. Taxi licenses are assigned for a five years period, with a possibility of renewal.

37. For example, before this restriction was introduced, in Bucharest there were about 7,000 taxi authorisations. Their number increased in 2004 to 8,500 and at present there are 10,000 authorisations. Although remarks were made at the previous debate on this issue that taxi services in Bucharest seem to be quite competitive and the quality of services beneficial for the customers, and with good reason, signals from the market show that the limitation imposed on licenses, aided by other secondary factors not necessary related to regulation, such as corruption, mentality and social issues, led to the proliferation of a quite substantial informal market.

38. According to the testimonials, big taxi companies currently do not have staff to operate their licensed vehicles, due to low salaries and high daily targets imposed. However, they keep their current licenses and would rather keep cars parked in company parking lots than downsizing business to increase productivity. As a result, even if on paper 10,000 taxis operate within city limits, in reality figures are significantly lower. The local council has more than 1500 applications for licenses on the waiting list, and in the meantime most of the applicants are forced to operate illegally.

39. The professional associations on the market right now are divided in two sides: big companies on one side and small or independent operators on the other side, most of them currently without licenses. The first declare themselves quite satisfied with the current state of regulations and are quite eager to participate in consultations on tariffs. The latter accuse the first of closing the market. Even if one might argue that a substantial presence of big operators on the market is not necessarily a bad thing for the quality and safety of services, since obviously big companies have the necessary resources to observe quality and safety regulations, there is always a concern related to prices. An absence of small and independent operators on the market might provide breeding grounds for concerted practices. Moreover, the resulting oligopoly is artificial and not the result of normal competition.

40. Currently, RCC has several ongoing investigations on local taxi markets regarding possible price agreements.

41. Social movements and public protests of taxi drivers occurred repeatedly in recent months: public rallies and demonstrations, hunger strikes, open letters to the regulators and the Government, even a letter to the European Parliament. The Mayor of Bucharest had several meetings with representatives of discontented taxi drivers and agreed to try to increase the limit of maximum licenses. This solution would provide however only temporary relief.
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CONTRIBUTION BY CHINESE TAIPEI
1. **Introduction**

1. According to Article 2 of the Fair Trade Law of Chinese Taipei (hereinafter the “Law”), the Law is applied to a company, a sole proprietorship or partnership, a trade association, and any other person or organisation engaging in transactions through the provision of goods or services. Therefore, almost all kinds of undertakings, regardless of whether they are natural persons, small-sized stores and vendors, different types of companies, or trade associations carrying out formal or informal economic activities will be under the jurisdiction of competition enforcement.

2. However, defining the informal economy and identifying data sources are difficult tasks because of varying degrees of non-compliance. The Directorate General of Budget, Accounting and Statistics (hereinafter the “DGBAS”), a Cabinet-level office, which handles most of the duties of the national statistical reports used as reference for policy-making, has estimated the underground economic activities in 1992 and 1999, respectively. In the past research conducted by the DGBAS, all kinds of informal trading activities have referred to paid informal work. Paid informal work is composed of the following types of economic activities:

   - illegal and unregistered activities, such as smuggling, unlawful lumbering, collecting river stones and sand without government approval;
   - evasion of direct and indirect taxes from earnings, by mainly focusing on the work performed by the professions, such as those comprising lawyers, accountants, physicians, pharmacists, architects and performers;
   - avoidance of taxes and regulations where the focus is on the production and sale of goods and services that are unregistered, or hidden from government regulations, such as goods and services supplied by street vendors, unregistered factories, loan clubs, tutors, nannies, and Japanese Pachinko parlours.

3. Different measures used to assess the ratio of the informal economic activities contributing to GNP give rise to different results. In spite of the lack of current official statistical data, in the 1990s, according to local academic research, the value of informal economic activities accounted for a share of some 20% to 30% of GNP. The ratio was even estimated as being as high as 47% in 1997 due to the hidden trade across the Taiwan Strait. Consequently, the figure of GNP was partly distorted. Some economists alleged that if the informal activities had been included in the national payments system, the value of GNP would have been higher. However, others have argued that considering that informal and formal players compete against each other in every sector in the economy, informality removes the incentive for businesses to improve their productivity, which means that it holds back GNP growth accordingly.

4. From the consumer’s point of view, the supply of goods and services by the informal sector provides added variety, offers more competitive prices and brings convenience. Before the deregulation was implemented, including the opening of direct air and sea routes across the Strait, the opening of banks to China, and the loosening of restrictions on the number of Chinese tourists, Chinese Taipei shipped about 20% and 15% of its exports to China and Hong Kong, respectively, and most of the Hong Kong-bound exports were then transported to China. This illustrates that the cross-Strait economic activities were characterised by gray economic activities due to the strict regulations.
5. The existence of night markets in Chinese Taipei is another example that demonstrates that informality provides variety. A night market clustered with large numbers of street vendors providing assorted snacks, souvenirs and entertainment services is a combination of traditional culture and modern consumption, and has also gradually become a tourist attraction. On the other hand, luxury boutiques, department stores, and supermarkets may be many times as attractive as their informal rivals, and they may also offer higher quality. After all, the market variety provides consumers with opportunities to freely interact with both formal and informal businesses.

2. Examples of Fair Trade Commission Practices

Case I

6. A case currently under discussion, can demonstrate how government regulations that curb the informality affect the provision of services. The Children’s Bureau under the Ministry of Interior (hereinafter the “CBI”) is the competent agency responsible for child welfare services. To achieve its policy goal, the CBI has a vision to establish a community nanny-support system, to reinforce the training of nanny, and to build a professional image with nanny certification so as to upgrade the quality of nurseries.

7. The CBI has planned to implement a subsidisation project to improve professional babysitter practices and promote community nanny-support systems. According to its draft plan, every household sending a child to a nanny with both CBI certification and membership of the community nanny-support system will be able to apply to the local government for a subsidy of NTD3,000 per month (approximately US$100). Furthermore, in order to prevent nannies eligible for subsidies to collude accordingly on increasing pro rata their service charges, the CBI recommended that local governments set a maximum cap for the nanny services to ensure that the system will not be circumvented. Due to concerns that the price-cap recommendation may run against the Law, the CBI sent a letter to solicit the opinions of the Fair Trade Commission of Chinese Taipei (hereinafter the “Commission”).

8. In the past, households could acquire child-care services by hiring experienced unlicensed nannies, college students or day-care centres, or by having free services provided by family members, such as grandparents. Although the number of babysitters with official certification has increased from 7,302 in 1998 to 37,610 since the CBI was established in 1999 and there are 41 community nanny-support systems organised by 23 local governments, nannies from the formal sector can not meet the demands of parents since the average number of children under the age of 6 is more than 300,000. The huge gap between demand and supply make the task of assessing the scale of the informal economy in the nanny service sector too difficult to develop a pro-competition policy.

9. Although the Women’s Rights Council of the CBI insisted that formulating the maximum standard for the service charge was the only way parents could prevent nannies from exploiting the provision of the government cash subsidy for their own advantages and ensure the quality of the child-care services, the Commission advocated that the CBI implement other optional policies to achieve the same policy goals. The Commission tried to persuade the CBI to accept that the best way to ease the upward pressure on the price was to increase the provision of nanny services instead of setting the price cap. The Commission further suggested that the CBI avoid unnecessary or disproportionate restrictions on the provision of nanny services to avoid unexpected price rises due to collusion. This case is still under consultation by different government agencies.
**Case II**

10. The second case is concerned with how the government streamlines taxes and regulations to tackle the problems created by the informal sector. With the island of Taiwan located in the middle of a chain of islands stretching from Japan in the north to the Philippines in the south, and only 160 kilometres off the south eastern coast of the Chinese mainland, the fishery industry is one of the most important primary industries of Chinese Taipei due to its superior geographical location. Owing to the painstaking devotion of researchers as well as the diligence of the fishing entrepreneurs, Chinese Taipei’s fishery industry has rapidly developed and has gained worldwide recognition. In recent years, its overall production has exceeded 1.3 million tons, with a total value of nearly NT$100 billion. Over 130,000 households, or approximately 340,000 people, are engaged in the work of the industry.

11. The Council of Agriculture (hereinafter the “COA”) is the highest fishery policymaking body in Chinese Taipei, under which the Fishery Administration (hereinafter the “FA”), is established to be the highest fishery administrative agency. Fishermen’s associations formed by fishermen operate for such purposes as safeguarding fishermen’s rights and interests, enhancing fishermen’s knowledge and skills, boosting the modernisation of the fishery industry, increasing fishing production, and improving the fishermen’s livelihood. The FA has authorised the state as well as 39 local fishermen’s associations to handle affairs regarding awards, aid and subsidies to encourage the industry.

12. In recognising that fuel costs account for as much as half the earnings from the boats themselves and cannot be passed on, the Chinese Taipei government has continued delivering funding support in relation to the fishing boats’ fuel consumption since 1958. The CPC, which is a state-owned monopoly with overwhelming power in both the wholesale and retail petroleum markets, has offered preferential rates in respect of fishing fuel prices for any type of vessel registered in Chinese Taipei for the purposes of fishery operations. The CPC has submitted the applications for such subsidies to the FA to compensate for the difference between the wholesale price and the preferential price of the fuel.

13. In addition, according to Article 59 of the 1991 amendment to the Fisheries Act and Article 8 of the Value-added and Non-value-added Business Tax Act, fuel for powered equipment used in the fishery industry shall be exempted from commodity tax (approximately NT$3.8 per litter for diesel fuel, and NT$6.5 per litter for gasoline in 2000) and business tax. The 1991 amendment to the Fisheries Act further strengthens the regulation on subsidising fishing fuel consumption in order to maintain the fairness of the market, and such an amendment has required the Cabinet to set the operating standard for fishing fuel purchased at preferential prices. In practice, the FA has been continuously providing a 14% subsidy based on the wholesale price excluding taxes.

14. Since the petrochemical components of the fuel used for the purpose of powering the fishing boats are almost identical to those for diesel, the amount of the exemption together with the government subsidy have been giving fishermen financial inducements to sell the fuel to local gasoline stations so as to earn additional profits to that from fishing income. In particular with the fishing industry having been hard hit with the progressive increases in petroleum prices, the FA has made many efforts to raise the subsidy over the period from 2002 to 2007 in order to help the fishing industry adapt to the high fuel costs.

15. When global oil and commodity prices remained at high levels, domestic trading firms and unregistered oil firms that fully or partially evaded taxes, and product, labour, land and security regulations, took advantage of the special features of the diesel market. As the government has been continuously providing a 14% fishing fuel price subsidy to revitalise a sluggish fishing industry caused by a depletion of fishing resources, the excess fishing fuel, which is estimated to amount to 410,000 kiloliters a year, has been sold as diesel in domestic gasoline stations or informal oil firms for higher profits. These practices have not only directly affected the tax revenues of the government and wasted the government’s
funding support, but they have also significantly affected the competition in the formal sector. The use of inferior gasoline or diesel will damage the engines of vehicles as well as increase the level of air pollution. In addition, as such practices are usually carried out using makeshift facilities such as storage tanks, they have posed a great threat to security and the environment. In order to prevent underground trading from undermining the well-intentioned subsidy to fishermen from the government subsidy, the FA gradually requested that fishermen equip fishing vessels with mileage tracking facilities so as to assess the real fuel consumption amount and prevent non-users from avoiding fuel taxes.

16. Unlike the fishery administrative agency, the Commission has been more concerned with the inappropriate government regulations in the market. The petroleum and its related upstream and downstream product industries were highly regulated by the Ministry of Economic Affairs (“MOEA”) until the ban on privately-owned gasoline stations was lifted in 1987 as the very first stage of deregulation. Subsequently, in June 1996 the market was opened up to applications for the establishment of new petroleum refineries and at that time the privately-owned petroleum refining company Formosa Petrochemical Corporation (“FPCC”) was authorised to enter the market. After the promulgation of the Petroleum Management Law in October 2001, by removing the restrictions on the establishment of a petroleum refinery with a minimum capacity, the petroleum gasoline, diesel, fuel and related products market was free to be entered by any potential competitors.

17. However, the FPCC faced challenges as it sought to take part in the fishing fuel market. The FPCC in its report to the Commission pointed out that the FA had adopted a subsidy application procedure that differed from those used for fuel purchases from the CPC in 2003. The CPC filed the subsidy application form directly with the FA for its approval, while the FPCC was required to submit subsidy applications to the local government for purposes of government auditing so as to send the case to the FA for a final decision.

18. In the eyes of fishermen, buying fishing fuel from CPC-owned, CPC-franchised or private-owned petrol stations, or else fishermen’s associations with fuel storage facilities are all good substitutes for each other. However, the said subsidy application procedure is likely to have made retailers reluctant to source their fuel from the FPCC since the period for collecting the preferential price compensation due to the government subsidy has been constantly delayed by the lengthy review process.

19. The FA asserted that according to Article 17(1) of the Regulations Governing the Allocation of Bunker Fuels: “Fishermen’s associations acting as bunker fuel purchasing agents shall submit a detailed table of the previous month’s bunker fuel purchases and deliveries, and the circumstances of those transactions, to the relevant county (city) or special municipality and central government competent authority for fisheries by the fifth day of the following month.” Consequently, the FA has been able to require local governments to review the subsidy applications prior to its approval and the Fair Trade Law has not been applicable in such cases. Moreover, given that the CPC is a state enterprise supervised by the Commission of National Corporations under the MOEA and its budget allocations are subject to government budget auditing regulations, and the CPC has also been the sole fishing fuel wholesaler and retailer in the ports, to save on administrative costs, the FA ignored the review procedures of the local governments in regard to CPC subsidy applications in the past.

20. However, given the discrepancy in procedures for applying for fishing fuel subsidies, new entrants, who cannot offer as fair, or better, trading terms to compete with or substitute for the terms of the incumbent, will hardly survive. The Commission advocated that the FA take its suggestions into consideration in carrying out its fishing fuel subsidy processing operations in the interests of promoting fair competition in the domestic fishing fuel market so as to allow the new suppliers to enter the market when the domestic petroleum market was fully liberalised at the end of 2001.
21. On the one hand, the Commission has made efforts to streamline regulations to promote competition in the market with the informal sector; on the other hand, it has remained neutral on the issue of criminality in relation to informal activities. The following case will point out those criminal activities where the goods and services themselves are illegal.

22. When the volume of imported supply and domestic production as well as the domestic consumption and inventory according to the disclosure of Customs’ data are compared, it is found that an annual total of approximately 400,000 kiloliters of various imported oil products were blended into gasoline or diesel to be sold in 2003.

23. As it is difficult to detect and thereby root out the underground transactions of such inferior gasoline and diesel fuel, the police with insufficient legal tools can only passively inspect suspected inferior supplies. This has resulted in illegal transactions of unqualified gasoline and related products facing little curtailment.

24. Although both the CPC and the FPCC have complained that the weak governance structures contributing to such an informal economy will distort market order, the quality of the products sold through legal channels is not necessarily always good. In 2007, a worker at a gas station sourcing gasoline and diesel from the CPC admitted that she took orders from her boss to mix the gasoline with methyl alcohol. The workers’ confession prompted prosecutors and investigators to hunt for the owner of the gas station. Consequently, five executives of the state-run CPC, including its president and the CEO, were penalised with demerits for lax supervision of the operations of the gas station that had been selling oil products supplied by the CPC for many years. The MOEA announced the punishments for officials at its Energy Bureau, which is responsible for national energy policies. Unconfirmed reports show that the gas station owner purchased a shipment of 50,000 litters of methyl alcohol and mixed the chemical product with 500,000 litters of unleaded gasoline. This shipment alone could have filled up oil tanks and affected at least 30,000 vehicles. However, the Commission has seldom gotten involved in these issues. It seems clear that the Commission considered that the informal work covers only activities where the means do not comply with regulations but the end goods and services are legitimate.

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CONTRIBUTION DE LA TUNISIE
LA POLITIQUE DE LA CONCURRENCE ET L’ÉCONOMIE INFORMELLE

--Tunisie--

1. Définition de l’économie informelle

Il y a plusieurs définitions controversées de l’économie informelle plusieurs éléments peuvent être pris en compte: la taille de l’entreprise, le caractère loyal ou déloyal, la légalité de l’activité. Mais on peut définir l’économie informelle comme étant « toutes les activités exercées en dehors des circuits et formes habituellement admis selon les normes en vigueur dans chaque pays ».

2. Raisons, caractéristiques et taille ?

Les facteurs de développement de l’économie informelle peuvent être regroupés en plusieurs catégories:

- **Niveau de développement de l’économie**: Le poids du secteur informel dépend beaucoup du degré de développement de l’économie, plus une économie est développé plus le risque de développement du secteur informel est réduit.

- **La politique économique et sociale du pays** : la déperdition scolaire ainsi que la politique de l’emploi favorisent l’arrivée sur le marché de l’emploi de jeunes non qualifiés qui seront attirés par le marché informel. Ainsi que l’absence de territoires aménagés (zones industrielles, pépinière …) contribue au développement de ce fléau.

- **Obstacles à l’accès de l’économie formelle** qui se manifeste par la difficulté des conditions d’exercice et d’accès aux crédits ainsi que des coûts d’investissement élevés ce qui rend l’économie informelle moins coûteuse et plus attrayante.

*Quels sont les produits et les services généralement produits par le secteur informel :

3. Le champ d’intervention du secteur informel est très large touchant l’industrie (bâtiment, textile, mécanique, électrique…), le commerce, l’agriculture, l’artisanat et les services.

*Quelle est la taille du secteur :

4. Le secteur informel en Tunisie a pris de l’importance à partir des années 80 avec 365 milles entreprises opérant dans le secteur informel. Il contribue à :

- 15 à 20% du produit intérieur brut,
- 20% du commerce
- une valeur ajoutée estimée en 1997 à 5.541 millions de dinars (à l’exclusion du secteur agricole).

5. Il est signaler que les statistiques disponibles sur l’économie informelle sont estimatives, il est très difficile d’avoir des statistiques exactes sur le secteur mais les chiffres montrent que sa taille dans l’économie tunisienne est plus ou moins stable.
**Est-ce que l’économie informelle touche la concurrence dans le secteur formel ?**

6. Le secteur informel est généralement constitué de petites entités avec un capital réduit utilisant des méthodes de production primitive et un personnel non qualifié. Néanmoins, ces entreprises peuvent offrir des prix bas satisfaisant les besoins du consommateur. Pouvant ainsi concurrencer l’économie formelle dans certains secteurs (cosmétique et articles d’hygiène…) ce qui est contesté par le milieu professionnel qui demande l’intervention de l’administration pour lutter contre ce phénomène.

7. L’économie informelle peut aussi exercer une pression concurrentielle sur le secteur structuré stimulant les entreprises à offrir aux consommateurs des produits à des prix abordables.

**Est-ce que l’économie formelle et informelle collabore ?**


**4. Application de la loi relative à la concurrence :**

9. Le champ d’application de la loi sur la concurrence couvre tous les secteurs et toutes les entreprises opérant dans l’économie informelle ou formelle, l’application du droit de la concurrence n’est pas liée à des conditions de légalité ou de loyauté. Les autorités sont tenues de juger le comportement quelque soit le statut de l’opérateur. Mais dans la pratique les autorités de la concurrence trouvent des difficultés pour identifier les opérateurs, leur part de marché, leur chiffre d’affaires … ou les prouver ou de mesurer l’effet de cette pratique sur le marché.

**5. Encadrement du secteur informel :**

10. Bien que l’objectif des autorités de la concurrence n’est pas de faire disparaître le commerce informel mais il s’agit de le contourner, à cet effet plusieurs mesures ont été prises :

- Renforcement du dispositif juridique et économique :
  - suppression des autorisations et leurs remplacements par des cahiers des charges pour faciliter l’intégration du secteur informel
  - facilitation de l’octroi des prêts destinés à l’exercice de l’activité économique (Banque de Solidarité),
  - promulgation de plusieurs lois consolidant le principe de la liberté de l’exercice des activités économiques et l’intégration dans le secteur formel.

- Mécanismes réglementaires de contrôle technique à l’importation de produits et marchandises,

- Programme de mise à niveau des circuits de distribution.

- Renforcement des actions du contrôle économique :
  - lutte contre la contrefaçon,
  - lutte contre l’expansion géographique et temporelle des marchés hebdomadaires,
interdiction de l’implantation commerciale anarchique.

- Amélioration des conditions de l’exercice du commerce :
  - Création d’espaces spécialisés pour les commerçants opérant dans le secteur informel,
  - Organisation des marchés hebdomadaires et fixation des règles et conditions de création et de fonctionnement de ces marchés,
  - Aider les intervenants dans les circuits informels à s’intégrer dans le secteur organisé (campagne de sensibilisation…),
  - Facilitation d’installation dans les espaces aménagés
  - Mise en place d’un plan de modernisation des marchés municipaux (problèmes posés par le commerce anarchique sur la voie publique),
  - Instauration de commissions locales mixtes (commerce, intérieur) chargées du suivi de l’avancement des travaux dans ce domaine.
CONTRIBUTION BY TURKEY
INFORMAL ECONOMY AND COMPETITION POLICY:
CASES FROM THE TURKISH COMPETITION AUTHORITY

--Turkey--

1. Informal Economy: Conceptual Framework

1. The informal economy\(^1\) may be defined as economic transactions and activities which are hidden from public authorities for several reasons, such as to avoid the payment of taxes and social security contributions. Unreported activities are a prevalent characteristic of economic life, and assume substantial proportions even in the developed countries\(^2\).

2. The growth of the informal economy is caused by many different factors. The most important ones are the rise of the burden of taxes and social security contributions; increased regulation in the official economy, especially of labour markets; forced reduction of weekly working time; earlier retirement; unemployment\(^3\).

3. There are several methods of estimating the size of the shadow economy. They can be classified as direct and indirect approaches. Indirect approaches include “GNP Approach”, “Tax Analysis Approach”, “Employment” and “Monetarian Approach”\(^4\).

2. Informal Economy and Competition Policy in Turkey

4. According to a study which calculates the level of informality in the economy in Turkey between the years 1971 and 2000, size of informal economy fluctuates in these years but from the 90’s, it has started to grow\(^5\). In 2007, the level of shadow economy was predicted as 30 percent\(^6\).

5. The causes of the informal economy in Turkey are several, such as financial, economic, political, social and legal. Within this framework, the economic system and structural properties have important role in shaping informal economy. Especially, the informal sector is most widespread in sectors in which small enterprises are active and which are labour intensive. Beside this, high inflation, economy politics, instability, crises and underdeveloped economies can be seen as the factors that affect the informal economy. High tax rates, the high cost of registered activities and over regulation are other elements which encourage shadow economy\(^7\).

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\(^1\) Informal economy can be discussed using various concepts, such as parallel economy, shadow economy, ghost economy, hidden economy or underground economy. In this paper, the term of “informal economy” will be mostly used.


Informal economy exactly affects the market conditions. The official undertakings obey the rules and regulations while the underground producers do not. So the cost structures of these two groups of undertakings differ from each other. Informal undertakings have lower costs, because that they pay less for labour and input as a result of avoiding payroll taxes. Also, by disregarding safety and health standards underground producers gain a cost advantage. On the contrary, official firms are put at a competitive disadvantage, so that they have to choose between operating as informals or exit from the market. As a result of this problem, official firms may try to solve informality problem with anticompetitive conduct. For instance, they can be organised in the associations in order to avoid informality in the market by using anticompetitive measures. However, it is not the real and permanent solution for the market to use price-fixing agreements for fighting underground sector. In general, there has been a governmental body to prevent informality in the sector and make the market structure more competitive.

Another aspect of the informal economy is its importance in the calculation of market shares in the market. As it is mentioned in the definition, the transactions and activities of undertakings in the informal economy are not recorded. So it is hard to calculate the real values of the market size and each firm’s share in the market. For example, if the level of informality in the market is 50 percent and the leader firm has a market share of 60 percent in records, then the real market share for the firm is 30 percent. This huge difference affects the competition law assessments, especially in merger control and abuse of dominant position cases. Because market share is essential in these two types of analyses and real market share is closely related with the level of informality in the market, informal economy is crucial in competition law enforcement. Many firms defend themselves claiming that they have relatively lower market shares due to existence of informal economy. For instance, they usually argue that they are not in a dominant position in the market because of the underground economy, if they are investigated for abuse of a dominant position. Additionally, merging firms also use informal economy tools for lowering their market shares in order to get permission from antitrust authorities.

Informal Sector in the Decisions of Turkish Competition Authority (TCA)

There are many cases that TCA faced the informal sector. Relevant cases are cited below where informal sector was discussed.

3.1. Waste Accumulator Case

In the Competition Board decision dated 20.5.2008 and numbered 08-34/456-161, it has been detected that at the stage of the collection of waste accumulators, some accumulator-producing and waste accumulator-collecting firms were engaged in competition-limiting behaviour. In the pleas of the undertakings, which took place in the decision in question;

the claims that

“...Even if it is thought for a moment that competition rules are broken, those injured by it are a few number of scrap dealers working in extremely unsound conditions in an informal way, or small firms or personal enterprises working with those scrap dealers, it is not possible to agree with speaking that here the rights of people working in an informal way have been infringed.”

took place. However, the statements that

“Primarily it should be emphasised that the purpose of the Act No. 4054 is to ensure the “protection of competition”. Therefore, it is unnecessary to explain that in order for the Competition Board to make a detection that there is an infringement of competition in a market and to be able to establish a decision, a requirement such that large firms working in that market are injured does not exist. Moreover, consequences that decisions and acts detected to be an
infringement give rise to in terms of many actors in the sector have been put forward above in detail.”

were included in the assessment of this plea, and it was put forward that competing undertakings’ concluding agreements between themselves with a view to pushing out of the market those who commit informal activity did not rule out an infringement of competition. Furthermore, that competition-limiting agreements concluded can exceed their purpose in respect of their effect also takes place among the detections made. Because, it is understood that not only those firms working informally but also the other firms can be affected by an anti-competitive agreement. But, the decision in question does not render legal the activities of those working informally. All detections and assessments have been made in terms of “competition law”. As a matter of fact, whilst assessing the pleas made by the undertakings that

“Licensed or unlicensed scrap dealers collected waste accumulators in an informal way, they were engaged in free-riding, they, by means of not filling the quotas of themselves and the other members of AKÜDER, caused them to be considered guilty vis-à-vis the Ministry of Environment and Forestry.”;

the statements that

“the addressee of the plea that scrap dealers working unlicensed collected waste accumulators in an informal way, they were engaged in free-riding, consequently they, by means of not filling the quotas of themselves and the other members of AKÜDER, caused them to be considered guilty vis-à-vis the Ministry of Environment and Forestry is not the Competition Board certainly. Public bodies to supervise and administratively penalise the sector in this regard are the Ministry of Finance and the Ministry of Environment and Forestry.”

were included, and emphasis was put on the fact that the other assessments outside competition law were required to be done by the relevant public agencies. In the result part of the decision given by the Board, the plea of the “prevention of informality” has not been assessed as a mitigating factor when establishing penalty about the undertakings concerned after having reached the conclusion that they infringed competition. In other words, in the decision in question, the “prevention of informality” has not been evaluated both at the stage of detecting infringement and when assessing penalty.

3.2. Denizli Precious Metal Dealers and Jewellers Chamber Case

10. In another Competition Board decision dated 19.9.2007 and numbered 07-73/892-336, it has been detected that Denizli Precious Metal Dealers and Jewellers Chamber infringed article 4 of the Act on the Protection of Competition No. 4054 by means of determining the selling and purchase price of gold outside the market. In the investigation referred to, the plea that

“……

• there was no commercial logic for sales below the cost,
• informality would be inevitable,
• it would give rise to products with a low degree of fineness and weight in gram, or to fake products,
• a consumer who preferred this product due to its cheapness would suffer, and
• this situation would contradict with the purpose of protecting the consumer, which was mentioned in the reasoning for the Act No. 4054.”
has been made by the association of undertakings. In the assessment of this plea;

the statements that

“In its plea, the Chamber referred to article 11 of the Act No. 5362 and mentioned that it was commissioned for controlling the quality of goods and whether they are produced according to the standard. Primarily it should be mentioned that an assessment as to the quality control of the Chamber has not been made. There is no relationship between controlling the quality of goods, and price determination and controlling whether the price list is complied with. The control of the quality of goods should not be through price determination, but in the manner of having their degree of fineness controlled in houses for degree of fineness by means of getting specimens from jewellers. Furthermore, it is required that the provision of article 11 be assessed together with article 62 of the same Act. In article 62, it has been mentioned that price tariffs show maximum limits. Control to be made by chambers should be whether tradesmen and craftsmen sell above the price tariffs determined. But in the existing incident, sales made by a low price create discomfort and they are tried to be prevented.”

were included, and it was expressly mentioned that combating informality was not regarded in detecting an infringement of competition. Because, it was tried to be emphasised that controlling whether standards determined within the market are complied with was possible for behaviour other than those restricting competition and that a competitive market structure did not lead to informality.

3.3. Ceramic Coating Case

11. In the Competition Board decision dated 24.2.2004 and numbered 04-16/123-26 given as a result of an investigation conducted against undertakings operating in the markets for ceramic coating materials and/or ceramic health appliances, there are also statements as to informality. Among the evidence obtained from the undertakings in the process of investigation, statements that

“expressed that…

• ceramic health appliances was a sector in the world where there was excess capacity,
• crises in the Far East and Russia created narrowing of demand,
• the European Union countries were saturated markets,
• in Turkey, investments continued despite these conditions,
• since export prices were low and dates of maturity were very high in internal markets, net prices amounted to export prices,
• increased capacities constantly pulled prices down due to narrowing of market,
• intense combat was required to be continued with those organisations which created unfair competition by working informally in order to be able to cope with these conditions,
• investment decisions were required to be taken by behaving with further common sense.”

“closed the meeting by expressing that…

• there was a significant segment in the sector which grew by exploiting informal economy,
• this put in a difficult situation those organisations which survived in conformity to laws and according to the rules of economy,
therefore, combating unfair competition was the most important subject of the Association,
methods to protect members but to prevent unfair competition could be determined by ensuring the required reconciliation,
a research that would put forward the consumption in Turkey overall and capacities of small producers would be very beneficial.”

took place. However, convening, in the name of combating informality, of undertakings which committed competition-restricting acts has not been found sufficient at the stage of decision in detecting infringement or assessing penalty. Because, as is also expressed in the previous decisions, in combating informality, tolerating competition-infringing behaviour or exempting such acts from the practices of competition law is not in question. Just as there exist other public agencies that combat informality, it is possible to tell that the market would also push informal firms out of the market within the dynamics of itself.

3.4. **TESK Case**

12. Likewise, in the Competition Board decision numbered 7.1.2005 and dated 05-02/18-9, the investigation conducted in respect of the bread and pita market in Gaziantep has been concluded. In the decision in question, TESK which fixed a base price as to breads and pitas has made a plea that

> “the demand in question has been examined by the Executive Board of the Confederation, and it is understood that offering for sale below cost those goods and services produced by our tradesmen and craftsmen arises out of reasons such as working and having work informally, and forming goods and services that are of low quality and that do not conform to conditions of health. It has been held to be appropriate that in price tariffs as to bread, prepared by our Chambers and approved by our Associations, the cost (base) price of bread as well as its maximum price be fixed and this price be also included in price tariffs since it would not only prevent suffering of the tradesmen and craftsmen concerned but also protect them from unfair competition. Therefore, provided that it is only limited to bread tariffs, also fixing the cost (base) price of bread besides the maximum selling price of bread and this fixed price’s taking place in bread price tariffs have been found to be appropriate by our Confederation.”

As is seen, the confederation made up by tradesmen and craftsmen has detected a base price in the name of preventing informality in markets. It has been thought that thus it would be revealed that bakeries selling below the base price would produce and sell illegally or in a manner not conforming to standards. However, the plea in question has been replied by the statements that

> “it is not possible to agree with the thought that the declaration of cost-base price is at least beneficial for drawing the attention of consumers, as TESK argues, even if it shall be calculated by taking into consideration the fulfilment of all legal obligations. It is defended in theory that, differently from the ceiling price, base price practices are far from ensuring a benefit in economic terms, such practices merely serve the aim of preventing predatory price war and of undertakings’ gaining from it. Also indeed, particularly hypermarkets’ selling at quite low prices the bread they produce at bakeries within them for purposes of drawing consumers to the point has become a typical quality of the market. Also in the letter of the Federation, dated 10.4.2002, emphasis has been put on this issue exactly. However, from both the Circular No. 29 and its correspondences with the Associations, it is understood that TESK is aware that cost-base price fixing cannot be applied to undertakings having the nature of merchant. Moreover, low-price sales of large stores do not remain limited to only bread and similar products, they create effect on markets of the other consumption goods as well to the degree of the ending of small-scale
producers’ activities. However, to what extent the determination of cost-base price would be an efficient solution is also controversial against the reality that capacities, costs and profit-related expectations of undertakings would present difference.

Relieving deficiencies in a market via determining a base price expressly sets contrariness to law in the context of article 4 of the Act No. 4054. Therefore, the opinion reached was that TESK infringed article 4 of the Act through its decisions directed at fixing and declaring the base price as well together with the ceiling price in bread price tariffs.”

In other words, emphasis was put on the fact that the determination of a base price is not necessary in preventing informality in a market, and benefits that may be obtained by a consumer are prevented in this manner. On the other hand, in assessing penalty, the purpose of the association of undertakings to prevent informality has been considered as a mitigating factor as it would be understood from the statements that

“Also in the assessment of the fine to be imposed, market-related conditions explained above and associations of undertakings’ acting with a view to correcting these conditions, and...

...are required to be accepted as mitigating factors.”

3.5. Karbogaz Case

13. Likewise, in the Competition Board decision dated 23.08.2002 and numbered 02-49/634-257, it has been mentioned that Karboğaz Inc. which was identified to be in dominant position in the relevant product market detected as the “market for liquid carbon dioxide” included in its plea the statements that

“It is asserted that the market share of Karboğaz Inc. is below the detected rates and is around 50 %. And particularly with the citation that informal economy is an important problem in our country, it is defended that this difference stems from the fact that sales of competing companies, which are realised without invoice are not reflected in the actual figures and therefore, the market share of competitors appears to be at lower levels than it is. It is mentioned that within this framework, the market position of Karboğaz Inc. appears stronger than it is, and it is implied that Karboğaz Inc. is not in dominant position in the market for liquid carbon dioxide which is the relevant product market.”

When assessing this plea, the statements that

“When making an assessment as to the fact that Karboğaz Inc. is in dominant position, there was not a limitation merely to the market share, the other factors outside the market share have also been considered. On the other hand, not only today’s but also 1996 and later-periods market share of Karboğaz Inc. have also been regarded. In determining the latest 5-year market share and the market position of Karboğaz Inc. within this framework, total sale figures have been asked from all companies (including Karboğaz Inc.) operating in the market, and also import figures obtained from the Undersecretariat of Foreign Trade have been regarded. Furthermore, sale figures based on customers have been asked from all producing undertakings (Güney Natural Gas Inc., Barit Inc. and Habaş Inc.) including Karboğaz Inc. These sale figures obtained from the companies in question are also based on invoices charged by the companies.” have been used.

As is seen, it is stressed that only the market share was not regarded when identifying dominant position. However, it is understood that the figures employed in the identification of market share are based on invoices. Because, it is not possible to use sales without invoice in the calculation of market
share. For this reason, besides the fact that in markets where there is much informality, reaching actual market share information gets difficult, values to be used in calculation are required to exist within entries. However much it presents importance in identifying “dominant position” which is an important issue in respect of competition law, informality cannot be used in calculations of market share and market power since it is not possible to put forward its level definitely.

4. Conclusions and Recommendations

14. In summary, as it would be understood from the decisions included above, informality can be encountered in various ways in competition law practices. In general, when explaining a competition-restricting behaviour, it is likely that the “purpose of preventing informality” be used. Particularly, associations of undertakings’ committing behaviour such as price fixing in the name of having a specific standard established and combating informality in their relevant market becomes the subject of investigations in our country. In these examinations, the “purpose of preventing informality” is not considered as a valid plea, it is likely for it to be deemed a mitigating factor in some files in terms of aim. Also, when identifying dominant position, it is likely that there are pleas as to the calculation of the market share of informal production. However, the inability to calculate informality due to its nature, and the utilisation of invoices that are “registered” in identifying market share do not justify the plea of “informality” of those undertakings which are identified to be in “dominant position”.
CONTRIBUTION BY UKRAINE
COMPETITIVE POLICY AND INFORMAL ECONOMY

--Ukraine--

1. Definition of the informal economy

1. In Ukraine, the informal economy or, as it is usually called, “shadow economy,” has been quite a severe problem since the second half of the 1990s to the beginning of 2000s.

2. At the same time, the informal economy in Ukrainian research works and governmental documents is understood as the economic activity, i.e. production and sale of goods performed outside the mechanisms of legal regulation and official monitoring. First of all, it consists in evasion of taxes and of going through the established licensing procedures for business start-up, as well as evasion of quality and product safety control, non-compliance with environmental requirements and the requirements concerning working conditions etc.

3. For the most part, informal economy exists in two major forms: functioning of non-legalised agents and part of the activity of legalised economic agents, which is performed outside the formal monitoring mechanisms and legal regulation.

2. Causes, characteristics, and extent

4. The emergence of fairly significant sector of informal (shadow) economy in Ukraine in the mid-1990s was caused, in our view, by two main groups of reasons.

5. Firstly, in the conditions of market transformation, a significant number of independent economic agents emerged, which for some time existed without completing the relevant legalisation procedures, because as a result of poor development of government regulation of market and lack of business experience, the market did not feel any benefits from such legalisation or any loss from its absence. Effects of the above-mentioned reasons were temporary and almost stopped in the second half of the 1990s.

6. Secondly, emergence and development of the informal (underground) economy is a reaction to excessive tax and regulatory pressure on the part of the state. For example, according to experts, in early 2000s, the share of net taxes in the legal sector amounted to 20.1 per cent of GDP, the level of budget and extra-budgetary funds revenue amounted to 44 per cent of the official GDP. However, with account of the informal sector, net taxes declined to 14.4 per cent, that is, became closer to that figure in the OECD countries, and the level of the budget and extra-budgetary funds revenue decreased to 31.4 percent of the aggregate GDP. [Крючкова І.В. Структурні чинники розвитку економіки України., Київ, 2004. стор 265].

7. Of the respondents surveyed in 2003 by the International Financial Corporation, 70 per cent characterised the administrative procedures necessary for obtaining permission for business start-up as difficult and very difficult, mentioning that to obtain such permissions, one must spend an average of 33 days and the equivalent of 115 euro (moreover, the third of those surveyed had to spend three years or more to get such permissions), 72 percent of those surveyed described the certification procedures as difficult and very difficult, 54 per cent described the registration procedures as such. [Бізнес-середовище в Україні 2005. Міжнародна фінансова корпорація. 2005 Стор.6].

8. According to the official data, the informal (shadow) economy reached its maximum size in 1997, when it amounted to 43.5 per cent of the legal economy, and decreased to 35 per cent in 2003 [Послання Президента України до Верховної Ради України. Про внутрішнє і зовнішнє становище
України у 2003 році. Київ, 2004 Стр 7, 143]. According to expert estimations, in 2001, the ratio of total shadow output of products and services to the official output was no less than 30 per cent, the gross value added was no less than 57 per cent of the legal value added [Крючкова І.В. Структурні чинники розвитку економіки України, Київ, 2004, стр 265]. Official or expert data on estimates of the size of the informal sector of the Ukrainian economy within the period of 2004–2008 is unknown, but certain figures allow the assumption that there is a tendency to its reduction. For example, the number of industrial enterprises in Ukraine in 2003-2007 declined by 6 percent, while the financial result of industry increased (with account of inflation) by 2.89 times. Since substantial technology changes during that time did not take place, the above-mentioned increase occurred largely as a result of the legalisation of activities that previously had been carried out in the informal sector.

9. Functioning of informal (shadow) economic agents is primarily inherent to products and services markets where there are individual entrepreneurs or small number of partnerships, the activity of which is difficult to control for the government. Such markets are, in particular, retail trade, consumer services, certain kinds of agricultural production that do not require any special cultivation and processing technologies, certain categories of transport, some types of construction work, particularly civil construction, and the like. The informal (shadow) activity of legalised economic agents covers much broader range of economic activities.

10. According to the International Financial Corporation, in 2004, less than 20 per cent of the 3 thousand surveyed chief executives of companies in different economy branches confirmed that they did not hide their profit from tax authorities [Бізнес-середовище в Україні. 2005. Стр 29].

3. Level of markets and productivity

11. In the areas with a large number of informal economic agents, they were significant competitors of the legalised economic agents. However, conditions of competition in such areas have certain characteristics compared to the fully legalised sector. On the one hand, informal economic agents and economic agents who sell their products in the informal conditions do not incur certain expenses that their competitors incur in the legal sector. Although they also have specific costs associated with maintaining their informal status. However, these costs are lower compared to the cost of legalisation and taxation; otherwise the relevant economic agents would leave the informal sector. Consequently, in terms of the transaction costs, the economic agents of the informal sector have an advantage over competitors from the legal sector. At the same time, the condition of the informal sector functioning is information opacity (informal economic agents, informal economic activities seeking to "hide" from government control). As a result, competitors from formal and informal sectors are asymmetric in terms of information for the consumer, and this asymmetry creates advantages for the legal sector.

12. In addition, the specific conditions of the informal sector functioning, usually do not allow economic agents to use technological advantages and economies of scale.

13. Ultimately, as the government reduces tax and regulatory pressure, the advantages of legal sector become more substantial, thus reducing the informal sector.

14. In the practice of the Antimonopoly Committee of Ukraine, there is no data that would clearly indicate that the informal sectors generated any significant barriers for legal companies, including foreign ones, to enter commodity markets.

15. However, in conditions of the transformational crisis of 1994-1999, the existence of the informal sector contributed to satisfaction of consumer demand, especially of the disadvantaged groups, which had little opportunity to purchase goods from economic agents of the legal sector.
4. Application of the competition law

16. Direct application of the laws on protection of economic competition on the relations that arise in the informal economy is not possible. Business processes that occur in the informal economy could become the subject of regulation of competition law only if legalised. For example, if during an investigation of unfair competition, facts of misuse of someone else's business reputation by an informal economic agent are revealed, this agent may be held liable only if legalised.

17. Similarly, for example, a statement of certain business entities that they are experiencing significant competition from the informal economic agents could have legal consequences only if the existence of these economic agents is proven using the formal legal mechanisms of monitoring and government control. But in this case, the relevant economic agents no longer belong to the informal sector. If there is no evidence, no allegations of existence of competitors in the informal sector can be taken into consideration. At the same time, since the existence of informal competition can only increase the market size and reduce the actual market shares of separate legal entities, non-consideration of such competitors may not lead to a lack of competition or insufficient resistance to the abuse of market power.

5. Facilitation of legalisation of the informal sector

18. The legalisation of the informal sector can be done in two ways: restrictive and encouraging. Restrictive method consists in creating so much risk for the informal economic agents (in case of their identification) that these risks would prevail over the benefits they have operating outside the formal monitoring mechanism and government regulation. Restrictive activities include the removal of legal business methods (such as barter payments) that reduce the transparency of economic processes and create conditions to avoid formal monitoring and regulation. The promotional method lies in reducing regulatory and tax pressure on the economic agents that eliminates the inducement to leave the sphere of official monitoring and government regulation.

19. The most effective method is a combination of both ways, with an emphasis on the latter. For example, in Ukraine in 2004-2005, a number of measures were taken to mitigate regulatory pressure on business entities. Their consequence was, in particular, the increase during 2004-2007 of the number of registered small businesses up to 40.6 thousand or 14 per cent. A large part of them are the economic agents that previously operated in the informal sector and legalised themselves.

20. Participation in the activities of the restrictive nature, aimed at legalizing informal agents, is generally not inherent to the competition departments.

21. With regard to promotional activities that are aimed at legalizing the informal sector, competition authorities may take part in them, if they are, in particular, authorised in relation to the actions of state bodies that lead to increase of costs of economic agents related to the legalisation and official procedures for monitoring and regulation and hence stimulate activities in the informal sector. In Ukraine such problem exists, in particular, in the field of paid services of public authorities relating to the implementation of state quality control standards, the examination required for business start-up, etc. The relevant services are provided by public authorities for payment to those who need them, that is, sold as a commodity. But because such services are provided at the sole basis, the markets which they form are for the most part monopolistic. In 2007, the Antimonopoly Committee of Ukraine identified more than 960 monopolised markets of paid services of public authorities.

22. Planned total volume of paid services of public authorities in 2008 exceeded the amount of revenue from excise duty of goods produced in Ukraine. It should be noted that in the above-mentioned markets there is an acute problem of monopoly abuse, in particular, the high prices, discriminatory prices,
imposition of terms and conditions of contracts that are not related to the subjects of these contracts. Only during 2006-2007, the Antimonopoly Committee of Ukraine discovered more than 1500 such violations in the markets of paid services of public authorities. Their termination in some way helped to mitigate regulatory and administrative pressure on economic agents.

23. Another area of activity of a competition agency that promotes legalisation of the informal sector is termination of actions of state authorities that have anticompetitive effects and, at the same time, lead to increased regulatory pressures on businesses. It is a particular question of establishment of unlawful prohibitions or obstacles to the entrepreneurship, or prohibitions not provided by law, and restrictions on independence of companies (such actions may be, for example, in the introduction of additional permitting procedures not provided by law, or in an unauthorised shortening of validity of the relevant permits). Only during 2006-2007, the Antimonopoly Committee of Ukraine terminated more than 260 such acts of state bodies, which also, in a certain way, helped to mitigate the regulatory burden on entrepreneurship.
CONTRIBUTION BY THE UNITED STATES
COMPETITION POLICY AND THE INFORMAL ECONOMY

--United States--

1. The influence of the informal economy is not as prevalent in the United States as it is in some economies. While there are many reasons for this, one of the most significant is that the regulatory cost of doing business in most markets in the United States is sufficiently low that entrepreneurs do not feel a need to retreat to the informal economy in order to avoid those costs. The informal economy thus has a minimal impact on the antitrust agencies’ direct enforcement responsibilities. The need to ensure that the regulatory cost of doing business remains at a level that encourages firms to remain within the formal economy suggests a critical role for competition advocacy to oppose overly burdensome regulations.

1. The Informal Economy and Enforcement

2. The United States antitrust agencies, the Department of Justice and the Federal Trade Commission, do not directly attempt to address the causes and effects of the informal economy. For example, the failure to pay taxes is addressed by the Internal Revenue Service and state and local taxing authorities, laws requiring the registration of businesses are enforced by the business registration authorities in the various states, counterfeiting of trademarks and patent infringement is subject to the imposition of legal remedies under the intellectual property regime, and relevant health and safety regulations are enforced by specialised regulators. To be sure, the failure of firms in the informal economy to abide by these rules can affect their role in the market, to the extent that firms that do not comply with these regulations likely incur fewer costs than firms that comply with regulatory requirements. Nonetheless, these problems are more effectively addressed by specialised regulators who have particular expertise and appropriate enforcement tools.

3. To some extent, the market can play a role in correcting competitive distortions created by the informal economy. In some sectors, consumers may perceive goods and services provided through the informal economy as being of uncertain quality and purchase them from informal sources only at a substantial discount. The FTC’s consumer protection function includes a consumer education component which, among other things, provides information to consumers about doing business through the informal economy.

4. In cases in which informal market participants play a role in an antitrust market under investigation, the role of those market participants is taken into account just as formal participants are. Their market shares would be estimated according to the best available data and their ability to constrain an anticompetitive rise in prices or decrease in output would be considered. Consideration of their ability to constrain prices would, of course, need to take into account any limitations on their competitive significance that is caused by the informal nature of their market participation, the likelihood of market exit that might be caused by law enforcement efforts, and the extent to which price discrimination is feasible against an infra-marginal group of purchasers who insist on lawful products and who qualify as a distinct market.

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1 According to the World Bank, it takes six days to form a business in the United States, as opposed to 64.5 days in the Latin America and the Caribbean region; 40 days to deal with construction permits as opposed to 271.1 days in sub-Saharan Africa; and 12 days to register real property, as opposed to 106 days in South Asia. World Bank, Doing Business Project, available at http://www.doingbusiness.org/.

5. For instance, the Department of Justice investigated the formation by the major record companies’ of two joint ventures, pressplay and MusicNet, for the sale and distribution of digital music to consumers. Among the issues considered in the investigation was whether competing distributors of digital music over the Internet, including the informal unauthorised sharing of digital music among consumers, would limit the ability of the joint ventures and the parent record companies to exercise market power in recorded music in their Internet subscription services and in their positions in the distribution of music on physical media. Based in part on the well-publicised size of the informal sector in the music industry, the Department closed its investigation of the joint ventures without taking any action.

2. Removal of Incentives to Participate in the Informal Economy

6. Identifying the most appropriate role for a competition agency in addressing market distortions caused by the informal economy requires asking why firms operate in the shadows rather than as part of the formal economy. While there are many reasons, one documented cause is that burdensome regulation can make it difficult for entrepreneurs to enter the formal market and thus drive them underground. As Hernando De Soto notes:

   “in Peru, for example, it takes a new entrepreneur thirteen years to overcome the legal and administrative hurdles required to build a retail market for food that would help take vendors off the street; twenty-one years to obtain authorisation to construct a legally titled building on wasteland; twenty-six months to get authorisation to operate a new bus route; and nearly a year, working six hours a day, to gain the legal license to operate a sewing machine for commercial purposes.

   In the face of such obstacles, new entrepreneurs hold their assets outside the law and therefore do not have access to the facilitative devices that a formal legal system should provide to help them organise and leverage resources. Because they have no secure property rights and cannot issue shares, they cannot capture investment. Because they have no patents or royalties, they cannot encourage or protect innovations. Because they do not have access to contracts and justice organised on a wide scale, they cannot develop long-term projects. Because they cannot legally burden their assets, they are unable to use their homes and businesses to guarantee credit.”

7. Submissions made by participants in this Global Forum echo this theme. According to Ukraine, “emergence and development of the informal (underground) economy is a reaction to excessive tax and regulatory pressure on the part of the state,” and it takes 33 days and 115 Euro to start a business, a process that 70% of Ukrainian survey respondents described as difficult or very difficult. Mongolia tells us that among the reasons why herdsmen prefer to sell their livestock to the informal sector instead of to established processing plants is the many kinds of documents they are asked to provide by the latter.

8. Even though the presence of the informal economy is not as significant in the United States today as it is in some other countries, its experience during the “Prohibition era” in the 1920s amply illustrates the potential for regulation to fuel the rise of a vigorous informal sector. In 1920, the 18th Amendment to the United States Constitution effectively prohibited the production, sale, importation, and export of

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alcoholic beverages. As a result, an entire industry was effectively replaced by an informal sector, much of which was dominated by organised crime. Tax revenue previously generated by the sector was lost to the government altogether. When Prohibition was repealed in 1933, most of the industry returned to the formal sector.

9. While regulation clearly has an important role in protecting consumers’ health, safety, and well being, a valuable role that a competition agency can play is to encourage regulators and lawmakers to balance the costs and benefits of regulation. In the United States, through their competition advocacy functions, the DOJ and FTC assist in such balancing when the regulation in question appears to unduly harm competition. This function has a long history at both agencies and was in “full swing” at the FTC since at least June 1980, which was around the time that the move to deregulate air and surface transportation was beginning to take hold. More broadly, the Office of Information and Regulatory Affairs in the Office of Management and Budget has responsibility for balancing costs and benefits of federal regulation generally. Without an informed balance of costs and benefits, it can be difficult to understand the hidden effects of regulation and to recognise when those costs outweigh the desired benefits. Indeed, there are many cases where proponents of regulation assert some public benefit when the real purpose and effect of the proposed regulation is to restrict or eliminate competition.

10. Through its competition advocacy functions, a competition agency can bring great value by helping to illuminate the difference between the legitimate purposes of regulation and attempts to use regulation to hinder competition. Restrictive business regulation is typically promoted by those who have an economic stake in restricting entry into markets, normally vested incumbents.

11. More broadly, competition agencies may be among those within government who institutionally appreciate the importance of applying a cost-benefit analysis to regulation. They may thus be well-positioned to assist legislators and regulators to develop an approach to regulation informed by an understanding of how their actions can create or destroy incentives for entrepreneurs to participate in the formal economy. In some cases, the competition agency may be the only government institution with the expertise, interest, and resources to balance the costs and benefits of regulation and to advocate publicly for the removal of regulations that prevent entrepreneurs from entering the market.

12. As other participants in this Forum have pointed out, the informal sector is most prominent in sectors that require little capital, use primitive production and marketing methods and employ unskilled workers. We examine sectors meeting these criteria in which we have engaged in competition advocacy aimed at explaining to regulators and legislators how burdensome regulation impedes entrepreneurs from entering markets.

13. While these interventions were aimed at increasing competition and were not specifically aimed at moving entrepreneurs from the informal sector to the formal one, the effect may have been the same.

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7 James C. Cooper, Paul A. Pautler, Todd J. Zywicki, Theory and Practice of Competition Advocacy At The FTC, 72 Antitrust L.J. 1091, 1094-95 (2005).

8 See http://www.whitehouse.gov/omb/inforeg/regpol.html.

9 Submission of Jordan, ¶24.
2.1. Taxis

In the United States, taxi services are regulated at the state or local level. Although the details of regulation vary from place to place, most major cities continue to regulate entry and fares in some manner, most also regulate the types of service that can be provided (e.g., minimum number of cabs per company or association, 24/7 coverage of telephone requests, shared riding, conditions for service refusals, definitions of service areas, required dispatch capability, required taximeters), vehicle and driver characteristics (e.g., cab age and design, signs, no criminal background, knowledge of the city streets and landmarks, record keeping, neatness, facility with the English language, and sensitivity training), and service quality (e.g., cab cleanliness, maximum response times). In addition, jurisdictions often regulate the maximum hours of service per driver per day, license transferability, safety inspection frequency, and insurance and bond requirements. In some cities, particularly around airports, a significant unlicensed sector operates outside of the formal economy.

From the time that most cities in the United States adopted entry restrictions in the 1930s, a time when many U.S. industries sought governmental protection from competition, a handful of experiments with taxicab deregulation have provided important evidence on the relationship between regulation and market entry. The involvement of the Federal Trade Commission in this sector has focused primarily on efforts to assist deregulation in the industry, through reports and advocacy efforts, including 19 filings with various local authorities from 1984 through the present. The FTC’s advocacy efforts were largely based on a staff report on taxicab regulation.

Among other things, reviews of the effects of deregulation experiences in the United States indicate that the number of cabs and cab companies rises and, therefore, employment opportunities and the number of cab hours of service rise and that the bulk of the new entrants are individual drivers who serve taxi-stand markets that do not require radio-dispatch capability. Entry restraints were not shown to have any appreciable benefit to consumers. While the reviews did not address the extent to which deregulation reduced the number of unlicensed cabs on the street, it is fair to infer that many of the newly licensed taxis may have come from the ranks of unlicensed drivers.

2.2. Trucking

Trucking is an industry that is highly susceptible to participation by the informal economy. Entry into the trucking business requires only a truck and a telephone, and may be paid for in cash. Thirty years ago, interstate trucking was heavily regulated at the federal level, with new entry restricted and specific routes subject to approval. Deregulation of the industry began in 1980. Today little economic regulation of interstate trucking remains, although regulation of intrastate trucking at the state level persisted for years afterwards. Entry is no longer restricted and barriers to entry are low.

13 The need for targeted regulatory intervention may continue to exist at airports and taxi stands, based on the particular characteristics of that part of the market.
18. The FTC and DOJ were active proponents of trucking deregulation, and sought to advocate competition in the sector by explaining the costs that trucking regulation imposed on consumers and the benefits of competition. The Federal Trade Commission (FTC) alone made at least 17 such submissions, principally directed to state governments that retained the power to regulate intrastate trucking even after interstate regulation ended at the Federal level. In a submission to the Railroad Commission of Texas, for example, the FTC presented evidence that shipping of a common consumer product cost $2.52 per mile between two key cities in Texas' regulated market cost only $1.46 per mile for a similar distance in the unregulated interstate market. It also cited the positive effects of deregulation in states that had deregulated: lower prices, continued service to small communities, and undiminished service.

19. A 1988 FTC study is especially instructive because it closely examined and addressed the arguments advanced by proponents of trucking regulation. Opponents of trucking deregulation have made four main predictions about the effects of partial deregulation: that service to small communities will be reduced, that “destructive competition” will ultimately harm consumers, that confusion and inefficiency will be created, and that highway safety will deteriorate. None of these predictions was supported by the evidence.

20. According to the 1988 FTC study, federal and state regulation of trucking drove prices up and encouraged inefficient practices. Among other things, it found that employment in the trucking industry has risen sharply since deregulation. In 1980, 1.48 million people were employed in trucking services. By 1987 that number had risen 29.2% to 1.8 million. Regardless of whether these new entrants came from expansion or by bringing truckers from the informal to the formal sectors, deregulation reduced incentives for truckers to operate in the shadows.

3. Conclusion

21. The United States’ experience has shown that removal of burdensome regulation can open the way to new entry into a variety of sectors of the economy and help to eliminate disincentives from participating in the formal economy.

22. The United States’ experience also highlights how a competition agency can help legislators and regulators to understand the importance of balancing the costs – including the possible expansion of the informal sector -- against the benefits of regulation. The fact that some regulations serve only to advance

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14 E.g., Comment of the Staff of the Bureau of Economics to the South Carolina Legislative Audit Commission (1994), available at http://www.ftc.gov/be/healthcare/docs/V940003%20SC%20Trucking%20Regulation.PDF.
15 Letter from Thomas Carter, Regional Director, Federal Trade Commission, to Raymond Bennett, Director, Transportation/Gas Utilities Division, Railroad Commission of Texas, October 2, 1989.
17 When trucking was deregulated in the 1980s, it was expected that private carriage – trucking service that was performed in-house by firms that were not regulated by the Interstate Commerce Commission but was inefficient because firms could carry only their own goods and thus had many empty return trips – would be replaced by for-hire service as prices declined. In fact private trucking has not lost a significant market share, and some transportation experts attribute this to private carriers entering the formal for-hire market.
18 It would go too far to suggest that the underground economy does not exist in the United States. Even after the repeal of prohibition, a significant traffic in illegal alcohol persisted, especially in mountainous southern regions, in response to the pervasive state regulation that replaced prohibition. Passengers arriving in American airports are familiar with promoters of unlicensed taxis that frequent the arrivals areas.
the economic interests of their proponents does not mean that others do not serve a legitimate purpose. The state does have a legitimate interest in ensuring the safe operation of trucks, and ensuring that taxis are safe and readily available. Due consideration must be given to the legitimate ends of regulation, while putting them into context and balancing them against how they impact entry.
CONTRIBUTION BY ZAMBIA
ALLEGATION OF UNFAIR PRACTICES BY ZAMBIA BANANA TRADERS ASSOCIATION AGAINST BANANA FARMERS

--Zambia--

1. Information and relevant background

1. On 15th July, 2008, the Commission received a complaint from Zambia Banana Traders Association (ZABATA) against commercial banana farmers who had constructed cold rooms for treatment of bananas. Specifically, ZABATA alleged that there was a group of farmers who had stopped supplying them bananas and had instead opted to trade as both wholesalers and traders.

2. According to ZABATA, their refusal to supply has resulted in the association not having enough bananas to sell as they cannot source bananas elsewhere. ZABATA claimed that they needed about 35 tonnes a day to meet consumer demand. At the time of the complaint, the association was reportedly only able to access about 10 tonnes of bananas per week, which they were sourcing from small scale farmers.

3. The other concern by the association was that the commercial banana farmers were likely to drive them out of business as the traders were not able to compete with them as the farmers end up selling directly to consumers at relatively low prices which were not competitive for the middle men (i.e. the traders). Further, ZABATA wanted to know whether these farmers had obtained licenses from Government to engage in wholesaling and retailing as well.

2. Legal provisions and assessment tests

2.1 Section 9 of the Act states that:

“(1) It shall be an offence for enterprises engaged on the market in rival or potentially rival activities to engage in practices appearing in sub-section (2) where such practices limit access to markets or otherwise unduly restrict competition. Provided that this subsection shall not apply where enterprises are dealing with each other in the context of a common entity wherein they are under common control or where they are otherwise not able to act independently of each other.

(2) This section applies to formal, informal, written and unwritten agreements and arrangements.

(3) For the purposes of subsection (1), the following are prohibited:

.....

(f) concerted refusals to supply goods and services to potential purchasers.”

2.2 Assessment Tests

4. In view of the provision of Section 9, the following are the Statutory Assessment Tests:

(i) Whether there is rivalry or potentially rival activities in the relevant market Section 9(1.)

(ii) Whether there was concerted refusal to supply

(iii) Whether the defendant/s was/were the only feasible suppliers of the goods and services
3. Findings

3.1 Parties

3.1.1 Zambia Banana Traders Association (ZABATA)

5. ZABATA was formed in 2002 and was registered under the Registrar of Societies in the same year (ZABATA constitution is attached). ZABATA is situated at Soweto behind City Market. ZABATA has over 200 members who deal in treating and selling of bananas which are sourced from commercial farmers.

6. ZABATA submitted that the farmers had stopped supplying them with bananas as they opted to sell the bananas directly as wholesalers and retailers. ZABATA alleged that this has likelihood to drive them out of business as they are unable to compete with these farmers who are selling at low prices which are not competitive to the middle men. ZABATA also alleged that they are having shortages of supply as an association as before, they could access about 35 tonnes of bananas per day from farmers but are currently accessing only about 10 tonnes of bananas per week. ZABATA, however, said that there was no shortage of supply of bananas to meet consumer demand as the farmers were selling instead of them.

7. ZABATA also clearly stated that these farmers were acting as individuals in their refusal to supply them with bananas.

3.1.2 Banana Farmers

8. These are commercial farmers distributed mainly on the Southern part of Zambia. They constitute more than half the number of total commercial farmers involved in banana production in Zambia. They include Chiawa Farms in Kafue District which runs a cold room at Citizen Breweries in the industrial area in Lusaka; Go-Banana in Mazabuka which runs a cold room opposite Mukupa Guest House about 500m away from Soweto Market; Hot Man of Sikongo in Siavonga which runs a cold room opposite Stanbic Bank in the Industrial area; Mafosholo of Siavonga which runs a cold room at Soweto market and Jerry Cabine of Chiawa who is into exporting of bananas.

3.1.3 The Zambia National Farmers Union

9. Zambia National Farmers Union (ZNFU) expressed ignorance of the existence of ZABATA and said that they did not appear in their data base. As such, ZNFU said they could not say that they ever had dealings with ZABATA.

3.1.4 The Relevant Product Market

10. The relevant market is the distribution of bananas to the middlemen (wholesalers and retailers)

3.1.5 The Geographic Market

11. The geographic market is Lusaka (the capital city of Zambia).

3.2 Competitors and Market Shares

12. The market for the production and supply of bananas is highly fragmented and it is difficult to ascertain and assign market share to each producer, more than that the sector is not formally organised – both from the producer and the retail trade. However, the principal suppliers of ZABATA are the banana
growing commercial farmers, whose competition is largely imports which trickle in through only two South African owned national retail outlets.

13. Apart from the formally organised commercial farmers, ZABATA has another source of bananas for resale and this is the micro and small scale farmers who are unable to satisfy their demand. Currently these farmers are reckoned to only supply ZABATA about 10 tonnes per week as opposed to about 35 tonnes per day that ZABATA would order from the farmers.

3.3 Major Customers

14. Major customers are the general public who buy banana at Soweto market. Soweto market is a mass market with both in-door and a massive outdoor market area of all informal traders dealing in all kinds of agricultural products. Over the years, the market has also began to carter of informal sector furniture, second hand clothes, car spare parts, and traditional medicinal herbs.

3.4 Ease of Market Entry

15. There seems to be easy entry in this sector as anyone can acquire a market stall from Lusaka City Council and trade. One can either be given a wholesale or a retail licence depending on the needs of the trader.

4. Analysis of the Case

16. It would appear from the market conduct that the banana farmers were acting in collusion - either an explicit or passive collusion to avoid selling bananas to the informal traders who for obvious, may not have been a steady and lucrative market and thus opted to add a bit more value to the bananas and trade directly with some of their valued customers.

17. However, the informal sector is not legally protected under the law and thus the accusation against the banana farmers did not appear to be legally enforceable against an “illegal” grouping of informal self-employed traders. The trend appeared to be targeted at reaching directly the formal trade of the market where the returns for the farmers were higher and steadier, thus eliminating the informal middle-man. The traders wanted to be protected using the competition law – which law could not protect them.

18. It has been submitted that through the farmers directly selling and by-passing the middle-men, the consumer ends up buying the product at a lower price. This achieves one of the major objectives of the Act, which is to achieve consumer welfare. This has a positive effect on the economy in general.

5. Conclusion

19. This case is a paradox of how a possible collusive conduct, which is prohibited outright, could not be enforced due to lack of a legal platform by the complainant – the informal trader – hence not considered an enforcement priority within the resources of the Commission.

20. The Commission also considered the fact that the banana farmers were actually adding value to the process and affording the consumer to buy bananas in a more conducive state and at a relatively lower price.
6. **Commission decision**

21. From the analysis above, the Commission resolved to discontinue the investigations and closed the case.
CONTRIBUTION BY SIDDHARTHA MITRA
(CUTS INTERNATIONAL)
INFORMAL SECTOR AND COMPETITION: A COMPREHENSIVE AGENDA FOR RESEARCH AND ACTION

Siddhartha Mitra¹
--CUTS International--

1. Abstract

The existence of the informal sector has both positive and negative implications for the level of competition in the economy. The positive influences emanate from the fact that informal firms are usually small and therefore individually less likely to be the source of dominance than formal firms. Negative implications can arise in myriad ways: unmonitored price collusion and dominance by some informal sector firms affecting other informal sector firms; formal sector being subjected to unfair competition by the informal sector in the form of lower prices facilitated by tax avoidance, hard to catch product adulteration and even physical obstruction; and last, formal sector firms employing anti-competitive practices such as predatory pricing to eliminate informal competition.

2. The paper recommends that the decision to formalise the informal sector should be based on a cost-benefit analysis. It goes on to elaborate on the various methods of formalisation: reduction in the number of procedures/clearances involved or time involved in registration of firms in the formal sector, extent of corruption that determines the magnitude of bribery involved in the same process; and reduction of disincentives such as high tax rates coupled with enhancement of incentives such as credit leveraging and entrepreneurial assistance/training provided by the government to the formal sector.

2. Introduction

In many developing countries such as India the informal sector accounts for a large chunk of economic activity. As informal firms are very different from formal firms in nature, management and scope for government control, the existence of a large informal sector can have significant implications for the level of competition in the economy.

4. This paper specifies a research and action agenda which examines the implications of the informal sector for economy wide competition through a component by component examination of effects. It goes on to explain how such examination can help in deciding whether formalisation of this sector is desirable from the viewpoint of enhancement of competition. Last, it spells out the needed research and action in the implementation of a decision to formalise.

3. Working Definition of the Informal Sector

Though the 'informal sector' has been defined in a many ways (see Sethuraman, 1974), adding to the confusion in identifying it, a convenient and broad definition is “economic activity in a nation which is not administered in any substantial way by the government”. Informal sector enterprises do not pay any taxes to the government or adhere to labour regulations nor are they the recipient of government provided/facilitated credit, entrepreneurial advice/training or other facilities. Though informal sector firms do not have to adhere to formal rules laid down by the government, those in the same product line often follow a set of informal business norms arrived at by mutual consent.

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6. The informal sector needs to be decomposed into various parts to facilitate better analysis of its behaviour:

   a) Activities that deal with the distribution and manufacture of products that are strictly banned (manufacture of mind altering drugs, certain explosives etc and services such as prostitution)

   b) Cross-border trading in products which can be legally consumed but is illegal on account of not being registered with the government and/or in violation of embargoes and official tariffs

   c) Unauthorised internal distribution of services /amenities which are also being lawfully produced/distributed (power theft and distribution to unregistered customers)

   d) Production of goods/services which is not administered by the government (e.g. that by small workshops manufacturing shoes, small restaurants etc)

   e) Hawking and vending activities, which the government finds difficult to account for or administer, because of small magnitudes and geographical mobility

7. Note that a) is very different from the other categories which have a formal counterpart – businesses registered with the government producing the mentioned products.

4. The Informal Sector and Competition

8. It is only the formal sector which is administered by the government. Thus, the government has records of the location, number and business activity of firms operating in this sector but not of firms in the informal sector. Thus, the firms in the latter sector are generally outside the ambit of competition law. Because these firms usually do not maintain any written records or give receipts for payment it would in any case be very difficult to punish these for anti-competitive practices. Usually their small size and large number ensure that detection of anti-competitive practices by informal sector firms and consequent punishment are not economically viable for competition agencies because of enforcement costs exceeding economic benefits.

9. The following sum up the impact that the informal sector has on the level of competition in the economy:

4.1. Positive impact

10. In many product lines, such as fruit and vegetable selling, the informal sellers in a market approximate a perfectly competitive set up as individual businesses are small, products are identical (for instance, cauliflower sold by seller A is very similar to that sold by seller B) and sellers are physically proximate to each other.

11. Such perfect competition is often not seen in the formal sector because of various reasons: larger businesses, product differentiation either because of distinctive content or packaging etc. The assumption here of course, is that more competition is desirable with perfect competition constituting an ideal state in which competition among firms is maximised i.e. a frictionless world.
4.2. **Negative Impacts**

12. Again these are of different kinds:

- A larger size of the informal sector in any product line implies a smaller formal sector. A smaller number of firms in the formal sector increases the market power of individual firms and therefore has a deleterious impact on competition. (B1)²

- Because the government does not have a list of informal firms it is often difficult for the competition authority to identify abuse of dominance from the formal sector impacting the informal sector (B2). This can be a powerful anti-competitive force when the number of formal firms is small and these are geographically spread out, giving rise to strong monopolistic or oligopolistic tendencies.

   For example, consider a single formal producer/distributor of milk competing against numerous informal producers (these are milkmen not registered with the government). The formal producer/distributor might try to wipe out competition from the rival milkmen through predatory pricing. The competition authority might not be able to rigorously establish ‘abuse of dominance’ because of the absence of statistical data on prices charged by informal producers or even of their existence, the reluctance of informal producers to lodge complaints because of their unofficial status and the difficulty in comparing informal product quality to formal product quality.

   A real life version of this example was noticed in Peru where predatory pricing by the major milk industrialist against small dairy producers brought down the price of milk in Peru to $0.26 while it was $0.38 and $0.43 in neighbouring Chile and Brazil (Via Lactea, 2007).

- Anti-competitive practices originating within the informal sector and impinging on informal sector firms (B3): Competition inside the informal sector will be high if it is made up of a large number of small producers/distributors selling/producing identical products. Whether that is indeed the case in the informal sector for every product line is a question which begs further research. For example, vegetable markets and their resident sellers often belong to the informal sector. The fact that they sell visually indistinguishable products and are not separated by any considerable physical distance leads to an equalisation of prices for their product, over the level of which each seller exhibits very little control.

13. But whether all product-specific informal sectors have the same characteristics as the mentioned vegetable market is an interesting question that needs to be explored. The most important feature that needs to be examined is the relative sizes of various players operating within the informal sector. Consider an informal seller of sweets who is suddenly faced with competition from another sweet seller who sets up his shop nearby. If the former seller has enough cash balances to fall back on, he can resort to predatory pricing, thus squeezing the second seller out of the market. The important question is whether such differences in the size of wealth exist among agents in the informal sector.

14. What about collusion in the informal sector? Again the unorganised nature of processes makes it very difficult to ascertain whether there is collusion inside the informal sector, say a vegetable market. However, systematic research which covers different vegetable markets can determine whether there are any unexplained differences in prices across vegetable markets (the assumption being that within a vegetable market, proximity leads to identical prices for a given product across sellers but also might

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² Note these letter-number combinations are used to denote various categories of effects of informality on economy wide competition and sub-categories within these
facilitate collusion). If such unexplained differences do exist, then price collusion which holds product prices artificially above the competitive level is a major possibility.

15. Another major source of distortion in competition is product adulteration. Most items of consumption, be these food items or furniture, can be adulterated without the consumer knowing that this is the case. Adulteration can be employed to augment profits as the consumer’s lack of knowledge about product inputs can be used to cut costs without commensurate change in prices. Adulteration not only detracts from consumer welfare but its differential application by producers implies that competition is often unfair and results in a low equilibrium level of product quality. Misleading advertisements in the informal sector (signs on shops etc) can also be treated as ‘product adulteration’.

16. Thus, anti-competitive practices originating in the informal sector and impinging only on informal sector firms are possibly of three types:

- Abuse of dominance (B3a)
- Price collusion (B3b)
- Product adulteration (B3c)

17. Anti-competitive practices originating within the informal sector impinging on the formal sector (B4): Not only does the existence of the informal sector have implications for the extent of competition among constituent agents but it also influences the sales of the formal sector. Note that many products are sold by both formal and informal sector firms. Because informal firms do not pay any taxes they might be able to out price formal sector firms. This amounts to unfair competition.

18. Informal sellers, such as neighbourhood vegetable vendors, are often more mobile than formal sellers selling the same product who are fixed in space. Purchase of products from such informal sellers might be more convenient for customers. In many cases informal sellers might physically block access to formal sellers. For example, hawkers and peddlers outside formal sector shops or on footpaths leading up to these shops might create difficulties for parking of cars or even for pedestrians trying to access these shops.

19. A real life example of unfair competition provided by the informal sector to the formal sector can be cited from the Peruvian experience. In the 1970s the 30 largest bus companies in Peru commanded 70 percent of the bus fleet and 60 percent of the routes. After the 1970s numerous small/informal bus operators entered the industry and depleted the market share of the large bus companies given that they did not have to pay much of the taxes required from the formal sector or adhere to many of the formal quality norms. As a result in 2000, the mentioned top 30 percent commanded only 30 percent of the fleet and 12 percent of the routes (Roca et al, 2008).
Table 1. Impact of Informal Sector Expansion on Economy Wide Competition

<table>
<thead>
<tr>
<th>Type of effect</th>
<th>Description/Component</th>
<th>Symbols</th>
</tr>
</thead>
<tbody>
<tr>
<td>Positive</td>
<td>Caused by small geographically proximate firms selling uniform product</td>
<td>A</td>
</tr>
<tr>
<td>Negative</td>
<td>Depressing the number of formal firms</td>
<td>B1</td>
</tr>
<tr>
<td>Negative</td>
<td>Increase in incidence of abuse of dominance by formal firms</td>
<td>B2</td>
</tr>
<tr>
<td>Negative</td>
<td>An increase in the size of the informal sector increasing the scale of associated anti-competitive practices</td>
<td>B3</td>
</tr>
<tr>
<td>Negative</td>
<td>Abuse of Dominance</td>
<td>B3a</td>
</tr>
<tr>
<td>Negative</td>
<td>Price Collusion</td>
<td>B3b</td>
</tr>
<tr>
<td>Negative</td>
<td>Product Adulteration</td>
<td>B3c</td>
</tr>
<tr>
<td>Negative</td>
<td>Increase in unfair competition from the informal sector for the formal sector</td>
<td>B4</td>
</tr>
</tbody>
</table>

Note: The meaning of symbols remains unchanged in the figure below.

20. The net impact of the informal sector on the level of competition in the economy is an algebraic sum of the positive and negative effects. It is a matter for research to investigate the relative magnitudes of these effects to determine whether the net effect is positive or negative. Interestingly, the answer could be qualitatively different across countries and could be a function of the economic, geographic and demographic characteristics of the country.

21. The table above summarises the various impacts of the informal sector on economy wide competition. Note that effects outlined in bold font represent broad categories of effects; the constituent sub-categories if any are outlined in ordinary font. The figure below presents a more visual depiction of these effects. Arrows that go from the informal sector to the formal sector or vice-versa depict inter-sectoral effects while circular arrows refer to ‘within sector’ effects. The arrow that emanates from the boundary between sectors illustrates the effect that the shifting of the boundary has on formal sector competition.

![Impact of Informal Sector on Competition](image)

Note: Refer to Table above for a classification of impacts.
5. **When do we need to tackle informality?**

22. Because informality is often synonymous with small size (a characteristic which aids competition) and formality is associated with larger sizes, in many cases formalising the informal sector might not be desirable for competition. It is only when the sum of the magnitudes of negative effects (B1-B4) overwhelms the positive effects of small size that accompany informal activity that formalisation of the informal sector might be advocated.

23. In other words, any decision to formalise the informal sector must be preceded by a rough cost-benefit analysis with respect to implications for competition. Given a policy objective of maximisation of competition, a general policy decision to formalise is recommended if the net expected benefit in competition terms is positive. Alternatively, a broader decision framework can be used: net benefits from competition can be added to those in terms of tax revenues etc to arrive at a more holistic measure of net benefit from formalisation. The decision to formalise then rests on whether this measure of net benefit is positive or negative.

24. Another way to make this approach more nuanced would involve taking the decision of formalisation separately for the different sectors of the economy (dairy, fruits and vegetables, construction etc) on the basis of separate cost-benefit analyses.

6. **A guide to formalisation**

25. Once the decision to formalise is taken it obviously has to be implemented by nipping the motives for running/establishing informal firms in the bud. The various reasons why individuals set up informal firms might be the following:

- Too many procedures and clearances required for setting up formal firms
- Time consuming nature of the above procedures with attendant opportunity costs of time borne by the entrepreneur
- Corruption at the entry points to the formal sector i.e. money has to change hands to get the required clearances
- Credit and other facilities provided by the government for formal sector firms not large enough to entice entrepreneurs into the formal sector.
- High tax rates in the formal sector

26. Each of these barriers to formalisation has to be tackled (see Mitra, 2005 for related discussion). For example, the number of procedures and clearances required for setting up of firms can be pruned by following the example of countries which require fewer procedures/clearances. The Doing Business 2008 Report published by the World Bank can help in identifying countries with the fewest required procedures and their example could be followed.

27. While pruning the number of procedures, legal or constitutional costs have to be taken into account i.e. the removal of procedures/clearances from the list of requirements should be sought only if a) these are not central to the process of setting up business and its economic ramifications and b) their removal is not associated with prohibitive legal or constitutional costs in terms of both time and money.
28. Total procedural time costs can be reduced substantially by identifying procedures that involve the highest costs. Again the Doing Business Reports of the World Bank might be helpful in this regard. In reducing the time costs, removal of the procedures with high time costs from the list of requirements might be a possibility but only if criteria a) and b) are met. The second way is to institute organisational changes i.e. clubbing procedures under common windows or instituting a single window system of clearances.

29. The removal of corruption requires a systemic analysis specific to each country. Such analysis is bound to reveal different causes of corruption. The first step in this regard is to ascertain whether the level of corruption is indeed high. Indicators such as the Corruption Perception Index estimated by Transparency International might be useful in this regard.

30. Once indices reveal the level of corruption to be high, then the involved researchers face the difficult task of ascertaining underlying reasons. The literature on corruption points to many possible causes of corruption – the existence of all of these has to be verified.

31. The list of possible causes, as pointed out by the economics literature, may be as follows:
   - Low salaries of government officials
   - Inadequate efforts/expenditure devoted to monitoring of government officials
   - Inadequate punishment or legal barriers in punishing government officials
   - Deeper causes e.g. corruption at the entry points of government service forcing recruited government officials to turn corrupt for repayment of debts thus incurred

32. If any of the above factors is/are found to be present and linked to the problem of corruption, then suitable remedial steps can be taken. The existence of deeper causes if ascertained can be helpful in working out a strategic approach for the elimination of corruption.

33. For example, if corruption at the entry points (see Mitra, 2003 for an elaborate discussion of this issue) is a significant cause for government officials turning corrupt then a strategic approach can concentrate on trying to remove corruption at the entry points only, rather than trying to remove it everywhere. This is because anti-corruption programmes involve costs in terms of human capital and money.

34. Cost and benefits of formal operation relative to that of informal operation might be another factor determining entry. If tax rates are very high then the government might consider reducing these. As a lower tax rate encourages entry into the formal sector, therefore, contrary to common perception, it might result in higher revenues for the government. In that case tax reduction might be a win-win measure for government and business.

35. The ability of the government to leverage easy credit for formal firms from the formal credit market and at rates much below those corresponding to the informal financing sector (suppliers of credit to the informal sector) might also encourage firms to enter the formal sector. Good entrepreneurial advice and training provided by the government might be another factor.
7. Conclusion

36. According to the paper the informal sector can be broadly defined as those producers/sellers who fall outside the scope of government control for various reasons. The existence of the informal sector has both positive and negative implications for the level of competition in the economy.

37. The paper then goes on to elaborate on the positive and negative influences. The positive influences emanate from the fact that informal firms are usually small and therefore individually less likely to be the source of any dominance. Negative implications can arise in myriad ways: price collusion and dominance by some informal sector firms affecting other informal sector firms; formal sector being subjected to unfair competition by the informal sector in the form of lower prices facilitated by tax avoidance, hard to catch product adulteration and even physical obstruction; and last, formal sector firms employing anti-competitive practices such as predatory pricing to eliminate informal competition.

38. The paper recommends that the decision to formalise the informal sector should be based on a cost-benefit analysis – the positive effects can be termed as competition related benefits and the negative effects as cost. A net negative effect justifies formalisation; otherwise continuation of informality might be desirable.

39. The paper goes on to elaborate on the various methods of formalisation: reduction in the number of procedures/clearances involved or time taken in registration of firms in the formal sector, corruption that determines the magnitude of bribery involved in such processes; and reduction of disincentives such as high tax rates and enhancement of incentives such as credit leveraging and entrepreneurial assistance/training provided by the government to the formal sector.

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CONTRIBUTION BY MS. TAIMOON STEWART
THE INFORMAL SECTOR IN JAMAICA: EXPLORING COMPETITION, COMPETITIVENESS, AND ANTITRUST ENFORCEMENT ISSUES

--Ms. Taimoon Stewart--

Abstract

1. The paper provides a brief description of informality in Jamaica and the features of this sector. A conservative estimate is that 41 per cent of GDP is generated by this sector, and businesses span the subsistence sub-sector through micro, small, medium and even large firms that do not conform to regulations and evade taxes. It concludes that informality is the norm in Jamaica.

2. Competitiveness of informal firms is reduced because of their expenditure on protecting themselves from criminal activities. Productivity levels can be increased if informal firms access government assistance, both financial and technical, but this requires firms to be registered. However, this can prove to be an incentive to move into the formal sector.

3. The Jamaican government is making serious efforts to eradicate corruption in customs, to stamp out evasion of customs duties, and to enforce the law in respect of tax obligations. However, there are bureaucratic bottlenecks that still need to be addressed, and the need to introduce good governance practices within government.

4. While under the Fair Competition Act (FCA), all businesses, regardless of size, are under the jurisdiction of the Fair Trading Commission (FTC), it does not cover practices involving evasion of government business regulations. The FTC does, in the course of its investigations, encounter firms that are operating illegally, and does engage in advocacy to the relevant government agencies. The FTC also encounters problems in defining relevant market because of grey areas in terms of market segmentation. However, there are geographic locations where markets are segmented.

The Jamaican Informal Business Landscape

Types of Business

5. Fifty-two per cent of the 2.7 million population of Jamaica lives in urban areas (Statistical Institute of Jamaica 2007) and there exists in these areas large and volatile inner cities, particularly in Kingston. Poverty and unemployment rates are high, and there is a large informal economy, here defined as economic activities in the production of goods and services that are unregistered and operate outside government regulation and taxation systems.

6. Features of this sector found in other countries also apply to Jamaica. It generally involves use of cash as the most common medium of exchange, or bartering or swapping goods or services. In both cases, it means receiving payment that is not traceable, and the income is not reported for tax purposes. Another feature of the informal sector is that labour laws, health conditions, safety standards, and location of activities according to zoning laws are all largely ignored. (Losby et al. 2002: 6-8). These strategies provide the informal business persons with a competitive advantage: paying lower wages, non-compliance with tax, and inattention to other regulations allow them to operate at cost levels that give them their edge (ibid: 37). In Jamaica, avoidance of custom duties is an important part of cost cutting strategies.

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1 Between 1989 and 2003, Jamaica’s poverty headcount ratio declined from 30.5 percent to 19.1 percent (World Bank Development Progress Report, October 2008). Many analysts attribute this remarkable phenomenon to the existence of the informal subsistence sub-sector in the economy.
7. Crime has a great impact on the competitiveness of both the subsistence sub-sector and established firms throughout the economy, as the criminals are organised “mafia-style” and extract “protection” money, rob, steal, and threaten physical safety. This has negative impacts on costs and productivity throughout the economy. In the World Economic Forum, Global Competitiveness Report 2008-2009, 22.7 per cent of Jamaican business persons identified crime and theft as the most problematic factor for doing business, while 12.7 per cent identified inefficient government bureaucracy, and 9.8 per cent identified corruption as the greatest problem. Small businesses were identified as the ones most affected by criminal activity (World Bank 2004, The Road to Sustained Growth in Jamaica. www.worldbank.org). These firms may not be able to pay the cost of high security and are thus rendered vulnerable to the criminals.

8. Types of businesses found in the informal sector include subsistence level operations, micro and small enterprises (MSEs), and even medium and large enterprises.

- In the subsistence informal sub-sector are found street vendors or itinerant traders selling out of vehicles or hand pushed carts. Others include domestic helpers and cleaners, hairdressers, gardeners, taxi-drivers, construction workers, cosmetologists, and so on. Businesses of these types can be very transient because of under-financing or unprofitability where there are too many players in the market. In the rural areas, they produce and sell food products (ground provisions, vegetables and poultry etc.), engage in agro-processing (jams, jellies, sweets, etc.) and even provide technical agricultural services, such as artificial insemination of animals (which has been learned from technicians and sold on at a lower price).

- There is also a multitude of persons operating as informal taxis in the transport sector, and competing with the registered taxis. There are no limits imposed on the number of registered taxis that can operate on a route. It is standard procedure for a car owner who needs additional income to operate illegally in this sector, or hire drivers to do so. As such, there are too many operators, too much competition, and too little regulation.

- Beyond these, there are the informal firms that deliberately remain invisible to escape meeting tax and regulatory requirements (MSEs, medium and large firms), the home-based business persons of higher education who do not register, and those who operate both in the formal and informal sectors. Medium, Small and micro firms employ approximately 84.9 per cent of the working population and are therefore very important. According to a recent IADB study, the size of the informal sector in Jamaica is estimated at 43 per cent of GDP as at 2001, and is estimated to have doubled over the previous decade.

9. The IADB study revealed that many enterprises are concentrated in low-productivity, labour-intensive activities, with some 60 per cent of persons operating in the informal sector engaging in

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2 Jamaica is an extremely open economy, and domestic firms compete with imports in their home market, and export competitiveness is lessened.

3 According to data published by the Statistical Institute of Jamaica, in July 2008, there were 1,163,200 persons employed, and of that, only 175,936 were employed in large establishments. Therefore, 987,264 persons were employed by medium, small, and micro enterprises.


5 The target groups that were measured in this study were in three categories: pure tax evaders (operating registered businesses but not reporting earnings); the irregular economy (unregistered businesses); illegal activities (evading taxes, unregistered and criminal activities). The survey was based on a size-stratified random sampling of 1,226 out of a full listing of Jamaican [business] premises.
wholesale/retail trade. Most own-account business persons do not have a bank account, either maintaining total financial self-sufficiency or managing their affairs through other informal financial institutions. Banks require a business plan and lower income persons generally do not have the skills to produce it, and do not have the money to pay someone to do it.

Level of non-compliance

10. An important finding of this study is that most Micro and Small Enterprises (MSE) do comply with some regulations, but not all. The authors concluded that “… informality is a continuum…”, given that most MSEs satisfy some requirements but not others, and that informality is, to a large extent, standard operating procedure among Jamaican MSEs (IADB 2006:27). Indeed, in the January 2009 budget speech, the Prime Minster pointed out that a mere 1 percent of firms pay 80 per cent or more of taxes, and only a handful of the employed labour force pays income tax. He also said that far too many eligible firms are not registered to pay or do not remit their General Consumption Tax (The Gleaner, Editorial, Monday January 19, 2009).

11. The authors of the IADB study found that ignorance and high bureaucracy were among the most cited reasons for non-compliance among MSEs. Yet, the World Bank study, Doing Business 2009 (www.worldbank.org), which undertook to compare regulations in 181 countries, found that in Jamaica, six procedures were required which took 8 days to accomplish, at a cost of 7.9 % GNI per capita. Jamaica had a global rank of 11 out of 181 countries. The Business Registration website for Jamaica confirms this.

12. The Doing Business 2009 ranked Jamaica a low 173 out of 181 countries in terms of ease of paying taxes. They found that 414 hours were needed to prepare and submit tax returns, and the total tax rate was 51.3 per cent of profit. In the Global Competitiveness Index, 8.2 percent of businesses felt that the tax rate was the most problematic factor for doing business. It therefore seems that the bureaucratic tangle is at the level of doing business rather than the initial registration, and procedures for paying taxes. This and the high rate of taxation are the major disincentives to compliance. These factors are exacerbated by lack of trust in government’s usage of the tax dollars, lack of enforcement on the part of government, and a culture of lawlessness in the country.

Trends toward formalisation of firms

13. Certainly there are advantages to be gained by subsistence level informal businesses if they moved to the formal sector and some businesses are taking advantage of incentives. For instance,

- registering with the Ministry of Agriculture would then give persons access to free plants, chicks and other supplies; and

- in times of natural disaster, such as hurricane damage, only those businesses that are registered would get access to government’s recovery assistance. Insurance is generally too expensive for these poorer entrepreneurs.

14. In addition to these carrots, government is also wielding the big stick. It is becoming increasingly difficult to evade custom duties and tax obligations, government increased enforcement in the last year. A six month tax amnesty was offered to non-compliant businesses, ending 31 October 2008; recalcitrant tax payers were invited to pay fully or in tranches, without incurring the interest and penalties involved. Since then, the Tax Administration has taken legal action against 200 self employed persons and companies, for

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6 The “pardner” system, which involves pooling of resources by depositing each week a small amount of money, and taking turns accessing the accumulated capital (getting a draw).
failing to make arrangements to pay outstanding taxes. They may have to pay over half a billion Jamaican dollars in outstanding tax and fines (4.8 million Euros). There is also a crackdown on firms that have not been submitting funds collected from the General Consumer Tax to the relevant government authority. Moreover, systems are being put in place, requiring a tax registration number (TRN). This is similar to the social security number in the US, the intention being that the TNR will have to be provided for every transaction with a government agency. In addition, a tax compliance certificate (TCC), has recently been introduced and this must be provided by importers before goods are cleared from the wharf or airport. Tax evasion will therefore become much more difficult.

15. The transport sector poses a serious challenge because of the size of informal operators, the difficulty of enforcing regulations due to the chaotic and brutal nature of the fierce competition in the sector. There is a concern that removing illegal taxis and bringing efficiencies to the sector my incur a high social cost and lead to increased crime as such operators lose income.7

The Interface between the Formal and Informal Sectors and Competition Issues

16. There is trade taking place between the formal and informal sectors. Larger businesses supply informal businesses with goods:

- Street vendors buy final goods or intermediate products from the formal sector (wholesale stores, supermarkets), and then sell these goods on the streets.

- Manufacturers and distributors supply goods to MSEs and corner shops in inner cities. For instance, Grace Kennedy Ltd., one of the conglomerates in the economy, stocks informal businesses in inner-cities and rural areas with agro-processed products and give a time line to pay. Vendors are provided with biscuits and sweets.

- Supermarkets provide vendors with expired or soon to be expired goods to sell on the streets. Retailers use vendors to sell their goods on the pavements outside their stores and the GCT is not charged (a practice called “fronting”). By doing so, the established businesses can compete with the informal businesses at their level, and also gain advantages over their rivals in the formal sector.

17. Large formal businesses purchase goods from the informal sector. For instance, Courts Ltd. and Singer Ltd. purchase furniture from small informal operators. Grace Kennedy Ltd. purchases raw materials from the informal producers in the agricultural sector. These large conglomerates do not face competition from the subsistence level operators. Rather, they draw consumers away from the informal sector by offering hire purchase arrangements with guarantees, and a monthly payment that is manageable for lower income groups.

18. Some persons employed in the formal sector also work in the informal sector in order to supplement their income: tradesmen such as electricians, plumbers; or civil servants may operate as private taxi drivers in their non office hours, or higher skilled workers such as computer technicians may lure customers away from their employers by offering to do jobs privately at a lesser cost. In doing so, they are competing directly with their employers, taking jobs that would have gone to the company.

What action can the Jamaican Fair Trading Commission (JFTC) take to deal with anti-competitive practices in the informal sector?

19. According to the JFTC, in its interpretation of the application of the law, it has jurisdiction to investigate and sanction all business persons operating in the Jamaican market, including vendors, and irrespective of legality of the business operations. The Jamaican Fair Competition Act (FCA) addresses the conduct of ‘enterprises, suppliers and persons’. There are standard exemptions, but these do not include the categories of businesses dealt with in this paper. The FCA does not provide a definition for ‘person’ or supplier, but Jamaica’s Interpretation Act defines “person” as including any corporation either aggregate or sole, any club, society, association or other body, of one or more persons. Businesses in the informal sector fall within this definition.

20. A decision was made by the Commissioners of the JFTC on this issue. A legal firm came under surveillance for offering an illegal DSS satellite service, and the question was raised as to whether the FTC has jurisdiction. The Commissioners directed that, as a matter of policy, a legitimate business offering an illegal service falls under the ambit of the FCA and should therefore be investigated (communication from the JFTC).

21. However, the FTC is limited to investigating conduct of firms as defined in the FCA, and while the process of compliance with regulations and paying of taxes increases considerably costs of operations of firms, thereby giving an unfair competitive advantage to those firms that do not comply, this does not fall within the scope of the FCA. In this regard, therefore, the FTC is limited to engaging in advocacy with other government agencies to encourage enforcement of the law.

22. In the process of investigations conducted by the FTC, in defining the relevant market, the illegal status of some firms has surfaced, and advocacy measures were taken with the relevant government departments. In addition, in investigations related to predatory pricing or any investigation that requires calculation of the cost price of a product, the FTC has, in the case of illegal firms, determined cost price by including the cost of paying all relevant government obligations, thereby increasing cost and more than likely rendering selling price as below cost.

23. Moreover, the FTC would only investigate a case if the conduct has substantial effect in the market. For that reason, price fixing and barriers to entry that are practiced in the subsistence sector, imposed by Dons, are unlikely to be investigated, even though the FTC has jurisdiction. Moreover, it is physically dangerous to challenge the Dons.

24. There are businesses established in the Kingston downtown area by recent migrants (from China and India in particular), which are medium-sized establishments that operate without regard to any regulations or tax laws, and that undersell similar establishments in the ‘uptown’ areas. They buy in bulk to achieve economies of scale, and the goods are split and shared. They compete with medium sized supermarkets and general department stores, offering similar goods at much lower prices. Vendors frequent these businesses to get supplies at much cheaper costs. This is unfair competition, but the FTC has not undertaken any investigations because conducts involving non-compliance with regulations are not covered by the FCA.
Market segmentation issues

25. This is a hazy area, because while there are some clearly segmented markets, some areas are greyer.

- In most respects, the subsistence sub-sector operating in the inner cities does not compete in the same market as medium and large businesses, because the market is segmented. Those selling within inner-cities target the inhabitants of those areas, catering specifically to their income level and needs\(^8\). Persons from “uptown”, that is, the middle and higher income consumers, would not shop for goods or services (e.g., beauty services) in the inner city communities for several reasons:
  - such locations may not be considered safe;
  - because most vendors are itinerant, selling products that are of questionable quality, and offer no guarantees, those who can afford it would choose to shop at establishments that are stable and offer guarantees on goods so that they could have recourse if a product is defective;
  - the point above is even more pronounced when food items and pharmaceuticals products are involved because of health issues associated with poor standards and expired products; persons of means would choose to go to the established businesses where there is greater assurance of good quality.

- However, in some specific lines of businesses, such as apparel and shoes sold by the Informal Commercial Importers (ICIs)\(^9\), there is direct competition with the small apparel businesses. In response, many of these businesses exit the “formal” market by not registering and paying taxes in order to cut cost and compete, or give up their premises and become itinerant traders, serving their customers by taking products to them or selling from home. Small businesses within the established sector are the ones most affected by the activities in the subsistence sub-sector of the informal sector, by being placed at a competitive disadvantage by similar businesses in the informal sector.

- Market segmentation is not so clear-cut in sectors such as supermarkets, whereby the shops operated by the Chinese and Indians in downtown Kingston draw a customer base from employees of the financial and legal industries, whose businesses have remained in that area, and who feel safer because of familiarity with the area (Other businesses moved out of downtown Kingston decades ago). Such consumers may frequent both uptown and downtown businesses. The FTC takes this into account in defining the market share of a firm under investigation.

26. The JFTC has not conducted any investigation specific to the informal sector. Nor has it conducted any studies in the area. It does plan, however, to do so in the near future.

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\(^8\) As such, persons from these communities may not be able to afford buying a five pound bag of flour from the supermarket, but could buy one or half a pound from the corner shop, or through credit from the shop.

\(^9\) Women who travel to the US and other destinations to buy supplies, evade customs duties and sell at lower cost, sometimes plying their trade in their cars.
Conclusions

27. There are already efforts undertaken by government to track down tax evaders and to clamp down on lax and corrupt practices in customs. This will accelerate the movement away from the informal sector into the formal sector. However, it is necessary for government to complement this crackdown on businesses with rigorous application of good governance practices. They must make greater effort at enforcing the law so as to reduce crime and protect businesses, freeing the monies that are currently paid to Dons for “protection” and/or are invested in security systems (guards, electronic systems, security cameras etc.). This money could then be used to pay government taxes.

28. The government now needs to simplify and streamline procedures for preparing and submitting tax returns, consider reducing the tax rate, so as to encourage compliance and spread the burden over a greater number of firms, and reform the bureaucracy to remove the bottlenecks encountered in the course of doing business.

29. The government should also embark on a programme of information dissemination and education targeting the lower income groups to highlight the benefits to be gained from government projects that can only be accessed by registered businesses. Productivity levels would rise, given the technical assistance that government agencies provide, but which is now not accessed by many informal businesses.

30. The FTC has the jurisdiction to investigate all businesses in Jamaica, however small, but can only intervene on the issue of non-compliance at the level of advocacy, and this they are doing. The FCA does not allow them to investigate “unfair” competition when cost advantages are gained though non-compliance with government regulations. They do, however, take this into account when calculating costs in predatory pricing cases.
CONTRIBUTION BY M. KHELIFA TOUNEKTI
POLITIQUE DE LA TUNISIE DANS LA LUTTE CONTRE LE COMMERCE INFORMEL

--M. Khelifa Tounekti--

PLAN

Introduction

I. Données sur le commerce parallèle en Tunisie
II. Objectifs de lutte contre le phénomène
III. Actions entreprises pour l’encadrement du secteur informel
IV. Rôle de la DGCEE en tant qu’autorité de la concurrence face à l’activité informelle
V. Conclusion
INTRODUCTION

• Le commerce informel est un phénomène mondial qui existe dans tous les pays et représente 15% à 20% du commerce international. Ce phénomène est amplifié par plusieurs facteurs dont :
  − la hausse des prix dans le secteur formel
  − l’augmentation du coût d’accès aux secteurs réglementés
  − la limitation des sources de financement
  − l’incapacité du marché du travail d’absorber les demandes croissantes de travail
  − l’ouverture du marché asiatique sur l’économie mondiale
  − la multiplicité des mesures de protection des économies locales (taxes, barrières …)
• Émergence du commerce parallèle en Tunisie durant la dernière décennie suite à la libéralisation du commerce extérieur et intérieur
• Le secteur informel est devenu une source d’inquiétude et d’appréhension pour les différents opérateurs économiques (producteurs, commerçants, artisans …)
• Distinction entre commerce parallèle et secteur informel

I. DONNÉES SUR LE SECTEUR INFORMEL EN TUNISIE

• 365 milles entreprises opérant dans le secteur informel dont :
  − 70 mille employant au moins six personnes
  − 295 mille non déclarées
  il contribue à :
  − 15 à 20% du produit intérieur brut
  − une valeur ajoutée estimée en 1997 à 5.541 millions de dinars (à l’exclusion du secteur agricole)
  − 423 mille emplois (85,4% d’hommes)
  − 21,6% des emplois (hors secteur agricole) se répartissent comme suit :
    • industrie et artisanat.......... 21,6%
    • commerce.......................... 45,5%
    • services.......................... 30%
II. OBJECTIFS DE LUTTE CONTRE LE SECTEUR INFORMEL

- Le phénomène est un problème structurel
- Contenir et limiter les effets négatifs du commerce informel à un degré n’affectant pas le tissu économique
- Protéger l’économie nationale contre les pratiques illégales (dumping, contrefaçon, importations anarchiques ...)
- Sauvegarder la santé et la sécurité du consommateur
- Assurer les équilibres économiques et sociaux

III. ACTIONS ENTREPRISES POUR L’ENCADREMENT DU SECTEUR INFORMEL

1. Renforcement du dispositif juridique et économique

- Suppression des autorisations et leurs remplacement par des cahiers des charges
- Facilitation de l’octroi des prêts destinés à l’exercice de l’activité économique (Banque de Solidarité)
- Promulgation de plusieurs lois consolidant le principe de la liberté de l’exercice des activités économiques et l’intégration dans le secteur formel :
  1.- Loi n°64 de 1991 relative à la concurrence et aux prix
- Interdiction de l’usage de moyens frauduleux lors des transactions (factures non conformes ou de complaisance...)
- Interdiction de la détention de produits ne relevant pas de l’activité professionnelle déclarée
  2. - Loi 91 – 44 relative au commerce de distribution
  3. – Loi 92 – 117 relative à la protection du consommateur
  4. - Loi n°86 de 1994 relative aux circuits de distribution des produits de l'agriculture et de la pêche
1. Renforcement du dispositif juridique et économique (suite)

5 - Loi n° 40 de 1998 relative aux techniques de vente et à la publicité commerciale :
   - interdiction des ventes hors des locaux du commerce
   - organisation des ventes à distance

6 - Loi n° 36 de 2001 relative à la protection des marques de fabrique, de commerce et de services (incrimination des pratiques de contrefaçon)

7 - Loi n° 9 de 1999 relative à la défense contre les pratiques déloyales à l’importation

8 - Mécanismes réglementaires de contrôle technique à l’importation de produits et marchandises

9 - Programme de mise à niveau des circuits de distribution

2. Renforcement des actions de contrôle économique

• Publication d’une circulaire en 2006 relative aux différentes actions de lutte contre le commerce informel et la contrefaçon, comprenant en particulier :
  – des mesures de lutte contre le flux de produits portant préjudice à la santé et à la sécurité du consommateur et au patrimoine nationale tel que le carburant et les produits de l’artisanat
  – instauration d’un système d’animation de contrôle mixte (douanes, police judiciaire, commerce, santé …)
  – lutte contre la contrefaçon
  – lutte contre l’expansion géographique et temporelle des marchés hebdomadaires
  – interdiction de l’implantation commerciale anarchique
2. Renforcement des actions de contrôle économique (suite)

- Restructuration des services de douanes et mise à niveau des ports et points frontaliers par le renforcement des ressources humaines et matérielles (scanner, formation, recrutement ...) et adoption du principe de la rotation des effectifs
- Mise en place d’un dispositif de communication et d’information sur les tendances spéculatives et d’importations anarchiques (observatoire, collecte d’informations sur les opérations de contrebandes et de fraudes, procédures de ciblage et d’inspection systématique)
- Formation de brigades mixtes « centrale et régionale » (police judiciaire, douanes, commerce) pour assurer le contrôle à posteriori
- Mise en place d’un outil de contrôle sectoriel piloté par les structures spécialisées (santé, industrie, finance, transport ...) visant les produits portant préjudice à la sécurité et à la santé du consommateur tels que les aliments, les produits cosmétiques, le carburant, les pièces de rechange usagées, les cigarettes

3. Amélioration des conditions de l’exercice du commerce

- Création d’espaces spécialisés pour les commerçants opérant dans le secteur informel
- Organisation des marchés hebdomadaires et fixation des règles et conditions de création et de fonctionnement de ces marchés
- Aide aux intervenants dans les circuits informels pour faciliter leur intégration dans le secteur organisé (campagne de sensibilisation...)
- Facilitation d’installation dans les espaces aménagés
- Mise en place d’un plan de modernisation des marchés municipaux (problèmes posés par le commerce anarchique sur la voie Publique)
- Instauration de commissions locales mixtes (commerce, intérieur) chargées du suivi de l’avancement des travaux dans ce domaine
4. Lutte contre l'expansion géographique et temporelle des marchés hebdomadaires
- Restreindre l'ouverture des marchés hebdomadaires à l'horaire légal (se limiter à un jour par semaine)
- Limiter l'espace des marchés hebdomadaires par des clôtures
- Renforcer et intensifier les campagnes de contrôle dans ces marchés

5. Lutte contre la contrefaçon et le piratage
- Réviser les textes qui protègent la propriété intellectuelle
- Incriminer les pratiques de contrefaçon
- Habiliter les agents de contrôle économique à constater et relever les infractions relatives aux pratiques de contrefaçon
- Traiter les plaintes des entreprises industrielles et commerciales
- Organiser des ateliers de formation au profit des agents de contrôle économiques en collaboration avec les détenteurs de marques victimes de la contrefaçon afin d'identifier les spécificités techniques des produits contrefaits
- Intensifier les campagnes de contrôle sur les produits contrefaits (saisie et destruction)
- Renforcer la coopération dans ce domaine
6. Information et sensibilisation des différents intervenants

- Mener des actions d’information et de sensibilisation, au profit du grand public, sur les effets néfastes des flux informels et leur impact sur le plan social (perte d’emploi...) en collaboration avec la profession et l’organisation de défense du consommateur
- Aider la profession à mieux apprécier les réglementations nationales et étrangères et mettre à leur disposition un support d’information favorisant son adhésion au plan gouvernemental de lutte contre les flux informels
- Participation aux foires spécialisées pour informer le public sur les dangers et risques éventuels que peuvent présenter certains produits issus de la contrefaçon ou de la piraterie pour la santé et la sécurité des consommateurs

7. Renforcer la coopération internationale

- Échange d’expériences avec les pays voisins en matière de lutte contre le commerce informel (stages de formation, séminaires...)
- Mise en place d’un groupe d’experts douaniers spécialisés en matière de contrôle et de lutte contre la fraude pour l’échange d’informations et l’initiation d’action commune de lutte contre la contrebande sous ses diverses formes
- Réduction des mesures de protection par la révision périodique de la tarification douanière selon les accords bilatéraux
IV. RÔLE DE LA DGCEE EN TANT QU’AUTORITÉ DE LA CONCURRENCE FACE À L’ACTIVITÉ INFORMELLE

1. L’autorité de la concurrence a plusieurs missions
   • Gérer la politique des prix
   • Surveiller le fonctionnement du marché
   • Contrôler la transparence des transactions
     \begin{itemize}
     \item pratiques illégales
     \item pratiques déloyales (soumises à contrôle)
     \end{itemize}

2. L’autorité doit assurer un environnement concurrentiel
   • Cadre juridique de plus en plus renforcé
   • Encadrement de l’activité par des dispositifs réglementaires diversifiés

IV. RÔLE DE L’AUTORITÉ DE CONCURRENCE FACE À L’ACTIVITÉ INFORMELLE

3. Renforcement de la concurrence légale et formelle
   • Libéralisation du commerce
     \begin{itemize}
     \item suppression des obstacles
     \item suppression des autorisations
     \item déprotection de l’économie (démantèlement tarifaire)
     \end{itemize}
   • Assurer l’augmentation de l’offre par la régulation et l’importation pour empêcher la spéculation informelle
   • Développement des dispositifs d’intégration du secteur informel dans le secteur formel :
     \begin{itemize}
     \item programme de mise à niveau
     \item octroi des subventions et crédits
     \item aménagement des zones et locaux
     \end{itemize}
IV. RÔLE DE L’ AUTORITÉ DE CONCURRENCE FACE À L’ ACTIVITÉ INFORMELLE

4. Soumettre le secteur à un contrôle :
   — contrôle classique de transparence
   — contrôle des sources d’approvisionnement
   — contrôle de la protection des consommateurs
   — contrôle des pratiques anticoncurrentielles

• Ententes éventuelles et obstacles à l’activité
• Ententes de spéculation ou de hausse des prix
• Aucune activité n’est à l’abri de la loi

CONCLUSION

• Phénomène complexe (économique, social)
• Responsabilité collective dans la lutte contre ce phénomène (profession, associations, médias, administration ...)
• Facteurs et origines multiples
• Nécessité d’un dispositif juridique
• Nécessité de renforcement d’un État de droit qui applique la réglementation dans tous les domaines (aménagement du territoire, municipalités...)

➢ Autorité de la concurrence pour contribuer à la politique d’encadrement de ce phénomène
ACTION CONCERTÉE INITIÉE PAR LES OPERATEURS D'UN SECTEUR INFORMEL

1. Dans le cadre de son plan de développement, la chaine de distribution Promogros, spécialisée dans la vente au détail des produits alimentaires a décidé de créer un point de vente dans la ville de Sfax : une grande agglomération économique située au sud du pays.

2. La direction de Promogros a obtenu des autorités compétentes toutes les autorisations nécessaires pour la construction et l’aménagement du local.

3. Au moment de l’achèvement des travaux et lorsque la Direction de la chaine concernée a commencé les préparatifs pour l’ouverture de son point de vente, les petits commerçants ont jugé que l’implantation d’une grande surface à Sfax serait de nature à compromettre leurs activités et à réduire leurs chiffres d’affaires.

4. Pour se défendre, ces commerçants ont introduit des requêtes auprès des autorités régionales pour exprimer leurs oppositions catégoriques à l’ouverture d’une grande surface.

5. Plusieurs raisons ont été évoquées pour argumenter leurs positions, tels que le non respect de la surface réglementaire ou les pratiques de prix bas pour les produits homologués et ont impliqué l’organisation professionnelle régionale dans cette démarche.

6. La direction de Promogros a essayé de répondre à tous les reproches pour éviter toute réaction qui puisse gêner les autorités de la région soumise à d’énormes pressions.

7. Les autorités régionales ont contacté le Ministère du Commerce et de l’Artisanat -autorité compétente sur le plan réglementaire- pour résoudre ce problème.

8. La DGCEE, en tant qu’autorité de concurrence, est intervenue au motif que le comportement des commerçants prouve l’opposition à l’implantation d’une grande surface et constitue un obstacle à l’accès d’un concurrent sérieux au marché de la distribution au détail et à la concurrence dans le secteur.

9. Considérant qu’une telle réaction est contraire à la réglementation d’autant plus que l’UTICA régional a parrainé les revendications des commerçants, la DGCEE a fait savoir aux représentants des commerçants que leur comportement constituait une pratique anticoncurrentielle au sens du droit de la concurrence et qu’une telle pratique pourrait être poursuivie et sanctionnée par le Conseil de la concurrence.

10. Compte tenu de cet avertissement les commerçants ont cessé leurs revendications et le magasin a ouvert ses portes sans aucun problème.
ENTENTES SUR LES PRIX DES VIANDES DANS UN SECTEUR INFORMEL

1. En 2007 et jusqu’au 1er Septembre 2008, les prix des aliments pour bétail ont considérablement augmenté. Avec le prolongement d’une période de sécheresse dans la région du sud de la Tunisie spécialisée dans l’élevage extensive, les éleveurs ne peuvent plus faire face à l’augmentation des frais d’entretien de leur cheptel, et ils se sont mis à s’en débarrasser à des prix très bas.

En conséquence, les boucheries ont profité de la situation et ont baissé leur prix de vente aux consommateurs et ce contrairement à d’autres régions du nord où les prix ont pu résister à la baisse en raison notamment de la fortes demande dans les grandes agglomérations.

2. Les boucheries installées dans les régions du sud ont constaté qu’ils sont en train de pratiquer des prix inférieurs aux prix moyens. Ils se sont entendus sous l’égide du bureau régional de l’UTICA (Union Tunisiennne de l’Industrie, du Commerce et de l’Artisanat) pour augmenter leur prix de 500 mil par Kg de viande rouge (agneau et chèvre) pour s’aligner sur les autres régions et rattraper le niveau antérieur des prix.

Constatant cette entente :

3. La Direction Régionale du Commerce a saisi la DGCEE qui a demandé à la Direction régionale du commerce de prouver l’existence d’une entente en cherchant des preuves éventuelles. Après enquête, il s’est avéré que l’UTICA régionale a organisé une réunion sur demande de ses boucheries en vue de consacrer cette augmentation et a consigné cette entente par un PV.

La DGCEE a demandé à l’UTICA régionale d’annuler cette entente par écrit et de revenir sur l’augmentation des prix. Faute de quoi, une ouverture d’enquête serait effectuée en vue de saisir le Conseil de la Concurrence.

L’UTICA a donné suite à la demande de la DGCEE et l’augmentation des prix a été annulée dans toutes les régions. Les autorités régionales ont salué ce geste et la vigilance de la DGCEE.
ANNEX 1 :
ACTION CONCERTÉE INITIÉE PAR LES OPERATEURS D’UN SECTEUR INFORMEL

Dans le cadre de son plan de développement, la chaine de distribution Promogros, spécialisée dans la vente au détail des produits alimentaires a décidé de créer un point de vente dans la ville de Sfax ; une grande agglomération économique située au sud du pays.

La direction de Promogros a obtenu des autorités compétentes toutes les autorisations nécessaires pour la construction et l’aménagement du local.

Au moment de l’achèvement des travaux et lorsque la Direction de la chaine concernée a commencé les préparatifs pour l’ouverture de son point de vente, les petits commerçants locaux ont jugé que l’implantation d’une grande surface à Sfax serait de nature à compromettre leurs activités et à réduire leurs chiffres d’affaires.

Pour se défendre, ces commerçants ont introduit des requêtes auprès des autorités régionales pour exprimer leur opposition catégorique à l’ouverture d’une grande surface.

Plusieurs raisons ont été évoquées pour argumenter leurs positions, telles que le non respect de la surface réglementaire ou les pratiques de prix bas pour les produits homologués. Par ailleurs, ils ont impliqué l’organisation professionnelle régionale dans cette démarche.

La direction de Promogros a essayé de répondre à toutes les reproches pour éviter toute réaction qui peut gêner les autorités de la région soumises à d’énormes pressions.

Les autorités régionales ont contacté le Ministère du Commerce et de l’Artisanat - autorité compétente sur le plan réglementaire - pour résoudre ce problème.

La DGCEE est intervenue en tant qu’autorité de concurrence, en sachant que le comportement des commerçants prouvait leur opposition à l’implantation d’une grande surface et constituait un obstacle à l’accès d’un concurrent sérieux au marché de la distribution au détail et à la concurrence dans le secteur.

Considérant qu’une telle réaction était contraire à la réglementation d’autant plus que l’UTICA régional avait parrainé les revendications des commerçants, la DGCEE a fait savoir aux représentants des commerçants que leur comportement constituait une pratique anticoncurrentielle au sens du droit de la concurrence et qu’une telle pratique pourrait être poursuivie et sanctionnée par le Conseil de la concurrence.

Compte tenu de cet avertissement, les commerçants ont cessé leurs revendications et le magasin a ouvert ses portes sans aucun problème.
ANNEX 2 : ENTENTES SUR LES PRIX DES VIANDES DANS LE SECTEUR INFORMEL

1. En 2007 et au 1er Septembre 2008, les prix des aliments pour bétail ont considérablement augmenté, conjointement avec le prolongement d’une période de sécheresse dans la région du sud de la Tunisie spécialisée dans l’élevage extensive. Les éleveurs ne pouvant plus faire face à l’augmentation des frais d’entretien de leur cheptel se sont mis à s’en débarrasser à des prix très bas.

En conséquence, les boucheries ont profité de la situation. Elles ont baissé leur prix de vente aux consommateurs, contrairement à d’autres régions du Nord où les prix ont pu résister à la baisse en raison notamment d’une forte demande de viande dans les grandes agglomérations.

2. Les boucheries installées dans les régions du sud ont constaté qu’elles étaient en trains de pratiquer des prix inférieurs aux prix moyens normaux. Elles se sont entendues sous l’égide du bureau régional de l’UTICA (Union Tunisienne de l’Industrie, du Commerce et de l’Artisanat) afin d’augmenter leurs prix de 500 mil par kg de viande rouge (agneau et chèvre), afin de s’aligner sur les prix pratiqués dans les autres régions et de rattraper le niveau antérieur des prix.

Constatant cette entente,

3. La Direction Régionale du Commerce a saisi la DGCEE qui lui a demandé en retour de prouver l’existence d’une entente par la recherche d’éventuelles preuves. Après investigation, il s’est avéré que l’UTICA régionale avait organisé une réunion à la demande des boucheries afin d’entériner cette augmentation des prix. Elle a donc sanctionné cette entente par un PV.

La DGCEE a ensuite demandé à l’UTICA régionale de mettre fin à cette entente par écrit et de revenir sur l’augmentation des prix, faute de quoi une ouverture d’enquête serait effectuée afin de saisir le Conseil de la Concurrence.

L’UTICA a donné suite à la demande de la DGCEE. L’augmentation des prix a été annulée dans toutes les régions. Les autorités régionales ont salué ce geste et la vigilance de la DGCEE.
PRESENTATION BY MS. RITA RAMALHO
Informality, Competition and Development: 
The Role of Business Regulatory Reform

Overview

• Informality comes at a cost for competition, and for development
  • Facilitation of formal entry is a natural counterpart to “traditional” competition policy – and plays a key role in inclusive growth

• Government policy efforts to simplify entry can make a difference
  • Growing evidence of impact, including on informality
  • Improved data sets make it possible to do better research and impact evaluation
Informality: A Constraint on Development

- Low income economies tend to be dominated by large incumbents, substantial informal sectors and relatively small formal SME sectors

- Compared with formal SMEs, informal firms:
  - Have more trouble accessing credit
  - Are less likely to contract with foreign-owned companies or to export
  - Grow more slowly and hire fewer people
  - Have workers without formal worker protections

Getting to Formal: Business Regulation Matters

Informal Sector (share of GDP)

Countries ranked by ease of doing business, quintiles
If the cost of starting a business is high, entrepreneurs delay registering...

... and formal firms face more competition from informal ones.
The Good News: Governments are Actively Reforming

- **Doing Business 2009** recorded 239 business regulation reforms in 113 countries in 2007/08
  - Eastern Europe and Central Asia – 62 reforms in 23 of the 25 countries, 25% of the total recorded worldwide.
  - Africa – 28 of 46 countries completing 58 reforms.

- Since **Doing Business** began, we have recorded nearly 1000 business regulation reforms.

The Most Popular Area for Reform: Business Start-Up

Percentage of Countries by Region which reformed in Starting a Business

- Europe & Central Asia: 9.2%
- High Income, OECD: 77%
- South Asia: 63%
- Middle East & North Africa: 58%
- Sub-Saharan Africa: 57%
- Latin America & Caribbean: 53%
- East Asia & Pacific: 50%
Getting to the Top: What the DB Top10 on Starting a Business Have in Common

1. New Zealand  
2. Canada  
3. Australia  
4. Georgia  
5. Ireland  
6. United States  
7. Mauritius  
8. United Kingdom  
9. Puerto Rico  
10. Singapore

- No or minimal minimum paid-in capital requirement
- Standardized forms
- No courts involved
- Fixed registration fee
- No publication in legal journal required
- 4 procedures, 5 days, start-up fees 1.5% GHFpc (on average)

What Happens When Governments Reform Business Start-up Regulation?

- **Firms take notice:**
  - E.g. Georgia: 55% increase in business registration – up to 15 formal firms per capita (equivalent to Malaysia, Singapore)

- **And broader benefits follow:**
  - Research findings: lower costs of entry associated with more entrepreneurship, less corruption, more employment opportunities, and a smaller informal sector
  - One example – Mexico: business registration up 5%, employment up 2.8%, prices down 1%
Building Datasets: Enterprise Surveys
www.enterprisesurveys.org/

Learning More About Informality: Building on the Enterprise Surveys

- New surveys underway in Africa, Nepal, targeting informal firms. Objectives are to:
  - Characterize informal businesses. Characteristics of the entrepreneurs, activity, use of capital and other assets, employment structure, seasonality
  - Explain differences in business performance when compared to formal counterparts
  - Assess the costs and benefits of formalization
  - Understand the industrial and spatial pattern of informal activity

- The challenge has been how to randomly select informal firms to survey. From a theoretical approach based on random walk ad hoc adjustments have been necessary to respond to the characteristics of each country

- Initial evidence is that response rates are very high (higher than in formal surveys).
Outline

• Working definition

• Classification arising out of working definition

• Informal sector and competition: peculiarities of the relationship

• Effects of informal Sector on competition
  ➢ Positive effects
  ➢ Negative effects
    o Dynamic effects
    o Static effects
Outline (2)

- Deciding to formalise: cost-benefit analysis
- Explanation for co-existence of formality and informality
- Facilitation of formalisation
  - Reasons for the existence of the informal sector
  - Formalisation by neutralising motives
- Conclusion

Informal Sector: Working Definition

- Defined in many ways
  - Size
    - Number of employees
    - Capital stock
  - Legality
  - Nature of functioning: informal norms versus rules

- Working Definition
  Economic activity in a nation which is not administered in any substantial way by the government
Classification Arising out of the Formal Definition

- Distribution and manufacture of banned products
- Illegal cross-border trading in products otherwise legal
- Unauthorised internal distribution of services /amenities otherwise legal
- Production of goods/services not administered by the government
- Hawking and vending activities

Informal Sector and Competition: Peculiarities

- Small size and undifferentiated products might imply closer approximation of perfect competition
- Such characteristics might not be seen in all sectors (vegetable selling versus restaurants)
- Lower surpluses: productivity enhancement through innovation/investment is less probable
- Competition law difficult/impossible to enforce in some informal sectors characterised by large numbers, small size, mobile nature of firms, lack of records, non-standard products
Impact of Informal Sector on Economy Wide Competition

• Positive Effects
  ➢ Physical proximity of sellers, small size, identical products

• Negative Effects
  ➢ Dynamic Effects
    o Lower surpluses: competition through innovation is impeded
  ➢ Static Effects
    o Smaller formal sector
    o Intra-informal sector anti-competitive activity
    o Unfair competition for the formal sector
    o Abuse of dominance held by formal sector firms over informal firms

The Decision to Formalise: Cost Benefit Analysis

• Aggregate algebraically all effects to arrive at net effect of informal sector on economy wide competition

• Negative effect can be used to justify formalisation: otherwise continuation of informality is advised

• Qualifying statements
  ➢ Aggregation might throw the baby out with the bath water: sector analyses are advisable
  ➢ Addition of other effects such as tax revenues foregone because of informality might be advisable
Co-existence of Formality and Informality: Explanation and Implications

- Initial differences in wealth
  - Less wealthy entrepreneurs cannot incur registration costs
  - They cannot pay the necessary bribes to gain entry

- Presence in other sectors might make the time costs needed to enter the formal sector more bearable (?)

- Equilibrium might be attained: unfair competitive advantage of informal firms might freeze the structure of a sector

Facilitation of Formalisation

Reasons for the Existence of the Informal Sector

- Too many procedures/ clearances required for setting up formal firms

- Time consuming nature of the above procedures

- Corruption at entry points to the formal sector

- Credit and other advantages provided to formal sector firms not large enough

- High tax rates in the formal sector
Facilitation of Formalisation

Formalisation by neutralising motives

- Lower the number of procedures – strategic approach directed towards areas of least resistance

- Lower time costs – single window or bunching of procedures

- Lower corruption
  - Increase salaries of government officials
  - Increase monitoring efforts/expenditure
  - Increase punishment and remove associated barriers
  - Tackle deeper causes through strategic approach

- Lower tax rates

Conclusions

- Informality has both positive and negative effects

- Formalisation needs to be preceded by a cost-benefit analysis

- Sector analysis is necessary – aggregation might lead to inappropriate decisions

- Initial wealth differences might lead to sectors with mixed presence – a self perpetuating phenomenon

- Formalisation requires a multi-pronged attack – deregulation, administrative restructuring and lubrication, campaign against corruption, more liberal tax regime etc