

Competition Law and Policy in the **Baltic Countries**



Centre for Co-operation with Non-Members

OECD

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FOREWORD

The Baltic countries of Estonia, Latvia and Lithuania have made significant progress in their transition to market economies since achieving independence in the early 1990s. An important part of the transition process has been the development of competition policy in the region. All three countries enacted competition laws in the early 1990s, and all three enacted new, “second generation” laws in 1998 and 1999. As a part of the Baltic Regional Programme of its Centre for Co-operation with Non-Members, the OECD has conducted reviews of competition policy in each country, and presents its findings in this publication.

This is the first comprehensive review ever conducted of competition policy in the Baltic States. The findings and recommendations were discussed at a five-day conference held in Riga, Latvia (May 1999), by competition policy officials from the Baltic states, the adjacent territories of Russia, and current or former competition officials from Germany, Sweden and the United States. The Review highlights the critical need for a comprehensive and stable legal framework enforced by a Competition Agency that is equipped with the necessary resources to ensure effective application of the laws.

This volume contains individual country reports together with a summary organised in the same manner as the reports themselves. Highlights and conclusions from the conference are presented in italic type in the relevant sections of the summary.

The primary author of the reports is John W. Clark, an OECD consultant (and former member of the OECD Secretariat) whose positions in the Antitrust Division of the United States Department of Justice included that of Acting Assistant Attorney-General. The opinions expressed in this report do not necessarily represent those of the OECD, its Member countries or the Baltic countries.

This book is published on the responsibility of the Secretary-General of the OECD.

Eric Burgeat
Director
Centre for Co-operation with Non-Members

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COMPETITION POLICY IN THE BALTICS -- A PROGRESS REPORT

by
*John Clark**

Estonia, Latvia and Lithuania have made significant progress toward achieving fully functioning market economies since regaining independence in 1991. An important part of this process has been the development of an effective competition policy. All three countries have competition laws and a competition agency actively enforcing them. All three are entering a critical second phase in competition enforcement, having enacted new competition laws recently, and each is undertaking the difficult steps that will lead, it is hoped, to full economic integration with Europe. This is an appropriate time for a review of competition policy in the Baltic states, for an assessment of how competition enforcement has developed in the region and for articulating approaches to a more effective competition policy in the future.

While Estonia, Latvia and Lithuania are of course quite different in many respects, their economies share many common traits. They are comparable in size, within the scale of national economies worldwide, and being geographically proximate to one another they are subject to similar economic influences. They have shared the same economic history in the last half of the 20th century, having been part of the Soviet Union for most of that time and having begun the transition to a market economy together at the beginning of the 1990s. Thus, it is not surprising that competition policy in the three countries has evolved in roughly parallel fashion. The three country reports reflect those common elements; several of the comments and recommendations in the reports apply equally to all three countries. In other respects there are differences, of course, and those are discussed as well.

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1. Laws

Latvia first enacted a competition law in 1991, followed by Lithuania in 1992 and Estonia in 1993. These three laws were generally comparable in their substantive provisions. Each proscribed abuses of dominance and anticompetitive restrictive agreements, and the statutory definitions of such conduct were similar. The laws of Latvia and Lithuania also provided for merger control, but Estonia's did not. The three laws also proscribed certain types of anticompetitive conduct by executive bodies of government, a provision that is found in the competition laws of several transition countries and that is mostly unique to them. The laws also contained provisions proscribing acts of unfair competition in terms that were roughly comparable.

All three countries enacted new competition laws in 1998 and 1999. Latvia's new law became effective on 1 January 1998, Estonia's on 1 October 1998 and Lithuania's on 2 April 1999. One notable feature common to the new laws is the approximation of the substantive provisions of the laws to the competition law of the European Union, as required by the Europe Agreements between the EU and each of the three Baltic countries. The relevant provisions of the new laws closely resemble Articles 85 and 86 of the EC Treaty. In addition, the new laws spell out in greater detail the administrative procedures for the conduct of investigations and cases by the competition agency. These differ in several respects across the three countries, however, reflecting the different national legal systems and traditions in each country.

In any case, the fact that all three countries are currently in the process of implementing completely new competition laws means that each is substantially in a state of flux, as the competition agency adjusts to the substantive and procedural changes of their new laws. The agencies are presented with significant challenges in making the transition quickly and effectively, but the new laws also provide opportunities for bringing about real improvement in the effectiveness and efficiency of competition enforcement in the three countries.

2. The Competition Agencies

In both Lithuania and Latvia the competition agency is a five-member Competition Council, whose members are appointed by the Government for terms of five years (Latvia) or six (Lithuania, except that the Chairman serves for five years). In Estonia the competition law is enforced by a Competition Board headed by a Director General.

In Lithuania the formation of the Office of the Competition Council under the new law was still underway at the time of the writing of the report. Formerly, the prosecutorial functions were conducted by the State Competition and Consumer Protection Office, which was divided into seven divisions, each with different enforcement responsibilities. The Lithuanian Competition Council, unlike the competition agencies in the other two countries, also has enforcement responsibility for consumer protection, monitoring state aids, and antidumping. In Latvia, a Competition Bureau within the Competition Council has the functions of investigator and prosecutor. The Bureau is further subdivided into five divisions or offices. In Estonia, investigations and prosecutions are conducted by four departments within the Competition Board.

The Lithuanian Competition Council is the largest of the three competition agencies, having a total of approximately 50 people at the end of 1998. Its larger size reflects the additional areas of responsibility, noted above, that have been assigned to it. The Estonian Competition Board employed a total of 38 people at year-end 1998, although it is expected that there will be an increase to 47 in 1999, and the Latvian Competition Council had 30 employees as of mid-1998.

3. Substantive Competition Enforcement

3.1 *Abuse of a Dominant Position*

The abuse of dominance provisions of the laws of all three countries are similar, but not identical, and they resemble Article 86 of the EC Treaty. Each contains a general definition of dominance, which includes in some fashion the ability unilaterally to operate independently of one's competitors in a market or to exercise decisive influence in a market. Each provides that a market share of 40 per cent is at least a threshold in the determination of dominance. In Latvia a 40 per cent market share is a necessary but not sufficient condition for dominance. In Lithuania such a market share establishes a rebuttable presumption of dominance, while in Estonia, the law seems to say that an enterprise with such a market share is conclusively presumed to be dominant. In addition to prohibiting generally the abuse of a dominant position, the laws also specify certain types of conduct that can constitute an abuse, in a manner similar to Article 86 of the EC Treaty.

In all three countries abuse of dominance cases have been relatively numerous. Many such cases arise in markets characterised by natural monopoly or an essential facility. Most of the cases have been resolved by the issuance of remedial orders by the competition agency. Structural remedies generally have

not been pursued. There has not been an instance in any of the three countries where the breakup of a dominant firm has been attempted.

The comments in the reports note the importance of abuse of dominance cases in transition countries, but also that such cases are difficult to prosecute successfully. It is recommended that the competition agencies increase their reliance on structural remedies, though not necessarily on breaking up enterprises, which is very difficult, but on eliminating unnecessary barriers to entry in the relevant markets. The reports also recommend that the competition agencies focus on “exclusionary conduct” by dominant firms – conduct that excludes actual or potential rivals from competing in the relevant market – rather than “exploitative conduct,” such as monopolistic pricing or improperly restricting output. The latter can be ambiguous; it is difficult both to identify truly anticompetitive conduct of that sort and to fashion an effective remedy against it.

In other comments, the apparently conclusive presumption of dominance that a 40 per cent market share confers in Estonia is noted as a possible problem. High market shares do not always indicate dominance, particularly if entry into the relevant market is easy. The Estonia report also notes some unique provisions in that law that apply specifically to natural or government-created monopolies. These provisions provide the Competition Board with special powers to deal with anticompetitive conduct by such firms.

3.1.1 Discussion

Abuse of dominance cases continue to be the most numerous of all types of cases encountered by the participating competition agencies, and the majority of these matters involve situations of “natural monopoly” in network infrastructure industries, including electricity, telecommunications, heat supply and railroads. Regulatory systems in these industries are not fully established in the participating countries, and it often falls to the competition agency to correct actual or perceived abuses by the monopolist.

In abuse of dominance cases not involving network infrastructure industries, market definition is often critical to the analysis. A central issue in defining markets in these cases is the extent to which imported products are actual or potential substitutes for those produced domestically. The participating competition agencies are becoming increasingly sophisticated in the use of information from third parties – customers, suppliers and competitors – in the market definition analysis.

The most common types of conduct that are considered in abuse cases are discrimination in some form against certain classes of customers and monopolistic pricing. Often in times of sharply rising prices there is public pressure on the competition agency to control the increases in some fashion. The agencies resist this pressure to the extent possible, as it is exceptionally difficult for the agency to identify a “correct” price. One method employed with some success by the participating agencies has been to use a “yardstick,” whereby prices in other markets are compared to the market under examination.

3.2 Restrictive Agreements

These provisions of the three competition laws are modeled on Article 85 of the EC Treaty. Each contains a general prohibition of agreements that have the effect of “the prevention, restriction or distortion of competition,” and an enumeration of certain types of agreements that can have such an effect. The new laws all provide for the notification and exemption of restrictive agreements, again paralleling the procedures of the European Commission. The three countries are at various stages in implementing the exemption procedures. All are drafting regulations on the subject. Latvia appears to be the farthest along in that regard. In Lithuania, the Article on restrictive agreements does not become effective until the year 2000. Until then, the 1992 law continues to apply to horizontal agreements, and vertical agreements are considered to be lawful.

The three agencies have initiated relatively few cases under their restrictive agreement provisions, and even fewer have involved cartel conduct, such as price fixing or market allocation, which is considered by most experts to be the most unambiguously harmful of all types of anticompetitive conduct. Lithuania has perhaps been the most aggressive in recent years in prosecuting cartels. The experience of these countries is similar to that in most transition countries. Cartel agreements are difficult to identify and prosecute, in that they are usually conducted in secret. The reports strongly recommend, however, that the agencies give high priority to expanding their activities in this area. The recommendations contain specific steps for improving the agencies’ record in detection and prosecution of cartels.

The reports note that it is important that the agencies complete the process of promulgating block exemptions under their laws, and that they establish regulations for the notification of agreements and granting of individual exemptions that create minimal burdens for both the business community and the agencies themselves. The EC experience has shown that the

competition agency is not equipped to deal with large numbers of applications for exemptions.

3.2.1 Discussion

The participants agreed that they are having difficulty investigating possible cartel agreements and in acquiring good evidence of their existence. In the few successful cartel cases prosecuted to date, the best evidence of the agreement came from contemporaneously written documents found in the files of the cartel members. An effective way of discovering such documents has been to examine business files on the premises of suspected cartel operators during visits to their offices (the visits may be unannounced or prearranged).

The new laws of Lithuania and Latvia permit the competition agency to offer incentives for co-operation in the investigation by cartel participants, through immunity from prosecution or reduced fines. It was noted that the use of such incentives is increasing in OECD countries, with significant success, and the participants agreed that such tools would be useful in prosecuting cartels in their countries. Estonia currently does not have the necessary flexibility in its sanctioning powers, but is moving to amend its law to permit it.

3.3 Mergers

Latvia and Lithuania have merger control laws that include premerger notification. The substantive standard in Latvia's law is "prevent, restrict or distort competition," while the standard in Lithuania is "create or strengthen a dominant position and result in a substantial restriction of competition in a relevant market." Neither agency has blocked or caused to be modified many mergers to date, although Lithuania has been the more active of the two. Estonia does not currently have merger control, but its new law has instituted a merger notification requirement. It is anticipated that a merger control provision will be added to Estonia's law in the near future. In the absence of a specific prohibition of anticompetitive mergers in Estonia, it would seem that the abuse of dominance and restrictive agreement provisions of that law could be applied against anticompetitive mergers in appropriate circumstances. No such cases have arisen to date, however.

The reports emphasize the importance of setting merger notification thresholds at a relatively high level, high enough to catch only relatively large transactions and thereby minimising the burden of compliance on merging parties and the burden on the competition agency of having to review an unnecessarily large number of notifications. The thresholds set by the three

laws appear to be at reasonable levels, but the report recommends that there be periodic review of the thresholds and adjustment as necessary.

The Estonia report notes that the turnover threshold in Estonia's law appears to include worldwide turnover of the merging parties, not just turnover in Estonia. That threshold may catch many mergers that are not significant in Estonian markets, and it is recommended that consideration be given to modifying the law to include only turnover in Estonia. Also, Latvia's notification requirements include a criterion that one of the merging parties be dominant in a relevant market. The report recommends consideration of elimination of that criterion, for two reasons. First, determination of dominance is a difficult and relatively subjective exercise; objective criteria, such as amount of turnover or total assets, are more easily administered in a merger notification regime. Second, mergers of enterprises that are not dominant can be competitively harmful, as well as those involving firms that are already dominant.

With regard to substantive merger enforcement, the reports note that the great majority of mergers are not competitively harmful, and that most competition agencies oppose only a very small proportion of the mergers that they evaluate. The reports stress that the competition agencies in the three countries should evaluate the mergers that are presented to them according to current market conditions, especially taking into account actual or potential competition from sources outside the country.

3.3.1 Discussion

In the few merger cases that have occurred in the participating Baltic countries, market definition has often been the determining issue. Cases often turn on the decision on whether to include foreign sources of supply in the relevant geographic market. The participants also agreed that the issue of entry barriers, including barriers to expansion by small firms currently in the relevant market, has been important.

Merger cases can be politically sensitive. The competition agency may be subject to considerable pressure to approve a merger that appears to be competitively harmful. In some cases the agency has approved such a merger subject to a remedial order that imposes certain behavioural obligations on the merged entity, such as reporting price increases or eliminating an apparently discriminatory pricing structure. It was pointed out that such behavioural remedies are generally less satisfactory than structural remedies, and more difficult to administer. Satisfactory structural remedies are not limited to outright prohibition of the merger, however. Partial divestitures of assets, such

as rights to the use of a brand name, often are sufficient to cure the anticompetitive aspects of a merger while permitting the underlying transaction to be consummated.

A vexing problem for the participants in merger control has been dealing with and understanding the sometimes complex corporate structures of merging parties. Affiliations with offshore companies, for example, are not always fully disclosed in merger notifications. It was agreed that each agency must work on regulations in the near future that will ensure greater accuracy and transparency in merger notifications. This subject appears to be a particularly fruitful one for future co-operation among competition agencies in the Baltic region, permitting them to share their knowledge and experience in this technical area.

3.4 *Anticompetitive Activities of State and Local Governments*

The laws of all three countries contain provisions obligating executive bodies of government to, in some fashion, refrain from acts that restrict competition or unfairly discriminate against economic entities. Such provisions are common in the competition laws of transition countries, as they strive to remove the lingering effects of central planning. The laws of Estonia and Lithuania are somewhat stronger than Latvia's in this regard, apparently permitting the competition agency to institute binding enforcement actions against such conduct. The Latvian Competition Council apparently has such powers only with respect to activities by government bodies as entrepreneurs.

Estonia has been quite active in enforcing these provisions of its law, Lithuania and Latvia somewhat less so. In all three countries, however, the resolution of such matters has proceeded almost entirely on the basis of voluntary negotiations between the competition agency and the government body. This is not surprising; all governments seek to avoid direct confrontation between constituent bodies.

The reports stress that unnecessary restraints on competition by government bodies can impose substantial harm upon consumers, and the competition agency should be active in pursuing the elimination of such restraints. Political realities will require the agencies to work co-operatively with the other parts of their governments toward this end, but the explicit provisions of their laws relating to such conduct give the agencies considerable leverage in their negotiations. The reports recommend that the competition agencies enlist the business community as an ally in this effort, and that the public be informed of successes in eliminating such restraints.

3.4.1 Discussion

Of the four Baltic countries participating in the conference, Russia has by far the most experience in cases against competitive restraints by bodies of government. It continues to file many cases against local and regional government bodies under Articles 7 and 8 of its competition law. In the other three Baltic states the number of such cases seems to be declining, and as noted in the reports, they are almost always resolved with the relevant government bodies co-operatively rather than through formal proceedings. These types of cases most often involve discrimination in some form by the government, either in favor of a government owned or controlled entity against private firms, or in favor of local enterprises against those from outside the region. In all four participating countries, an important tool against such abuses is an active public relations campaign by the competition agency. Also, in Estonia, Latvia and Lithuania new restraints on such conduct by governments are the limits on state aids, imposed as a result of the Europe Agreements between these countries and the EU.

3.5 Unfair Competition

The competition laws of all three countries proscribe acts of “unfair competition,” which under each of the laws includes misappropriation or misuse of intellectual property, such as trademarks or commercial secrets, and dissemination of false or misleading information about a competitor or another entity. The three competition agencies have all instituted several proceedings involving unfair competition in the past several years. In Latvia and Estonia, unfair competition cases and investigations were the most numerous of any type in that period. In Lithuania the number of unfair competition cases has been declining in recent years.

The reports note that the protection of intellectual property and prohibitions of improper disparagement of a competitor are important to the proper functioning of markets. The three agencies have properly focused attention on such violations in their early years of competition enforcement. It is likely, however, that the number of such cases will decline over time, as businesses learn what they are permitted to do under the law, and also because businesses tend to resolve such disputes directly, through private litigation or other means of enforcement. Lithuania’s competition law explicitly provides for the enforcement of the unfair competition provisions by private parties through suits in court. The reports urge the agencies to encourage such private resolution of acts of unfair competition, to permit the agencies to concentrate their limited resources on other types of anticompetitive conduct.

3.5.1 *Discussion*

This topic was not discussed at the conference.

3.6 **Competition Advocacy**

Each of the three competition laws explicitly creates the role of competition advocate for the competition agency. The laws authorise the agencies to submit opinions on draft legislation and other legal acts by the government. In Estonia the new law provides the Competition Board with special powers relating to natural monopolies and entities with government-created exclusive rights, as noted above in the discussion of abuse of dominance. The agencies have exercised these powers to some extent in recent years, Lithuania having been perhaps the most active in this regard. All have participated in some fashion in the privatisation of some of the network infrastructure industries in their countries, most notably in the telecommunications sector.

It cannot be said that any of the three agencies has achieved consistent and significant success as competition advocates. Their recommendations have not always been heeded. This is perhaps to be expected in any country where competition enforcement is relatively new and the competition agency is not well known. Moreover, competition advocacy is difficult. It requires the competition agency to gain expertise not only in competition policy but also in other complex areas, such as regulation of natural monopolies. The reports nevertheless recommend that the three agencies place growing emphasis on this aspect of their work. The benefits to consumers from the incorporation of sound principles of competition policy in the legislative and regulatory activities of government can be substantial, sometimes significantly outweighing the benefits from successful case prosecutions.

3.6.1 *Discussion*

Much of competition advocacy is simply education. A fledgling competition agency, enforcing a new competition law, is often at a disadvantage in dealing with powerful government ministries or regulatory bodies. One way of overcoming this imbalance is to “systematize” competition advocacy, that is, to create permanent working groups or commissions on which the competition agency is represented and that meet regularly to review government policy within an activity. Such a system ensures the regular participation of the competition agency in the formation of national economic policy. Also, as in most of the activities of the competition agency, public relations is an important part of effective competition advocacy.

4. Institutional Issues

4.1 Independence of the Competition Agency Within Government

The decisions of a competition agency can affect powerful business and economic interests, which may have considerable influence in the government. For this reason it is generally believed that the competition agency should have as much independence from the rest of the government as possible, so it can reach its decisions solely on the merits, without reference to politics.

The new competition laws of the three Baltic countries do afford their competition agencies some measure of independence. The structure of the Latvian and Lithuanian competition agencies are similar in this regard. As noted above, both are composed of five member commissions, whose members are appointed by either the government (Latvia) or the President (Lithuania) and serve for relatively long terms, which enhances the independence of the commissioners. The Lithuanian law limits the conditions under which a Council member can be removed from office to criminal misconduct or the equivalence of dereliction of duty. The Latvian law does not set forth explicit limits on removal of Council members, but a separate provision of the law forbids other ministries of government from issuing instructions to the Competition Council regarding investigations or decisions.

The structure of the Estonian Competition Board is somewhat different. The Board is an executive agency, headed by one person, nominally within the Ministry of Finance. Pursuant to a separate statute, however, the Board assumes a more autonomous role, and is considered to be independent in its decisions.

The legal and structural aspects of the formation of a competition agency, however, are only a part of the necessary conditions for independence, and perhaps the lesser part. At least equally important is the development of *de facto*, or informal independence within the government. The agency must actually be confident that it is free to decide its cases without political interference. This type of independence is created only over time, as government, business and the public develop an understanding of and appreciation for a strong and impartial competition policy.

4.1.1 Discussion

“De facto” independence is indeed more important than “de jure” independence, and the competition agencies in all participating countries are still struggling to achieve a measure of it. Too often in highly visible or

politically sensitive cases a political official freely picks up the telephone to inquire of the agency the status of the matter, or worse, to make suggestions about the outcome. Direct orders from the government are seldom, if ever, made, but outside influences may be felt indirectly. Two suggestions for minimising such influence were made: establish formal procedures for contacts with the competition agency; and conduct business with other parts of government in the “sunshine” as much as possible. These procedures would help to ensure against the exercise of influence which, if publicly known, would be considered improper.

4.2 Investigative Powers

The three competition agencies each appear to have adequate powers to conduct investigations and obtain information under their new laws. They can require the subjects of an investigation and third parties to provide written answers to questions, to submit documents from their files and to submit to oral interviews. They can conduct unannounced visits to the premises of investigation subjects (sometimes called “dawn raids”) and take away documents that are discovered there. (The Lithuanian law requires that a court order be obtained before such a visit. In Estonia the Director or Deputy Director must approve such a visit.) All of the laws require that the agency protect the confidentiality of information that it acquires during an investigation.

The agencies have used their powers to compel the production of information sparingly to date. Most of the information that they have acquired has been produced voluntarily. The reports note that it is likely that the agencies’ use of compulsory process will grow in the future. Businesses that are the subjects of investigations are likely to become less co-operative with the agencies, particularly in cartel investigations, as they learn that the consequences of a finding of a violation of the competition law could be severe.

The reports stress that the competition agencies should use their compulsory information gathering powers judiciously. Excessively broad or burdensome information requests should be avoided. The agencies should perfect techniques of acquiring and analysing business documents, which can be the most revealing and informative type of evidence in a competition investigation. Finally, the agencies should be prepared to prosecute vigorously any attempts by recipients of information requests to conceal or destroy evidence or to provide false information.

4.2.1 Discussion

Competition investigations in the participating Baltic countries are not as “adversarial” as they are in some OECD countries, that is, the subjects of the investigations tend to co-operate with the competition agency more readily, whether because of ignorance of the competition law or because they do not fear the consequences of having been found to violate it. In many cases the most important evidence, including that which establishes liability, has been provided voluntarily by the subject enterprise or enterprises.

If the competition agency aggressively enforces the law over time, however, this situation is bound to change. As co-operation by investigation subjects lessens, the agency must come to rely more on independent sources of information. Essentially there are two such sources: third parties – customers, suppliers and competitors of the investigative subjects, and contemporaneously created documents from the files of the investigative subjects and third parties. The Baltic competition agencies have the tools to acquire such evidence, but are not yet experienced in doing so. At the same time, the agencies wish to be able to temper their evidence gathering activities, especially to avoid acquiring large numbers of documents, which with their limited resources they could not process.

The subject of co-operation among the competition agencies of the participating Baltic countries was discussed. In 1996 the competition authorities of Lithuania, Latvia and Estonia signed a Memorandum of Understanding that provides that the parties will co-operate by: exchanging information on their national legislation and regulations relating to competition enforcement and on regulation of monopolies; notifying another party of its activities that affect an economic entity in the other party’s country and by exchanging information relating to such activities when permitted by national law; maintaining the confidentiality of all such information that is provided; and jointly conducting seminars, conferences and other public functions relating to competition enforcement in the region.

To date there has been little active co-operation pursuant to the MOU, however. The principal reason for the lack of joint activity in enforcement matters has been the strict laws of all three countries prohibiting the disclosure of confidential information to foreign parties (similar laws exist in OECD countries). It was suggested that examples exist within OECD countries of new legislation that permits the exchange of confidential information between national competition agencies where there is reciprocity regarding the strict protection of such information against unauthorised use or disclosure. It was agreed that absent such legislation, there could be increased co-operation within the region on procedural matters.

4.3 *Enforcement and Sanctioning Powers*

The laws of all three countries authorise the competition agency to issue remedial orders in its cases, forbidding specified conduct and, if necessary, requiring affirmative action to restore competition to the affected market. All three agencies have issued such orders in past cases, although many other cases were resolved simply by voluntary abandonment of unlawful conduct by the offending party. The reports note that drafting remedial orders that are both effective and easily administered is difficult. The reports suggest that the agencies undertake a review of past orders, resources permitting, to assess their effectiveness. In some cases, orders that are no longer necessary or that are causing unintended, anticompetitive effects should be terminated or modified.

A potential problem regarding remedial orders exists in the Latvian law. Certain provisions of the new law seem to require the Competition Council first to attempt a voluntary resolution to a violation before imposing a remedial order, and these provisions appear to foreclose the ability of the Council to issue a remedial order if the violation has been terminated and the status quo restored. The report notes that the requirement for preliminary negotiations in every case could result in substantial delays in reaching a final result. Also, in some cases a remedial order may be indicated even where the violation is no longer ongoing, if only to prevent its recurrence. There has been little experience with these provisions to date, however, and it may be possible to avoid these problems in the administration of the new law.

The new laws provide the agencies with the power to impose significant fines for violations of the law. Lithuania can impose fines of up to LTL 100 000 for substantive violations of the law, except that fines of up to ten per cent of an entity's gross annual income may be imposed for infringements "made in aggravating circumstances." Estonia and Latvia can fine up to five per cent of total annual turnover for most substantive violations (Latvia can fine up to ten per cent for certain types of cartel conduct). Other fines may be imposed for failures to supply requested information, failures to file required merger notifications and failures to observe agency orders. Fines can be imposed against both legal and natural persons. The laws of Lithuania and Latvia include useful provisions setting forth factors to be considered in assessing fines within the permissible ranges. The factors include the seriousness of the violation and the magnitude of the harm, the role of the offender in the violation and the extent of co-operation, if any, by the offender with the agency's investigation.

The reports conclude generally that the agencies' powers to fine appear to be adequate, although it is noted in the Lithuanian report that the

maximum fine of LTL 100 000 (currently about US\$25 000) would not be sufficient in many cases involving cartel conduct. The Lithuanian law authorises a higher fine of ten per cent of an entity's gross annual income in "aggravating circumstances." The report recommends that the Competition Council consider all conduct that is plainly cartel conduct as "aggravating." Otherwise, the report recommends that the Council periodically review the adequacy of the LTL100 000 maximum for other violations and seek changes in the law where indicated.

The reports note that the three agencies have not used their fining powers extensively, especially in cases involving cartel conduct. The reports recommend that the agencies impose increasingly large fines for cartel conduct, and also that the agencies' discretionary powers to ameliorate fines be employed as a tool to gain co-operation in cartel investigations.

The Estonian and Lithuanian competition laws provide for the ability of private parties to recover money damages that resulted from violations of the law. The Latvian law does not explicitly provide for such private recovery, though it may be possible through the country's civil code. There have been almost no such cases in any of the three countries, however. Private damage actions can be an important supplement to government enforcement of the competition law, and the reports recommend that the agencies work with the business and legal communities to foster such suits in appropriate circumstances.

4.3.1 Discussion

This topic was not separately discussed at the conference, but related issues were brought up often and are reflected elsewhere in the summaries.

4.4 Administrative Procedures and Appeals

Each of the three new laws establishes more open and detailed procedures for the handling of investigations and proceedings by the competition agency. The laws permit the agencies to initiate investigations *ex officio* or upon receiving complaints or petitions from private parties or other government agencies. In each country private parties have rights to participate formally in agency proceedings. The agencies are required to respond to all petitions or complaints within a specified period of time. The agencies have the right to reject a petition if they conclude that they do not state a potential violation. The agencies must conduct formal proceedings before reaching a conclusion that a violation has occurred. The proceeding must be public,

subject to necessary restrictions on the disclosure of confidential information. Private parties, including petitioners and third parties with an appropriate interest in the case, can participate in the hearings and offer evidence. The laws impose time limits for the completion of hearings and the issuance of decisions.

On the whole, the new openness and opportunity for private parties to participate in agency hearings are welcome developments. Transparency and accessibility to the work of the competition agency are important factors in building public support for competition enforcement. There are some tradeoffs, however. Agency procedures could become too cumbersome and slow. The unconstrained participation of private parties in agency hearings could lengthen the proceedings unnecessarily and impinge on the agency's enforcement discretion. The reports recommend that the agencies adopt procedures for handling petitions and for the participation of private parties in their proceedings that are rigorous but fair, consistent with the requirements of the law, to ensure against excessive demands on the agency's resources.

The three laws provide that appeals of final decisions of the competition agencies may be made to the courts. In Lithuania and Estonia, a few cases have been appealed each year. The agencies have a fairly good record on appeal, having more decisions upheld than reversed. Only a few cases in Latvia have been appealed to the courts.

The reports note that as the agencies become more active and prosecute more cases it can be expected that more of their decisions will be challenged in court. It is important that the agencies develop a record of success in court, which would contribute to their ability to negotiate and enforce effective administrative decisions. Thus, the agencies must give high priority to litigation of their cases, even if they are relatively few in number. The reports recommend that as a part of this effort the agencies develop good relationships with the courts that hear competition cases. This includes providing seminars or other opportunities for judges to become familiar with principles of competition analysis.

4.4.1 Discussion

The participants shared their experiences to date under their new laws. They seem to be managing well under their new administrative procedures. Most cases to date have been developed ex officio, and not through the formal complaint procedures. The agencies appear to have sufficient discretion to reject complaints that are insignificant or not sufficiently related to a possible violation of the law, although to date there have been no appeals to the courts of such rejections.

The participants foresee significant problems relating to litigation, however. The judges in their countries are almost wholly unfamiliar with competition analysis. Some judges are prone to concentrate on procedural issues rather than substantive ones, and may reverse an agency decision on a relatively minor procedural error. In particular, proving agreements in cartel cases is becoming a problem. Direct evidence of the agreement, which is difficult to obtain, is usually required (this is true in OECD countries as well, however, which points up the need for greater skill and aggressiveness in gathering such evidence). Finally, the shortage of qualified lawyers, noted in the reports, is becoming critical.

The possibility of employing precedent from EU competition cases in court cases in the Baltic states was discussed. Courts may be required to consider such cases under Article 63 of the Europe Agreements, but that Article applies only in situations in which the relevant conduct affects trade between the EU and the signing country. In any case, language problems may inhibit the widespread use of foreign precedent by local courts.

It was agreed that the competition agencies should begin to work with their local courts to build awareness of the competition law and of the principles of competition analysis.

4.5 *Public Relations – Developing a Competition Culture*

An indispensable element of a successful national competition policy is the development of an understanding of and support for competition enforcement within other parts of government and the public – a “competition culture.” This is an ongoing process that requires the constant attention of the competition agency. The reports list several steps that the agencies can take to enhance the competition culture in their countries. They include publishing the agency’s decisions, an annual report and regulations or guidelines explaining the agency’s analytical processes for the public; public appearances and speeches by senior competition officials; seminars on competition policy for the business and legal communities; a World Wide Web site; and cultivating relations with the press.

Each of the three agencies has made efforts in this regard. Lithuania has published informative annual reports for several years, and it maintains a Web site. Its officials regularly make public appearances, as do those from Estonia and Latvia. Estonia has published an informative brochure describing the Competition Board and it too has a Web site. It intends to begin publishing an annual report. Latvia has published informative regulations implementing

several provisions of its law. It is clear that more can be done in each country, however, within the limited resources available.

4.5.1 Discussion

This topic was not separately discussed in the conference, but it arose in some fashion in discussion of almost every other topic. It was agreed that an aggressive and proactive public relations programme is an indispensable element of a successful national competition policy.

4.6 Resources

Resources are a critical issue for the three agencies, as they work to implement their new laws. The staffs are hard working and dedicated, but they face important challenges in the near term. Each office has a problem with employee turnover – retaining good professionals in the agency. Latvia in particular has seen almost a complete turnover in the past two years. The problem is somewhat less acute in Lithuania and Estonia. Part of the problem in each country is disparity in pay between positions in the competition agency and positions elsewhere in the public and private sectors. No government can expect to provide full income comparability with the private sector for its employees, but there should be equality in pay within government for employees with comparable skills. It appears that some positions in these three competition offices are paid at a lower rate than comparable positions in other government agencies.

All three offices appear to have a serious shortage of lawyers. If litigation in court increases over time, as predicted, this shortage will become even more acute. It will be difficult to attract more lawyers to the competition agencies, however, in large part because there are not many lawyers in these countries and the standards for qualification are high. The problem can be partly overcome by hiring people with some legal training who could perform many of the tasks in the office that lawyers might otherwise do, leaving the lawyers free for appearances in court.

The Lithuanian Competition Office, although the largest of the three agencies, nevertheless has certain critical resource issues relating to the additional duties with which it is charged, namely, consumer protection, state aids monitoring and antidumping. The latter two functions are new, and the Office does not currently have adequate resources to conduct them. The report recommends that consideration be given to transferring one or both of these functions elsewhere in the government, or in the alternative, providing a

significant augmentation of staff for these activities. Latvia's agency is the smallest of the three and, as noted above, faces significant challenges related to the fact that its staff is mostly new and inexperienced. The office requires the addition of more fully trained, qualified professionals. Estonia appears to have fared relatively well regarding resources; its staff has grown from 21 to 47 between 1996 and 1999. It too will be faced with new challenges in the near future, as it implements merger control and exercises its special responsibilities relating to natural and government-created monopolies.

It is a fact of life in every country that its government agencies are understaffed. Resource problems in the public sector cannot be solved merely by adding employees. Government agencies must constantly strive for greater efficiency, and this is true of these three competition agencies. The reports recommend that the agencies can improve efficiency in the following ways: by exercising sound discretion in case selection – prosecuting the cases that are most significant for consumers and the economy; by adopting procedures that ensure against having to review unnecessary notifications or becoming engaged in lengthy and unmanageable hearings; and by using innovative means for resolving cases, such as through voluntary compliance or negotiated settlements.

4.6.1 Discussion

The participants acknowledged continuing resource problems. The discussion centered on means of attracting and keeping qualified, motivated personnel. As with many other issues discussed in the conference, it was agreed that an effective public relations program is part of the solution. As more citizens become aware of the mission of the competition agency and the type of work that it does, interest in employment in the agency will grow. The best selling point to prospective employees is the fact that the work in the agencies is extremely interesting. All of the agencies employ students as part of their work force. If there are too many students, of course, the work of the agency will suffer because of their lack of experience. A positive aspect of employing students, on the other hand, is that they are more likely to continue working at the agency after completing their studies.

Employee turnover is a problem in all the participating Baltic agencies. Various means of addressing the problem were discussed, including requiring a mandatory commitment to remain with the competition agency for a minimum period of time. It was generally thought that imposing such an obligation would not work, however. Employee attrition is a fact of life in all competition agencies; some employees will inevitably be attracted to higher salaries in the private sector after gaining experience as enforcement officials. The challenge

to the agency is to manage such turnover as much as possible. Indeed, it can be made into a positive aspect of working at the agency. The fact that experience in the government agency can be translated into enhanced opportunities in the private sector can be used to attract highly qualified young professionals to work there. They should be convinced, however, that their experience will be valuable only after a certain length of time – at least three years or so.

COMPETITION ENFORCEMENT IN ESTONIA

1. The Legal and Institutional Structure

1.1 *The Competition Law*

The current competition law of Estonia was enacted in March of 1998 and became effective on 1 October 1998, replacing a competition law that was enacted in 1993.¹ This report of necessity focuses on the country's experience with competition policy under the old law, since there has been little experience with the new one. Throughout the report, however, the possible impact of provisions in the new law will be noted, where applicable.

The new law resembles the 1993 law in several respects. In particular, the substantive provisions of the two laws – prohibitions of abuse of dominance², anticompetitive restrictive agreements³ and unfair competition⁴ – are not substantially different. In other respects the new law introduced changes. A significant feature of the new law is its approximation to the competition law of the European Community, as required by the Europe Agreement between European Communities and their Member States and the Republic of Estonia. In this regard, chapters providing for a system of exemptions from the prohibition on restrictive agreements,⁵ for merger notification⁶ and for the control and reporting of state aids⁷ are found in the new law. Also, a chapter relating to natural monopolies and undertakings that have been granted special or exclusive rights by state or local government has been added by the new law.⁸

1.2 *The Competition Agency*

The Competition Board was created by the 1993 law and is headed by a Director General. The Board is established within the area of government of the Ministry of Finance. In addition to the Director, officers of the Board include a Deputy Director, Counselor, an Accountant and a Secretary. There are four departments within the Board: the **Department of Market Relations**, which has responsibility for matters involving abuse of dominance, mergers and

unfair competition; the **Department of Agreements**, which has responsibility for restrictive agreements and concerted practices, including supervising the administration of individual and block exemptions; the **Department of External and Public Relations**, which has responsibility for dealing with competition authorities of other countries, matters relating to eurointegration, training, and providing information necessary for the work of the Board; and the **Legal Department**, which provides legal services to other departments, drafts competition legislation and reviews drafts of other legislation on behalf of the Board.

The Board employed a total of 38 people at the end of 1998. Of these, 26 were investigative specialists, four were lawyers, four were specialists in external relations and public affairs and four were clerical. It is expected that in 1999 the number of employees will increase to 47.

2. Substantive enforcement

In this section the Office's enforcement of the substantive provisions of the competition law will be reviewed. Each area of substantive law (*e.g.*, abuse of dominance, restrictive agreements, mergers) will be discussed separately. Brief descriptions of representative cases will be included where appropriate. Comments and recommendations will also be provided at the end of each section.

2.1 Abuse of a Dominant Position

Article 13 of the new law defines "dominant position" as having a market share of at least 40 per cent or having the ability "to operate in the market to an appreciable extent independently of competitors, suppliers and buyers." Article 14 prohibits generally the abuse of a dominant position, and specifically enumerates the following types of conduct as abuses: imposing unfair pricing or trading conditions, including unjustified pricing below cost resulting in the prejudice or exclusion of another undertaking from the market; limiting production, technical development or investment to the prejudice of consumers; applying dissimilar conditions to equivalent contracts; making an agreement conditional upon the entry into another, unrelated agreement; forcing an undertaking to merge or to enter into an agreement or concerted practices; unjustified refusal to sell goods to another undertaking; and unequal treatment of undertakings which participate in offers or bids.

The provisions of the 1993 law regarding abuse of dominance were similar, but not identical. A 40 per cent market share was not sufficient by itself to confer a dominant position, which appears to be true with the new law.

Abuse of dominance cases are among the most numerous of all types of matters that come before the Board. For the past five years the Board has considered about 20 such matters on average each year. Many of the cases involve entities that enjoy a natural monopoly or control an essential facility. Abuse cases have arisen in markets for heat supply, telecommunications and transportation, for example. Often the Board has been able to reach a solution through negotiations with the offending party, obviating the need for prescriptive orders. Occasionally, remedial orders have been necessary, however.

As noted above one feature of the new law that was not part of the 1993 law is Chapter 5 (articles 15-18), "Undertaking with Special or Exclusive rights or Natural Monopoly." Provisions of this sort, applying specifically to natural or government-created monopolies, are not often found in national competition laws. They provide the Estonian Competition Board with potentially important powers in dealing with these entities.

Article 15 acknowledges the power of state and local governments to grant special or exclusive rights to enterprises through legislation, but states that unless otherwise provided in the legislation, there must be a public competition for such rights. Article 17 provides that government bodies may establish procedures for regulation of the entities in a monopoly or exclusive position. In a potentially important provision, Article 18 sets forth certain rules of operation of these enterprises. They must provide access to their network or exclusive facility on a nondiscriminatory basis; they must provide a clear distinction, including separate accounting procedures, between "primary and secondary activities" (presumably, those that have characteristics of natural monopoly or legal exclusivity and those that do not); and their purchases and contracting procedures must be conducted according to the Estonian Public Procurement Act. Article 18 also sets forth permissible grounds for the refusal of access to natural monopoly or exclusive facilities. To date no cases or investigations have been undertaken pursuant to these provisions.

The following cases are illustrative of abuse of dominance cases in Estonia in recent years:

Mobile Telephones

In 1996 there were two providers of mobile telephone services in Estonia. Mobile I was the first to enter the market. It offered two services. One (NMT 450) offered local and long distance service throughout Estonia and in Nordic countries. The second, a global digital system (GSM) could be used worldwide where GSM facilities existed. Mobile I could not provide GSM services throughout Estonia, however. The second competitor, Mobile II, offered GSM only. For technical reasons, NMT 450 service could be provided by only one carrier. Mobile II's GSM facilities covered only a small portion of the territory of Estonia, although Mobile II was in the process of adding to its network. Mobile II's share of GSM services in Estonia was only eight per cent.

Mobile II complained that Mobile I was engaging in discriminatory pricing through its monopoly on NMT 450 service. Mobile II claimed that Mobile I's price of GSM service was below its cost – that it was cross-subsidizing its GSM prices through its NMT 450 monopoly. The Competition Board analysed the prices and costs of Mobile I and concluded that its prices were not discriminatory or below cost. It found that customers preferred Mobile I because of its wider coverage, and in some cases were paying more for Mobile I's GSM service than for that offered by Mobile II. The Board concluded that Mobile I was not abusing its dominant position. The Board did request that Mobile I make certain changes in the way that its prices were presented to customers, which Mobile I did.

Tallinn Bus Station

The station used for intercity passenger bus service in Tallinn (the only one in the city) was privatised in 1996. A majority interest was sold to Eesti Buss joint stock company, which also was the largest intercity bus operator. There were as many as 26 enterprises providing bus service through the station, although many had very small operations. The second largest bus operator, Sebe, had been operating at a separate location in the station, where it sold tickets and posted schedules. In negotiations for a new contract, however, Eesti Buss insisted that all operators use a single location in the station for these services. Sebe objected.

The Competition Board concluded that Eesti Buss was not guilty of abuse of dominance. Eesti Buss had created a separate business entity to operate the station, apart from Eesti Buss's bus operations. It appeared that all bus operators were receiving equal terms from the station operator. The investigation revealed that a principal reason for Sebe's insistence on a separate location for ticket sales was the past failure of Eesti Buss to remit the sales proceeds from its location in a timely fashion. This problem was resolved through separate negotiations, however.

Comment

Abuses of a dominant position tend to occur relatively more frequently in transition countries. Monopolies or dominant positions are more common in these countries, having been created by privatisation of formerly state-owned monopolies, and they tend to be more persistent, because entry by new competitors may be hindered by imperfectly functioning capital markets and scarcity of other important inputs, such as good distributors or retail outlets. Further, regulation of network infrastructure industries may not yet be fully effective, giving rise to abuses involving access to these monopoly assets. It may fall to the competition authority to prosecute such cases, at least in the first years of private operations in these sectors.

As noted above, abuse of dominance cases are frequent in Estonia. It is obviously an important area of enforcement for the Board. Abuse of dominance cases tend to be fact intensive and difficult to prosecute. Market definition and conditions of entry are often crucial to the dominance analysis, and in smaller transition countries such as Estonia both issues often revolve around the availability of imports as substitutes for domestic products or services.

Because its resources are so limited, the Competition Board will be able to successfully prosecute only a relatively few of these important cases each year. The fact that some of the cases involving abuse of dominance were successfully terminated by voluntary compliance by the dominant firms is a positive sign, in that scarce resources of the Board were conserved. In other instances, however, the Board may need to impose more comprehensive remedies to ensure the restoration of competition.

One feature of the Estonian competition law relating to abuse of dominance is potentially troublesome. The apparently automatic designation of dominance for an enterprise with a 40 per cent market share could lead to erroneous results in some situations. Even very high market shares do not confer dominance if entry into the relevant market is not difficult. In some other countries the competition law provides that a high market share, such as 40 per cent or more, establishes a presumption of dominance that can be rebutted by other

evidence tending to show that the enterprise does not have actual market power.

In other respects, some of the specific designations of abusive conduct in the law, such as “unfair pricing,” “limiting production,” or “unjustified refusal to sell to another undertaking,” are difficult to interpret and may be confused with legitimate competitive conduct. (Such provisions are not unique to the Estonian law, however.) Most competition experts consider that enforcement of abuse of dominance provisions should focus on exclusionary conduct – that which unnecessarily excludes actual or potential rivals from the market – rather than “exploitative” conduct – charging high prices or imposing terms that appear to be unfair. The mobile telephones case described above does involve potentially exclusionary conduct. If the pricing scheme of the dominant firm had been discriminatory as alleged (it turned out not to be so) it could have had the effect of excluding the smaller rival.

As noted above, Chapter 5 of the new law is potentially important for the Board in dealing with natural monopolies or enterprises with government-created exclusive rights. There may be many markets in Estonia that are dominated by such firms. The first priority of the Board is to seek to eliminate such monopoly power wherever possible, but where it exists the provisions of Chapter 5 afford the Board the opportunity to ensure that the dominant enterprise operates in a transparent and nondiscriminatory fashion. Of course, before applying the extraordinary remedies of Chapter 5, the Board must determine that monopoly power in fact exists, which requires an accurate definition of the relevant market or markets. The fact that an enterprise operates in a sector that usually has some characteristics of natural monopoly (telecommunications, for example), does not mean that it has monopoly power in all of its markets (competition may exist, or be possible, in long distance service, for example).

Recommendations

- Potential abuse of dominance cases should be carefully analysed for their importance to the Estonian economy and to consumers. While the law may permit a conclusive finding of dominance where an enterprise has a market share in excess of 40 per cent, in such cases the Board should also examine other relevant evidence, including particularly the conditions of entry, before concluding that dominance exists.
- Cases that involve exclusionary practices, rather than exploitative conduct (*e.g.*, monopolistic pricing) are more likely to have that significance. In deciding the decisive issues of market definition and conditions of entry, the availability of foreign sources of supply should be carefully considered.
- In cases where an abuse is shown, the Board should strive to achieve effective relief. This may mean, in selected cases, bringing about a change in the structure of the market such that the underlying position of dominance is eroded. This is most easily and effectively accomplished by measures that remove or ameliorate unnatural barriers to entry, rather than by attempts at breakup or restructuring of firms.
- Review markets dominated by natural monopolies or enterprises with government-created exclusive rights. First determine that actual monopoly power exists. Then work to eliminate such market power by restructuring or elimination of the government grant. In the remainder of such cases, apply the provisions of Chapter 5 of the new competition law to ameliorate the anticompetitive effects of such dominance.

2.2 Restrictive Agreements

Article 4 of the new law prohibits agreements or concerted practices that have as their object or effect “the restriction, prevention, limitation or distortion . . . of competition.” The following specific types of agreements are listed as unlawful: on prices or terms of sale; on limiting production, markets, technical development or investment; sharing markets; restricting market access to third persons; disseminating information which distorts competition;

applying dissimilar conditions to third parties in equivalent circumstances; and on conditioning contracts on entering into unrelated obligations. Article 4 does not distinguish by its terms between horizontal and vertical agreements. Article 5 excludes from the prohibitions of Article 4 agreements in which the combined turnover of the parties to the agreement does not exceed five per cent of the total turnover of the market affected by the agreement and similar agreements involving a party to the agreement in the relevant market do not exceed five per cent of the total in the market.

Article 6 provides for the granting by the Competition Board of individual exemptions, and Article 7 provides for the creation of block exemptions by Government regulation. The criteria for granting individual exemptions closely follow those employed by the European Union. Block exemptions may be granted for certain types of agreements that meet the criteria set forth in Article 6. Block exemptions do not apply to conduct that is considered an abuse of dominance or in markets in which “competition is virtually non-existent.” Block exemptions for four types of restrictive agreements (exclusive purchasing, distribution, motor vehicle distribution and servicing and franchise agreements) are in preparation.

Articles 9-12 set out the procedures for the granting of individual exemptions. The application for an exemption must be submitted within six months after entry into the agreement.⁹ An agreement that is caught by Article 4 is considered invalid until the exemption is granted. The Board must approve or deny the application, or order a supplemental proceeding, within two months after receiving the application. If a supplemental proceeding is ordered it must be completed within six months of the receipt of the additional information required. No applications for exemptions were received in the three months of 1998 in which the new law was in effect.

Since 1993 the Competition Board has considered a total of 28 cases and investigations involving possible restrictive agreements. In 1996 and 1997 the number of such matters reached its highest level, at nine and eight, respectively. Three matters of this type were considered in 1998. Most of these cases did not involve actual or possible cartel conduct, but some did. A few such matters were highly publicised, as they involved possible concerted activity in markets for basic consumer products. The Board observed prices rising or falling in concert, but for the most part it was unable to develop evidence of agreement, either tacit or explicit, among the market participants. The following case is one in which evidence of concerted practices was present.

Allied Bakers Association

The Allied Bakers Association was composed of 21 bakers, who accounted for about 80 per cent of total bread production in Estonia. In December of 1996 a newspaper Article quoted a representative of the association as saying that its members had agreed to raise their prices of bread because of the increasing cost of flour, which was the result of higher grain prices worldwide. The investigation by the Competition Board revealed that the members had agreed in principal to raise their prices according to the higher flour prices faced by each baker, and that in December the members did raise their prices by varying amounts, ranging from 10 to 33 per cent. There was no agreement, however, on a specific amount of increase or on the timing of the increase. The investigation further revealed that the price of flour had increased by 52-62 per cent in the period immediately preceding the announcement. Bakers who were not members of the association did not raise their prices in December, but it was felt that they would ultimately do so.

The investigation revealed that the association apparently was not fully aware that their agreement was prohibited by the competition law, and the reason that it had made the public announcement was to engage the Ministry of Agriculture in discussions about maintaining an adequate supply of this important consumer product.

The Board concluded that the agreement of the association was a violation of the competition law. It issued a prescriptive order prohibiting the members of the association from engaging in discussions of production, pricing policy and market behaviour.

Comment

The Estonian experience in restrictive agreements, and especially in cartel conduct, parallels that in many transition countries. To date the Board has prosecuted few cartel agreements, notwithstanding the likelihood that such agreements are common as carryovers from the period of central management. Given the unambiguous harm to consumers that results from cartel conduct, however, detection and prosecution of such agreements should have a high priority within the Board.

Acquiring evidence of an illegal agreement is difficult, especially when the subjects of the investigation are not co-operative. Successful prosecution tends to occur only when the subjects voluntarily produce evidence of the illegal activity, often because they do not know that the conduct is unlawful. The Allied Bakers case described above is such a case. It is likely, however,

that over time the Board will receive less co-operation from the subjects of cartel investigations, as cartel operators become more sophisticated, and thus it will be necessary to develop better investigative techniques in such cases.

The Allied Bakers case is interesting for another reason. The facts suggest that the unlawful concerted activity was perhaps not an explicit agreement but instead a common understanding on future prices based on exchanges of detailed, sensitive information among competitors. The Council correctly recognised that such conduct can lead to unlawful co-ordination by competitors, and correctly imposed an order prohibiting such information exchanges.

The Estonian system for notification and exemption of restrictive agreements closely parallels that of the European Union. This system offers, in the long run, the benefit of enhanced certainty for the business community about the legality of their agreements. The Board must be careful not to impose burdensome notification requirements, however. The EU experience has shown that a competition authority is ill-equipped to deal with large numbers of applications for exemptions. Indeed, the European Commission is currently considering substantial revisions of its exemption and notification procedures.

Recommendations

- Detection and prosecution of cartels should have a high priority within the Board. There are several facets to this effort:
 1. Educating consumers about the harm to them from cartels – higher prices and lower quality; encouraging consumers to co-operate with the Board's efforts to eliminate cartel activity by providing information about suspected illegal conduct.
 2. Educating businesspeople about their obligations under the competition law, encouraging voluntary compliance with its requirements; helping them also to realise that businesses are consumers too, and

therefore that they benefit from the elimination of cartels.

3. Becoming more aggressive in gathering evidence in situations of non-co-operation by investigation subjects; in particular, a) developing methods of obtaining potentially incriminating documentary evidence from the files of suspected cartel members, and b) encouraging co-operation by witnesses with information about cartel conduct by providing them with incentives, such as immunity from prosecution or reduced fines.
 4. Punishing cartel operators with significant fines, especially in situations where the activity was conducted in secret and the operators were aware of the illegality of their conduct.
- Complete the process of promulgating block exemptions under Article 7. Avoid, as much as possible, the implementation of unnecessary and burdensome notification and information procedures relating to exemptions.

2.3 Mergers

The 1993 law did not provide for merger control, nor does the new law. It is possible that mergers involving dominant firms could be prosecuted as abuse of dominance, but there have not been any such cases to date. The new law does envision the enactment of merger control provisions, however. Articles 26-27 provide for notification of certain mergers to the Competition Board. It is generally expected that this first step will lead to the enactment of substantive merger control provisions in the near future.

Article 27 requires that mergers of parties collectively having annual turnover of more than 100 million kroons (EEK) or separately or collectively having a share of more than 40 per cent of the relevant market be notified to the Board. Consummation of the transaction may not take place until one month after notification unless agreed by the Board. The Ministry of Finance has published a regulation setting forth the information required in the notification.

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Comment

Estonia is proceeding carefully in implementing merger control. It will be a useful exercise for the Board to consider the mergers that are currently being notified under the new law, even in the absence of a specific merger control law. The analysis will likely reveal that most mergers are not competitively harmful, which is true in almost every country, including OECD countries. The Board can employ this experience to draft an intelligent merger control law, one that identifies and targets the few truly anticompetitive mergers that occur in Estonia.

In this regard, the Board should be careful to take into account the possibility of foreign competition in its merger analysis. It is especially true in small countries like Estonia that imports are relatively more important than in larger countries. Absent significant restraints on imports, mergers of domestic firms may seldom be anticompetitive. (Domestic mergers may be of greater concern in markets involving nontradable goods or services.)

While there is no merger control provision in the current competition law, it would seem to be possible to prosecute anticompetitive mergers under Article 14, abuse of a dominant position, and possibly also under Article 4, restrictive agreements. If that is so, the premerger notification requirement would be useful whether or not merger control provisions are enacted.

In any case, it is important that the merger notification thresholds are not set so low that they catch an unnecessarily large number of transactions. Unduly low thresholds create burdens both for the business community, which must prepare and file the notifications, and for the competition agency, which must review them. In that regard, it appears that the EEK 100 million minimum turnover threshold includes worldwide turnover of the merging parties, not just turnover within Estonia. As such, the threshold may catch a relatively large number of transactions that are unlikely to have anticompetitive effects within Estonia.

Recommendations

- Work to enact substantive merger control provisions that employ reasonable and generally accepted standards, such as those employed by the EU. Merger analysis, however, should take into account the specific circumstances in Estonia. In the meantime consider the applicability of the abuse of dominance and restrictive agreement provisions of the law to harmful mergers.
- Review the merger notification experience under the new law for the purpose of determining the appropriateness of the notification thresholds, and if they appear to be too low, seek authority to raise them. Consider especially modifying the turnover threshold to include only turnover within Estonia.

2.4 *Anticompetitive Activities of Government Bodies*

The competition laws of several transition countries directly prohibit anticompetitive conduct by executive bodies of state and local government. These laws provide for direct action by the competition agency against the offending government body and for the application of the usual sanctions against such conduct. In enforcing these provisions the competition agency is limited by practical realities; it may not have sufficient political power to confront directly another body of government, especially a part of the national government, such as a ministry. Still, in several transition countries there have been cases or investigations instituted under these provisions. More often than not these cases are resolved not by mandatory sanctions or orders, but by negotiations that lead to a voluntary solution.

In Estonia, Article 4(2) of the 1993 act provided that conduct by bodies of state or local government that was contrary to the act and not permitted by other legislation was a violation of the competition act. Article 2(2) of the new act states that the provisions of the act extend to the “decisions or activities” of state and local government agencies that restrict competition. The Competition Board has been active in this area, having considered a total of 31 matters involving government activities since 1993. No formal orders have been entered in these matters, but in several, anticompetitive conduct was eliminated voluntarily by the offending agency after discussions with the Board.

Municipal Waste, Jõhvi City

The government of the city of Jõhvi imposed a requirement that trucks larger than eight tons must pay a fee to operate on the city streets. An entity that desired to enter the market for solid waste collection in the city and that used trucks larger than eight tons complained to the Competition Board that the city was not imposing the fee on a former municipal undertaking that was operating in the waste collection market with trucks larger than eight tons. The Board initiated a proceeding and determined that Jõhvi City was indeed discriminating in favor of its former affiliate. After negotiations with the Board, the city government eliminated the discriminatory treatment.

Discriminatory Application of the VAT Law

The Union of Private Physicians complained to the Competition Board that the value added tax law was being applied to them in an anticompetitive manner. Specifically, they alleged that those physicians who had contracted with the state Sick Fund were not required to pay the VAT, while private physicians who had not contracted with the Fund did have to pay the tax, placing them at a competitive disadvantage. After consultations between the Competition Board, the Tax Board and the Ministry of Finance, amendments to the VAT Law were drafted and adopted by the Parliament, eliminating the discriminatory treatment of the private physicians.

Comment

The Competition Board has been relatively active in pursuing anticompetitive conduct by other government agencies. It has achieved some success through voluntary negotiations and agreement with government agencies. It is evident that more can be accomplished, however.

The elimination of unnecessary and anticompetitive government regulations is an efficient use of a competition agency's limited resources. The benefits to consumers from such activities may be substantially greater than the benefits resulting from a comparable expenditure resources on prosecution of cases. Moreover, success in this area reflects quickly and favourably upon the competition agency, helping to build its credibility in the business and consumer communities.

Recommendations

- Place strong emphasis upon elimination of anticompetitive restraints by government bodies. Make the business community an ally in this effort.
- Approach offending government bodies judiciously. Seek to enlist their co-operation, rather than opposition, in this program.
- When there are successes, use available means to inform the public of them, thereby strengthening support for the work of the Board and for competition policy.

2.5 *Unfair Competition*

Chapter 8 of the new law (Articles 28-33) prohibits unfair competition. These provisions are similar to those of the 1993 law relating to unfair competition (Articles 7-13). Unfair competition is defined in the new law as including: publication of misleading information; disparagement of a competitor or a competitor's goods; misuse of confidential information; "misuse of an employee or representative of another organisation" (which includes influencing an employee or former employee to reveal confidential information belonging to the current or former employer); and "unfair restriction or promotion of goods" (which is further defined as a) restricting the amount of goods to be sold to a buyer or subjecting such sale to a condition unless such restrictions are necessary for the use of the good, b) calling for the prohibition of sales by a competitor (presumably without justification), and c) subjecting the sale of goods to the obligation to purchase other goods or to find a new buyer).

Investigations and cases involving allegations of unfair competition have been the most numerous of any type of matter considered by the Board since 1993. A total of 97 such matters have come before the Board in that period. In the years 1995-97 the Board handled between 21 and 25 unfair competition matters each year, but the number fell to 11 in 1998, the lowest since 1993. The most common type of unfair competition case that comes before the Board involves forms of misleading advertising, which includes the use of trademarks or business names of another entity. Most of the Board's unfair competition cases have been resolved through negotiations leading to voluntary compliance by the offender.

There have been some court cases instituted by private parties alleging acts of unfair competition (almost no private cases involving other forms of anticompetitive conduct have been brought in Estonia to date). Some of these cases involve “misuse of an employee” of another entity, including the hiring of such a person for the purpose of acquiring his or her clients or business contacts.

Comment

Protection of intellectual property rights and against untruthful and misleading disparagement of a competitor are important to the proper functioning of free markets. In countries whose economies have been recently liberalised, it is not uncommon for the competition agency to institute a relatively large number of cases of unfair competition, even when the practices do not have an impact on the economy as a whole. As economies mature, however, the number of such cases brought by the competition agency tends to decline, for at least two reasons. First, businesses become more knowledgeable about what the law permits in this area. Second, and possibly more important, in developed economies there is generally easier access to courts for resolution of private disputes, and businesses tend to resort to such remedies directly in cases of unfair competition. Apparently it is possible in Estonia for private entities to bring their own actions in court for acts of unfair competition. The Board could encourage the development of such a remedy as a means of conserving its own resources for prosecution of broader anticompetitive conduct.

Recommendations

- Continue to prosecute important cases of unfair competition, especially where significant issues of protection of intellectual property are involved, but to conserve important resources, encourage businesses to resolve their disputes privately, where possible.
- Use the authority of the Board to achieve voluntary compliance when it appears that violations have occurred, again to conserve resources.

2.6 *Consumer Protection*

The Competition Board does not have responsibility for consumer protection. That function is provided by the State Board of Protection of Consumers pursuant to the 1993 Consumer Protection Act.

2.7 *State Aids*

Chapter 6 of the new law (Articles 19-25) provides a new and comprehensive structure for the granting of state aid by state or local governments, pursuant to the requirements of the Europe Agreement between the European Communities and their Member States and Estonian Republic. The law defines the types of state aid that are permissible and establishes procedures for the application for state aid. The Minister of Finance has the responsibility for managing the application and grant procedures and for monitoring and reporting on state aid. The law does not provide for any direct involvement of the Competition Board in the process, but the Board has the ability to submit comments or recommendations in specific cases.

Comment

State aids can have important implications for competition policy. Improper and indiscriminate granting of state aids can result in significant market distortions, impeding competition and harming consumers. The competition agency should have an advisory role in this area, to ensure that markets function as free from government interference as possible. On the other hand, direct involvement in the state aid granting and monitoring functions could impose a heavy burden on the resources of the Competition Board. The role of the Board should be limited to the review of applications and decisions of the relevant body of the Ministry of Finance to ensure that it properly incorporates relevant principles of competition policy.

Recommendations

- Participate as an advisor in the granting and monitoring of state aid at a level consistent with the limited resources of the Competition Board. Review state aid applications for the purpose of ensuring, to the maximum extent possible within overall government policy, that markets remain competitive and free from unnecessary government interference.

2.8 *Competition Advocacy*

Article 35(2) of the new act authorises the Competition Board to make recommendations to other government bodies for the purpose of promoting competition and to review and propose legislation for that purpose. The 1993 law contained a similar provision. The Board has provided competition advocacy on occasion, notably in the privatisation and regulation of natural monopolies. The Board provided comments on drafts of the recently-enacted energy law which established an Energy Market Inspectorate with regulatory responsibility in the energy sector. The Board has commented on a draft telecommunications law, which is still in preparation. The Board's comments are submitted through the Ministry of Finance.

Comment

The Competition Board currently participates in a limited way as competition advocate in legislative and regulatory affairs. Both time and resources are required to develop expertise and credibility in competition advocacy, and so it could be expected that the Board would proceed carefully in this area. Moreover, competition advocacy is difficult in every country, and it is especially so in a transition or developing country. Paradoxically, competition advocacy is probably more important in those countries, which are engaged in wholesale reformulation of their economic policies, than in developed economies.

The Competition Board faces a significant challenge in this important area. It has limited resources, so it must carefully select the matters in which it will participate. The competition agency is usually most successful when its advocacy function is grounded in the agency's law enforcement experience. Perhaps most important, its independence within the government, or lack thereof (discussed further below), will control the extent to which it can be effective as competition advocate.

As discussed above in **section 2.1**, Chapter 5 of the new law provides the Competition Board with potentially important new powers in dealing with natural monopolies and entities with government-created exclusive rights. These provisions also have important implications for the Board's competition advocacy role. Chapter 5 sets forth general rules governing regulatory policy that will be applied in these sectors, requiring,

for example, price regulation that ensures that buyers “are not placed in a substantially worse situation than they would be if competition were present in that area of activity,” and access rules that “permit access to the network or infrastructure by other undertakings under reasonable and non-discriminatory conditions.” These provisions place the Board in a much stronger position than it would otherwise be as it participates in the design and implementation of regulatory regimes in Estonia.

Recommendations

- Place a growing emphasis on the Board’s role as competition advocate, consistent with available resources and within other priorities facing the Board. Select the matters in which it will participate carefully, with an eye toward the impact of the decision under consideration on consumers.
- Prepare the Board’s competition advocacy comments with care, striving for accuracy, to enhance the Board’s credibility in this arena. Where the Board lacks expertise in a technical area, enlist the aid of interested and sympathetic outsiders who have the requisite knowledge, such as academics or business groups.
- Consider means of utilizing the provisions of Chapter 5 of the new competition law effectively in competition advocacy.

3. Institutional Issues

3.1 Independence of the Board Within the Government

The new law does not specifically set forth the attributes of the Competition Board that describe its place within the Estonian government. Those aspects are controlled by the Government of the Republic Act,¹⁰ which provides that the Board is an executive government agency that operates within the area of government of the Ministry of Finance. In that capacity the Board exercises state supervision and applies enforcement powers of the state on the basis and to the extent prescribed by law. While Board operates in the area of

government of the Ministry of Finance, it is technically not part of that Ministry, and it is considered to be independent in its decisions. The Director of the Board is appointed to and removed from office by the Finance Minister upon the recommendation of the Secretary General.

Comment

It is generally accepted within the international competition community that a national competition authority should operate with as much independence from the rest of the government as possible. Its decisions, like those of regulatory agencies, may affect the interests of large and powerful businesses, which may have strong political influence with the government. The competition agency should be free of such influence to the extent possible. Thus, it is often recommended that the competition agency be created as a separate entity that is not a part of any other government ministry. The agency would be answerable directly to the legislature for its funding, and the head of the agency or the members of the commission would be appointed by the president or other chief executive, subject to removal only for gross negligence, corruption or clear inability to perform the functions of the office.

Such a structure may be the ideal, and does not exist in that form in most countries, but in many the competition agency is created as a nominally separate body, not a part of the state government. In Estonia this is not the case, where the Competition Board is part of the government, with Minister of Finance having the power to appoint and remove the Director General of the Board. On the other hand, the Board is considered to have independent decision making authority.

In many countries the competition authority exists as part of the government, usually as part of the Ministry of Justice, Economy or Finance. In these countries the competition agency is not fully independent from the structural standpoint, but this does not mean that it cannot be independent as a practical matter. A significant degree of “informal” independence can be achieved over time by the Board, by means of measured, impartial and transparent decision making, coupled with the building of public understanding and support for the Board’s mission. It appears that the Board already enjoys some independence in this regard, and it should have as a long term goal to maintain and strengthen it.

3.2 *Investigative Powers*

Articles 35-38 of the new law provide the Board with the power to conduct investigations and gather information. It can: monitor markets and conduct investigations and proceedings relating to possible violations of the law and require the submission of information relating thereto from individuals, legal persons and government agencies; compel the production oral testimony and the production of documentary material; and upon authorisation of the Director or Deputy Director inspect the premises of an undertaking without prior notice or consent. At such an inspection the representative of the Board has the power to examine documents of the undertaking and receive oral testimony of representatives of the undertaking. At the conclusion of such an inspection the representative of the Board has the obligation to prepare a summary of the inspection, which shall be signed by the undertaking's representative. The Board had similar powers under the 1993 law.

It appears that most investigations by the Board to date have been conducted on a voluntary basis. The Board has had some success in obtaining the co-operation of subjects in these matters, but in other cases the Board has had difficulties, particularly those involving possible cartel conduct, such as price fixing or market allocation. Parties to such agreements who know that their conduct is unlawful are unlikely to voluntarily provide evidence of the violation.

Comment

The Board has adequate powers of investigation under the new law. To date, its powers to compel the production of evidence have been used sparingly, however. As businesspeople become more sophisticated and knowledgeable about the competition law, and as investigations and cases become more sophisticated and complex, the Board will likely find it necessary to resort more frequently to its compulsory powers. It must use those powers judiciously, however. The Board must gain the confidence of the business community that its powers will be used fairly. Demands for information should not be issued indiscriminately, generating heavy burdens of compliance on investigative subjects and corresponding burdens on the Board of reviewing the information. Finally, the Board must be firm in enforcing these powers, vigorously prosecuting intentional untruthfulness or willful failure to comply with information demands.

Recommendations

- Employ the new information powers selectively and fairly.
- 1. Continue to use voluntary means of investigation whenever possible, especially when seeking information from non-subjects – “third parties” – in an investigation.
- 2. Conduct unannounced “dawn raids” and searches of business premises sparingly, for example only when serious, ongoing anticompetitive conduct is suspected, and co-operation by the subjects of the investigation is unlikely.
- 3. Perfect techniques of requesting and reviewing relevant business documents from relevant parties. Documents written in the regular course of business often are the best source of evidence for use in defining markets and assessing the competitive effects of relevant conduct.
- 4. Be willing to discuss demands for information with recipients with the purpose of meeting their legitimate concerns about burdens of production.
- 5. Institute rigorous procedures for safeguarding the confidentiality of information that is provided, as the law requires. Take pains to assure the providers of information, both voluntary and involuntary, that the confidentiality of their information will be maintained.
- Be prepared to prosecute economic subjects who intentionally provide false information or willfully withhold information specified in a demand. Seek strong sanctions for such conduct.

3.3 *Enforcement and Sanctioning Powers*

Article 40 of the new law provides that upon a finding by the Board that a violation of the competition law has occurred the Board may issue a mandatory order requiring any of the following: to terminate the violation; to restore the situation that existed before the violation; to take action to eliminate

the violation; and to refrain from performing acts that may lead to further violations. Under the 1993 law the Board had similar powers.

The Board has been fairly active in employing these powers to issue prescriptive orders. In the years 1995-97 it issued a total of 14 such orders. In 29 matters, violations of the law were resolved by voluntary agreement or abandonment of the relevant conduct by the parties. In 1998, out of a total of 58 matters, 10 were resolved by prescriptive orders and 10 by voluntary agreement or abandonment.

The new law provides an important new sanction: fines for substantive violations of the competition law. Under the 1993 law fines could be imposed only for failure to obey a prescriptive order of the Board. Article 45 of the new law provides that a fine of up to five per cent of the net turnover of the offending party in the preceding year, but not less than EEK 20 000, may be imposed for unlawful restrictive agreements or abuse of dominance. (No fines are provided for acts of unfair competition.) For failure to notify a merger to the Board as required by the law a fine of up to one per cent of net turnover, but not less than EEK 10 000, may be imposed. For failure to observe the requirements of Article 18, relating to natural monopolies or undertakings with exclusive rights, a fine of up to one per cent of net turnover, but not less than EEK 10 000, may be imposed. Fines for these violations must be imposed by an administrative judge. The law does not otherwise spell out the procedures for administrative hearings on fines.

Article 43 provides that the Competition Board may impose a fine of up to EEK 2 000 per day for failure to provide information or materials as required by the Board or refusal to permit an inspection of a business premises as contained in a directive of the Director. For failure to observe a prescriptive order of the Board the Board may impose a fine of up to EEK 5 000 per day.

Article 42 provides that both legal and natural persons are subject to the sanctions provided in Articles 43 and 45. In determining the amount of a fine, the fining authority shall take into account the extent of co-operation with the Board by the subject and whether or not the violation was voluntarily terminated by the subject before the imposition of sanctions.

Article 48 provides that private parties who suffer damage from violations of the competition act may pursue compensation for such damages in civil court. A similar provision was contained in the 1993 law. To date, however, this remedy has been used sparingly, if at all, in Estonia.

Comment

It appears that the new law provides the Board with adequate enforcement and sanctioning powers. Its challenge is to apply them fairly and effectively. It may be useful for the Board to undertake a review of remedial orders that have been entered in previous abuse of dominance and restrictive agreement cases. Have they succeeded in eliminating the unlawful conduct and restoring competition to the market? A simple order to cease a violation may not be sufficient in some circumstances. Some “fencing in” provisions may also be in order, but it is also important that such an order not be too intrusive and ultimately anticompetitive itself.

The power to fine for substantive violations of the law is an important addition to the new law. The maximum fine of five per cent of annual net turnover appears to be adequate, although that issue should be periodically reviewed over time. Fines should not be imposed in all cases. They are most appropriate for “hard core” violations, such as price fixing and market allocation, and some egregious abuses of dominance. In such cases they must be sufficiently large to create a deterrent to future violations. As noted above in section 2.2, it is hoped that the Board will become more aggressive in prosecuting these violations. The threat of heavy fines has a beneficial effect in such cases. It can encourage individuals and enterprises to co-operate in investigations and cases to achieve a reduction or elimination of their liability.

The ability for private parties to pursue redress for harm from violations of the competition law can be an important component of a country’s competition enforcement. Such private actions effectively supplement the work of the competition authority in enforcing the law. In addition, the threat of having to pay possibly large damages to private parties is an additional deterrent to those who would violate the law. The Estonian law permits such private actions, but apparently they are seldom if ever pursued. The Board could undertake a study of means of facilitating private actions and, within the limits of its discretionary powers, make efforts to inform the business and legal communities of the availability of such a remedy.

Recommendations

- Consider the effectiveness of prohibitions and remedial orders in abuse of dominance and restrictive agreement cases. Attempt to fashion orders that are limited to eliminating the illegal conduct and its effects, are easy to administer and limited in duration.
- Impose increasingly large fines for engaging in cartel conduct and for willful disobedience of the Board’s orders or the willful submission of false or incomplete information.
- Employ the Board’s discretionary powers to fine as a tool in gaining co-operation in investigations and cases, especially those involving cartel conduct.
- Work to educate the business and legal communities about the opportunities for the pursuit of private actions to recover damages caused by violations of the law.

3.4 Administrative Procedures and Appeals

Articles 39 and 40 of the new law set forth the procedures to be employed by the Board in proceedings under the competition law. The Director of the Competition Board may institute a proceeding either *ex officio* or upon receipt of a complaint or application. If a complaint is received the Director must decide within ten days whether or not to begin a proceeding. The Director may refuse to begin a proceeding if he or she concludes that the act has not been violated or the matter is not within the competence of the Board.

The Director must publish a notice of the commencement of a proceeding in at least one daily national newspaper. The entity or entities that are subjects of the proceeding must be informed of the proceeding in writing, and the Director may require the subjects to submit relevant information. Third parties “with an interest in the matter” may submit information to the Board, and the Board has the power to require the production of information by third parties. The Board may conduct a hearing on the matter, which may be attended by representatives of the subjects and the Board, and of third parties as agreed upon by the Board and the subjects. The Board must make a final decision on the matter within three months after the receipt of all information. The subjects of the proceeding are given ten days’ advance notice of the decision, during which the subjects may examine the relevant evidence, except

for business secrets of other parties. The decision of the Board must be published in at least one daily national newspaper within three months of the entry of the decision into force.

The proceedings of the Board are conducted according to the procedures provided in the Estonian Code of Administrative Offences. According to these procedures, final decisions of the Board may be appealed to the Administrative Court. The 1993 law provided for the appeal of a decision of the Board to court. In the period 1993-98 nine decisions of the Board were appealed. Four decisions were upheld in their entirety, one was upheld in part and one not upheld. Three cases were undecided at the end of 1998.

Comment

The new law is a substantial improvement over the 1993 law in this area. The old law did not spell out the procedures for the consideration of complaints or applications, or for the conduct of Board proceedings. The procedures provided in the new law provide sufficient opportunity for accused parties and interested third parties to present evidence and to be heard in Board proceedings. It is important that the Board's work be transparent. Transparency builds confidence in the business and consumer communities in the integrity of the agency and helps to generate support for the agency among its constituents.

On the other hand, it is not clear whether the Board must always conduct its inquiries by formal proceeding, as provided in Article 39, or whether in appropriate circumstances it can gather evidence in private, without public notice, in the initial stages of a matter. While it is clearly necessary that a formal decision by the Board be preceded by a public notice and hearing, it would also seem to be necessary for the board to have the ability to make a preliminary determination that a formal proceeding is warranted without having to conduct that inquiry in public. The Board could be seriously hindered in obtaining evidence if all such activities must be conducted in public.

There is also some risk that the provisions in the law relating to the institution of Board proceedings and the participation by interested third parties could generate undue burdens upon the Board. The requirement that the Board must formally consider

every application for an investigation could occupy a significant part of the time and resources of the Board, though it need not do so. The Board should ensure that it establishes procedures for receiving and evaluating applications that require a minimal expenditure of resources, and that it retains the power to reject applications for an investigation on the grounds that the complaint does not allege a violation of the law or involves an insignificant matter.

There have been few decisions of the Board appealed to the courts. As time goes on and as the public gains experience under the new law, the number of appeals will probably increase, however. Court cases may be few, but they are important. If the agency's record of success in litigation is high, private parties will tend to avoid taking the agency to court, and the agency will have greater success in negotiating and enforcing administrative decisions. If its record in court is poor, the converse will result. Thus, the Board must give priority to litigation, preparing carefully for court proceedings.

Almost certainly, Estonian judges are not experienced in competition analysis. The Board could consider means of developing its relationship with the courts and of providing opportunities for the professional development of the judges in the discipline of competition policy.

Recommendations

- Consider whether the new law permits the Board to obtain evidence of possible violations in private, in advance of a decision to initiate formal enforcement proceedings. If it does not, seek authorisation for such powers.
- Develop procedures for handling applications for proceedings that minimise the resources needed to consider them. Apply fair but rigorous standards to these applications, so that the Board will not be preoccupied with many proceedings of dubious merit.
- Develop standards for the participation of third parties in proceedings. Limit eligibility for participation to those whose interests are directly affected by the conduct in

question in a manner consistent with the underlying purpose of the competition law.

- Work to develop a good relationship with the Estonian courts, consistent with proper legal ethics. Sponsor workshops and seminars on competition policy, to the extent that time and resources permit.

3.5 *Public Relations – Developing a Competition Culture*

In addition to making its proceedings accessible to the public, it is in the broader interests of the competition agency to educate the public about its work – to help consumers, the business community and other parts of government understand the rationale for competition enforcement and why it benefits them. There are a variety of means for doing so:

- Publish all substantive decisions of the Board.
- Publish annual reports describing the Board’s activities and important cases.
- Cultivate relations with the press; issue press releases announcing important decisions or cases.
- Make speeches or other public appearances at appropriate occasions.
- Sponsor seminars or conferences on competition policy for interested parties – lawyers, business people, consumer groups.
- Develop a page on the World Wide Web.
- Publish guidelines explaining the substantive analysis that the agency employs in specific types of matters, or outlining procedures that are followed by the agency.

Comment

The Board has made progress in some of these areas. It has published an informative brochure describing the Board and its work, and it has created a page on the World Wide Web. It will

begin publishing an annual report in 1999. The provisions in the new law providing for the publication of notices of proceedings and of final decisions of the Board will enhance the public awareness of the competition law and the work of the Board. In general, however, it appears that much can be done to enhance the development of a “competition culture” in Estonia.

Recommendations

- Consider expanding activities in all of the above areas as time and resources permit.

3.6 *Resources*

Comments and Recommendations

The Competition Board appears to have fared better than the competition agencies in some other transition countries in acquiring necessary resources. The total number of people employed by the Board has grown from 21 to 47 between 1996 and 1999. At the same time, the new law will create additional burdens on the staff . It is receiving and processing notifications of mergers and restrictive agreements for the first time. The new procedures for Board proceedings impose strict deadlines and more formality that will tax the Board’s resources. The new provisions of the law relating to natural monopolies and undertakings with exclusive rights and to state aids may have resource implications.

The Board’s employees are dedicated and hard working. It appears that the Board has some difficulty in retaining qualified people because of disparity in salaries. While it is unrealistic to expect that the Board can match the highest salary opportunities in the private sector, its salaries should at least be commensurate with those of similarly qualified people in other parts of government.

Until recently there had been an acute shortage of lawyers on the Board staff. The Board intends to add a few lawyers to the Legal Department, which was recently created. It is likely, however, that it will continue to be difficult to hire and retain

qualified lawyers, given the rigorous and lengthy course of study and preparation required for qualification as a practicing lawyer in Estonia and the disparity in salaries for lawyers between the private and public sectors. In the longer run, the Board can work within the government to encourage review of these standards, which may be too restrictive. In the short run, if resources can be found to hire and retain only a few lawyers, priority can be given to hiring and training qualified people as paralegals – assistants who can conduct most of the work required in litigation, thereby making the few lawyers more efficient.

While it is obvious that the Board would benefit from additional resources in some areas, this can probably be said of most government agencies in Estonia and elsewhere. Thus, the Board should aggressively seek additional resources where they are truly needed, but it must also constantly strive to be more efficient with what it already has. Measures for doing so include:

- Identifying and giving priority to the most significant substantive areas of enforcement, and within those areas, concentrating on the most significant cases and investigations.
- Streamlining procedures, to ensure against committing too many resources to the review of unnecessary notifications and unmeritorious applications for investigations, or engaging in lengthy and undisciplined hearings in which extraneous evidence and arguments are offered.
- Devising means of achieving effective relief from anticompetitive conduct other than through hearings and litigation, such as through voluntary agreements and negotiated settlements.

NOTES

1. The new law is attached as an appendix.
2. Articles 13-14.
3. Articles 4-5.
4. Articles 28-33.
5. Articles 6-7.
6. Articles 26-27.
7. Articles 19-24.
8. Articles 15-18.
9. Article 51(2) provides that applications relating to agreements that were in effect before the enactment of the new law must be submitted within six months of the effective date of the new law.
10. Division 5, Section 1.

COMPETITION ENFORCEMENT IN LATVIA

1. The Legal and Institutional Structure

1.1 *The Competition Law*

Latvia's current competition law was enacted in 1997, and took effect on January 1, 1998, replacing a competition law that was enacted in 1991.¹ The law creates a five-member Competition Council, one of whom is Chairman.² The Council adopts decisions under the law, and has the power to impose remedies and fines for violations. The law creates a Competition Bureau, which is empowered to conduct investigations and make recommendations to the Council.³ The substantive provisions of the law include prohibitions of restrictive agreements,⁴ abuse of dominance,⁵ anticompetitive mergers,⁶ unfair competition,⁷ and misleading advertising.⁸

A principal feature of the new law is its approximation to the competition law of the European Union, as required by the Europe Agreement between Latvia and the EU. Like Article 85 of the EC Treaty, the Latvian law on restrictive agreements, in terms similar to Article 85(3) of the EC Treaty, provides for the competition agency to exempt from the law's prohibitions certain economically beneficial agreements. The language of Article 17 of the Latvian law, prohibiting abuse of dominance, closely resembles Article 86 of the EC Treaty. The merger control regime in Latvia is unique in some respects, but it does provide for notification of certain mergers in advance of consummation, as do the competition laws of the EU and most other countries. Mergers that "prevent, restrict or distort competition" are prohibited by the law.⁹ In many respects, of course, the Latvian competition law contains provisions that are specifically suited to that country, particularly including procedural aspects of the law.

The Latvian Cabinet of Ministers has adopted certain regulations that implement aspects of the law. Regulation No. 444 establishes procedures for the conduct of investigations and hearings by the Competition Council. Regulation No. 37 provides the procedures for notifications of restrictive agreements under Article 15 of the law. Regulations No. 74 and 341 provide

for block exemptions from Article 15 of exclusive supply and purchase agreements and specialisation agreements, respectively. Regulation No. 73 establishes the merger notification rules.

1.2 *The Competition Agency*

The Competition Council consists of five members, who serve for a term of five years. The Cabinet of Ministers appoints the Council members upon the recommendation of the Minister of Economy. One member is replaced each year on a rotating basis.¹⁰ The duties of the Council include adopting decisions regarding violations of the law and imposing remedies therefor, submitting cases to court as provided by the law, reviewing and commenting on draft legislation (normative acts), participating in state property privatisation by reviewing proposed transactions and submitting proposals or opinions on them, and working with local governments in Latvia and with institutions in foreign countries on matters of competition policy.¹¹

The Competition Bureau is a unit of the Competition Council. It is managed by a Bureau Director and a Deputy Director, who have civil servant status. The Bureau conducts investigations of possible violations of the competition law and submits recommendations to the Council. It reviews notifications, draft legislation and proposed privatisation transactions and prepares opinions on these matters for the Council. It prepares cases for submission to the courts, and it has the power to conduct negotiations with enterprises for the purpose of terminating violations of the law.

Within the Bureau there are two **Analytic Divisions**, which conduct the substantive analysis of possible violations of the law. A regional office in **Rezekne** exists within one of the analytic divisions. Additional units in the Bureau are the **Information and Foreign Affairs Division**, the **Law Division**, and the **Administrative Service**. As of mid-1998 there were 30 employees in the Competition Bureau, 40 per cent of whom were economists, 29 per cent lawyers, 14 per cent engineers and 17 per cent other professions.

2. Substantive Enforcement

In this section the Council's enforcement of the substantive provisions of the competition law will be reviewed. Each area of substantive law (*e.g.*, abuse of dominance, restrictive agreements, mergers) will be discussed separately. Brief descriptions of representative cases will be included where appropriate. Comments and recommendations will also be provided at the end

of each section. Where available, data on enforcement activity are presented, but data for the years prior to 1998 are incomplete.

2.1 *The 1998 Reforms*

The new law is a departure from the old one in several respects. Under the old law the competition agency, then called the Antimonopoly Committee, was confronted with significant obstacles, and it had difficulty establishing an effective presence. Neither the competition law nor the Antimonopoly Committee were well known or understood among the public at large. The new law is a substantial improvement, providing the newly-created Competition Council with more independence than its predecessor had, and with expanded powers of enforcement. In general it can be said the Council has the legal tools that it needs to provide an effective competition policy in Latvia, but it faces significant challenges in using these tools effectively for the benefit of Latvian consumers. Some of those specific issues are discussed more fully in the sections below.

2.2 *Abuse of a Dominant Position*

Article 17 of the competition law contains a general prohibition of “abuse of a dominant position.” The Article also enumerates five types of conduct that can constitute an abuse, including refusal to contract with another party without objective justification, limiting production or distribution without objective justification, imposing conditions in a contract that are not related to the subject of the contract, imposing unfair prices or other terms or conditions, and discrimination against market participants. “Dominant position” is defined in Article 1(2) of the law as having a market share in excess of 40 per cent and having the ability, “in full or partial independence,” to prevent, restrict or distort competition in the market

Cases and investigations involving abuse of dominance are relatively numerous in Latvia. Of a total of 76 investigations in 1998, 23 involved abuse of dominance. The investigations arose in several sectors in the economy, tending to occur often in markets characterised by natural monopoly or an essential facility, including telecommunications, heat supply, electricity supply and transportation. Of the 23 abuse of dominance investigations initiated in 1998, 15 were resolved, while the remainder were still underway at year’s end. Of the 15 that were completed, 12 were closed because it was determined that no violation had occurred, and three were closed after it was determined that the illegal conduct had been terminated. In no case was a remedial order or fine imposed.

Comment

Abuse of dominance cases are frequent in Latvia, which is typical of transition countries. Monopolies or dominant positions are likely to be more common in the transition context, having been created by privatisation of former state-owned monopolies, and they tend to be more persistent, because entry by new competitors may be hindered by imperfectly functioning capital markets and scarcity of other important inputs, such as good distributors or retail outlets.

A significant proportion of the abuse of dominance cases in Latvia involved markets characterised by natural monopoly or essential facility. Again, this is not uncommon in the transition context, where regulation of network infrastructure industries may not yet be fully effective, giving rise to abuses involving access to these monopoly assets. As noted below, the scheme for regulation of natural monopolies is undergoing change in Latvia. At least until the regulatory bodies are fully functioning and perhaps beyond, it is likely that the Council will be confronted with many cases of this type.

Market definition and conditions of entry are often crucial to the dominance analysis. In smaller countries such as Latvia both issues often revolve around the availability of imports as substitutes for domestic products or services.

Some of the specific designations of abusive conduct in the competition law, such as “unfair pricing,” “limiting production,” or “unjustified refusal to deal with another undertaking,” are difficult to interpret and may be confused with legitimate competitive conduct (these are not unique to Latvia, however). Most competition experts consider that enforcement of abuse of dominance provisions should focus on exclusionary conduct – that which unnecessarily excludes actual or potential rivals from the market – rather than “exploitative” conduct – charging prices or imposing terms that appear to be unfair. The reason is that high prices may signal a business opportunity, and in developed economies it is expected that new entry will occur quickly in most markets in which prices appear to be above competitive levels. On the other hand, in transition countries imperfections in capital and other markets mean that competition authorities may not be able to count on swift entry. Thus, there is thus a better case in

transition and developing countries for occasional intervention against monopoly pricing and other exploitative practices, but such intervention should be used as infrequently as possible because it deters entry and thus delays transition.

Because its resources are so limited, the Competition Council will be able to successfully prosecute only a relatively few of these important cases each year. The fact that some of the cases involving abuse of dominance were successfully terminated by voluntary compliance by the dominant firms is a positive sign, in that scarce resources of the Council and the Bureau were conserved. The fact that no remedial orders were entered in these cases, however, may indicate that the Council has not been sufficiently aggressive in seeking effective relief. In the abuse of dominance area it is important that good cases be brought and that when a violation of the law is established, effective and meaningful relief be achieved.

Recommendations

- Prosecuting abuse of dominance cases will continue to be one of the most important activities of the Competition Council. Abuse of dominance cases are difficult and time consuming for the competition agency, and some of them are likely to be politically sensitive, as they may involve large and politically powerful enterprises. Thus, it is necessary that the Council select cases that are important to the Latvian economy, and prosecute them vigorously and carefully.
- Analysis of abuse of dominance cases requires careful attention to the issues of market definition and entry barriers. Actual and potential competition from foreign suppliers is almost always important in this analysis, especially in a relatively small country such as Latvia.
- Achieving effective relief is critical in abuse of dominance cases. Structural relief is almost always to be preferred to behavioural remedies, which require ongoing monitoring by the competition agency. The easiest and the most effective means of achieving structural relief is by measures that remove or ameliorate unnatural barriers to entry, rather than by attempts at breakup or restructuring of firms.

2.3 *Restrictive Agreements*

Article 15(1) of the competition law prohibits and renders void agreements between market participants that have as their object or effect the “prevention, restriction or distortion of competition.” The Article identifies certain specific types of conduct that fall within that definition, including agreement: on prices, tariffs or related terms or conditions; on production or output, or market division; on contractual conditions that are unrelated to the subject of a contract; on participation in bids or tenders except pursuant to a legitimate joint venture; on joint discriminatory conduct; and on eliminating a market participant or raising entry barriers.

Article 15(2) authorises the Council to permit an agreement prohibited by 15(1) if it contributes to improvements in production or distribution, thereby benefiting consumers, and if does not impose restrictions that are unrelated to the beneficial objectives and does not substantially restrict competition. Article 15(4) authorises the Cabinet of Ministers to issue regulations that exempt classes or groups of agreements (block exemptions), and that provide for notification of individual agreements to the Council, which could be exempted if they have minimal impact on competition (individual exemptions). To date, block exemptions have been issued for exclusive supply and distribution agreements (Regulation No. 74 of the Cabinet of Ministers), specialisation agreements (Cabinet of Ministers Regulation No. 341), research and development agreements and franchise agreements. The drafting of block exemptions is underway for technology transfers and motor vehicle distribution agreements.

Regulation No. 37 of the Cabinet of Ministers establishes the procedures for notification of agreements to the Competition Council. It details the information that must be included in the notification. Article 13 of the regulation is an important provision, exempting from the notification requirement certain types of agreements that are otherwise caught by Article 15(1) of the competition law. Agreements between farmers, farm co-operatives and unions relating to “production, storage, first treatment and sale of agricultural products” are exempt if they do not provide for the fixing of prices. Agreements whose participants collectively account for a share of five per cent or less in the market affected by the agreement are exempt from the notification requirement.

Vertical agreements in general may be exempt from the notification requirement, including resale price maintenance agreements. Joint research and development agreements may be exempt, and specialisation agreements involving parties having a collective market share of not more than 15 per cent may be exempt. The exemption for these three types of agreements, however,

becomes effective only upon issuance of regulations by the Cabinet of Ministers further elaborating on such exemptions, which regulations have not yet been issued. The exemptions in Article 13 of the regulation apply only to the obligation to notify. The Council may nevertheless find that such an agreement violates Article 15 and may issue remedial orders (but not fines) for such violations.¹²

Regulation No. 37 establishes the procedures for examination of notifications by the Council. It must complete its examination within 30 days, except that it may extend the period for up to five months in complex cases. Parties to the agreement have the right to submit additional information to the Council, as do interested third parties. Upon completion of its review the Council must issue a decision, stating whether the agreement is valid. If the Council determines that the agreement does not satisfy the requirements of Article 15(2) it may require changes in the agreement or it may declare it invalid, providing a written explanation of its reasons therefor.

In 1998 the Council conducted 15 investigations of restrictive agreements. One was resolved by negotiation, one by enforcement order, ten were closed because no violation was found and three investigations were ongoing at the end of the year. Two agreements were notified to the Council under Regulation No. 37. One was approved unconditionally and one was approved with conditions. It appears that few investigations of restrictive agreements have involved cartel conduct – price fixing, bid rigging or market allocation – which is the most competitively harmful type of restrictive agreement. The following is a recent case under Article 15.

Distribution of Oxygen Gas

An agreement between “AGA,” a Swedish-owned distributor of oxygen gas and “Dauteks,” a Latvian producer and distributor of oxygen gas, was notified to the Council. The agreement provided that Dauteks would lease to AGA for a period of three years Dauteks’ assets for gas distribution. As a result of the lease, Dauteks would exit the market for distribution of oxygen gas in Latvia, but it would continue as a producer. The agreement also provided that Dauteks would provide AGA’s requirements of gas for the period of the lease. After the lease, AGA would be the largest distributor of oxygen gas in Latvia, holding a market share of 64 per cent. Several other, smaller distributors also competed in this market. AGA planned to make some significant investments in the Dauteks facilities to improve operations.

Distribution of Oxygen Gas (continued)

The agreement had both horizontal – the combination of two gas distributors – and vertical – the requirements contract – aspects. The Council concluded that the horizontal effects would result in the creation of a dominant firm, but concluded that the economic benefits of the agreement were such that it should be approved under Article 15(2). The Council imposed certain obligations upon the parties, however: i) to refrain from imposing unfair prices or unnecessary services and from restricting consumers' freedom of choice; ii) for the term of the agreement to notify the Council of increases in the price of oxygen gas within 10 days of the increase and, once each quarter, notify the Council of the quantity of gas purchases by AGA from Dauteks; and iii) publish information on sources of gas other than AGA and Dauteks available to distributors and consumers.

Comment

The Latvian experience in restrictive agreements, and especially in cartel conduct, parallels that in many transition countries. To date the Council has prosecuted few if any cartel agreements, notwithstanding the likelihood that such agreements are common as carryovers from the period of central management. Acquiring evidence of an illegal agreement is difficult, especially when the subjects of the investigation are not co-operative. Given the unambiguous harm to consumers that results from cartel conduct, however, detection and prosecution of such agreements should have a high priority within the Council and the Bureau.

In non-cartel cases, issues of market definition, entry barriers and efficiencies under the standard in Article 15(2) will be important in the analysis. The Latvian market is relatively small, and most markets are likely to be highly concentrated if only existing sellers are considered. The possibility of competition from abroad, however, may be significant in many markets.

The oxygen gas case described above is an example of the difficulty of analysing the competitive effects of non-cartel conduct. If competitive restraints in such cases are ultimately judged not to be harmful on balance, it must be determined that the restraint is ancillary to legitimate, pro-competitive conduct,

and that it is no more restrictive than necessary to achieve the pro-competitive result. The remedial order in the oxygen gas case also highlights the difficulty of drafting such orders that affect ongoing conduct of the respondent, especially, as noted above in the abuse of dominance discussion, orders that purport to control prices in some fashion.

The Latvian system for notification and exemption of restrictive agreements closely parallels that of the European Union. This system offers, in the long run, the benefit of enhanced certainty for the business community about the legality of their agreements. The Council has made a good start through regulations 37, 74 and 444 in implementing the procedures required by the new law.

The Council must be careful not to impose burdensome notification requirements under Article 15. The EU experience has shown that a competition authority is ill-equipped to deal with large numbers of applications for exemptions. Indeed, the European Commission is currently considering substantial revisions of its exemption and notification procedures. Article 13 of Regulation 37 is useful in this regard, in excluding certain classes of agreements from the notification requirement. The Council has yet to complete the process of issuing regulations that would fully implement the article, however.

Recommendations

- Detection and prosecution of cartels should have a high priority within the Council. There are several facets to this effort:
 1. Educating consumers about the harm to them from cartels – higher prices and lower quality; encouraging consumers to co-operate with the Council's efforts to eliminate cartel activity by providing information about suspected illegal conduct.
 2. Educating businesspeople about their obligations under the competition law, encouraging voluntary compliance with its requirements; helping them also to realise that businesses are consumers too, and

therefore that they benefit from the elimination of cartels.

3. Becoming more aggressive in gathering evidence in situations of non-co-operation by investigation subjects; in particular, a) developing methods of obtaining potentially incriminating documentary evidence from the files of suspected cartel members, and b) encouraging co-operation by witnesses with information about cartel conduct by providing them with incentives, such as immunity from prosecution or reduced fines.
 4. Punishing cartel operators with significant fines, especially in situations where the activity was conducted in secret and the operators were aware of the illegality of their conduct.
- In considering non-cartel cases, first determine whether the conduct in question is actually anticompetitive. This requires defining the relevant market, analysing the market concentration and conditions of entry, and assessing the actual effects of the relevant conduct. If it does restrain competition in some fashion, consider whether the restraint is reasonably related to some pro-competitive benefit resulting from the agreement, and is no more restrictive than necessary to achieve the beneficial results.
 - Complete the process of promulgating block exemptions under Article 15(4) and implementing regulations under Article 13 of Regulation 37. Avoid, as much as possible, the implementation of unnecessary and burdensome notification and information procedures relating to exemptions.

2.4 Mergers

Articles 19-21 of the competition law establish a premerger notification system. Mergers in which the parties have combined turnover in Latvia of 25 million lats (LVL) and at least one of the parties is in a dominant position in a relevant market must be notified to the Council. The Council must respond to the notification in some fashion within 60 days of receiving it or the

merger is deemed to be permitted. If the Council finds that the effect of the merger may be to “prevent, restrict or distort competition” it must disapprove the transaction or approve it subject to specified conditions. The Council may also impose the same remedies on mergers that are not subject to the notification requirement but which have the statutory anticompetitive effects.

Cabinet of Ministers Regulation No. 73 establishes procedures for the notification and examination of mergers pursuant to the law. The regulation defines certain terms, including “related enterprises” and “turnover.” It establishes certain exemptions from the notification requirement and specifies the information that must be supplied in the notification. Article 12 of the regulation sets forth relevant criteria for the Council in assessing the effect of the merger on competition. The criteria include: consideration of the market structure in Latvia and existing or future competition from foreign enterprises; entry barriers; demand and supply trends in the market; reactions of consumers; development of technical and economic progress; the situation of the participants in export markets; and the potential benefits of the merger to consumers and Latvian society as a whole.

Under the procedures established in the regulation, the Council must inform the merging parties within 30 days of the notification whether the transaction will be examined according to the regulation. If the Council determines that the merger does not have the anticompetitive effects specified in the law it shall enact a decision to that effect and notify the parties. If the Council determines preliminarily that the merger constitutes a “serious threat to competition” it shall enact a preliminary decision to forbid the merger or to allow it subject to certain terms. The merging parties, and interested third parties, then may submit additional information to the Council, which then makes a final decision. The Council applies the same procedures to mergers that have not been notified.

In 1998, seven mergers were notified to the Council. Of these, six were approved as not being significantly anticompetitive, one was resolved satisfactorily through voluntary agreement by the parties and one investigation was in progress at the end of the year. No mergers were disapproved or subjected to mandatory modifications of their terms.

Stevedoring Services in the Port of Ventspils

The notification of the merger of two enterprises that performed stevedoring services in the Latvian port of Ventspils was notified to the Antimonopoly Committee in 1997. The Competition Council reviewed the transaction under the 1998 law, however, according to the transition procedures provided in the new law.

The product market was determined to be stevedoring services performed on “general cargo,” which included containerised cargoes. Most of the cargoes shipped through Latvian ports were transhipped to and from inland points outside of Latvia. The decision in this case turned on the definition of the geographic market. The merging parties had a very large share of stevedoring services in Ventspils, and a share of 27 per cent of such services at the three Latvian ports, which included Riga and Liepaja. It was determined, however, that the relevant geographic market in this case was the east coast of the Baltic Sea, which included ports in Latvia, Lithuania, Estonia, Kaliningrad, Saint Petersburg and Helsinki. Shippers were generally indifferent as to which of these Baltic ports they used, and their decision was based on the factors of price, speed and safety. Thus, in this broader market, the merged enterprise did not possess any degree of market power, and the merger was permitted.

Comment

The Council has taken action against only a few mergers to date, but it is true in every country that most mergers are not competitively harmful. Certainly it is true that merger analysis in each country must take into account the specific characteristics of local markets. In small countries, for example, imports are usually relatively more important than in larger countries. Absent significant restraints on imports, mergers of domestic firms may seldom be anticompetitive in these countries. The stevedoring services case described above illustrates this point. The Board correctly determined that the relevant geographic market included ports in neighboring Baltic countries. Of course, in some cases the market may be limited to domestic suppliers, especially in markets involving nontradable goods or services.

There are other aspects of mergers that are likely to be especially significant in transition countries. Domestic assets that remain from the period of central planning will be relatively inefficient. Some restructuring of these assets, especially in the industrial sector, will almost certainly be necessary. Efficiency considerations will be important - possibly paramount - in these cases. These mergers will not

be anticompetitive, however, if barriers to entry, especially by foreign producers, are not high. If, on the other hand, domestic industries are restructured and concentrated and competitive imports are artificially excluded by government policies, consumers could be harmed by these transactions.

Another issue that can confront competition authorities in transition countries is understanding the real effect of complex mergers involving novel corporate forms and transactions, combined with participation by several entities. Difficult and arcane concepts of “control,” “decisive influence,” “person” and “group of persons” may affect the analysis of these cases. These concepts have different meanings in different countries, depending on national laws and traditions. While the new law and Regulation No. 73 define some of these terms, it will take some time and experience for the Council to develop expertise in this area.

An important consideration for competition authorities in small countries is the need to avoid surrendering too much of their limited resources to merger control. In the first instance, this means devising a notification scheme that does not produce an unnecessarily high number of notifications. Merely having to read a large number of notifications can siphon off important resources that would be more profitably devoted to other pursuits. Investigations of even a small number of mergers can occupy much more time and effort. Second, it means adapting one’s merger policies to the realities of the domestic market – learning to recognise and prosecute only those few mergers that truly threaten the welfare of the nation’s consumers.

The Council has made a good start in implementing a merger control regime by adopting Regulation No. 73. The notification thresholds in the competition law itself may present some difficulty, however. The size threshold, which is defined as total turnover in Latvia of LVL 25 000 000, appears to be a reasonable limit, although actual experience will determine whether that is true. The additional requirement that one of the firms be dominant in a relevant market, however, could create problems, possibly for two reasons. First, mergers of non-dominant firms can be competitively harmful. Second, the existence of dominance is a subjective determination, which can lead to inaccuracies in determining whether notification is necessary under the law. (It is not recommended that a list, or “register” of dominant firms be published, as is done in Russia.

Such a list would inevitably be inaccurate, and would itself require scarce resources to create and maintain.) In general it is thought that only objective standards, such as turnover or total assets, are proper as criteria for notification of mergers in the first instance.

Recommendations

- Monitor the trends in merger notification procedures; adjust the notification thresholds as necessary to minimise unnecessary notifications. Evaluate the appropriateness of the “dominance” requirement for notification, and if inappropriate, consider steps to amend that part of the competition law.
- Develop procedures for expedited review and decision making on notified mergers, with a view toward conserving the Council’s limited resources.
- Evaluate the competitive effects of mergers according to actual conditions in Latvian markets. Give appropriate consideration to actual or potential competition from sources outside the country.

2.5 *Anticompetitive Activities of Governments*

The competition laws of several transition countries directly prohibit anticompetitive conduct by executive bodies of state and local government. These laws provide for direct action by the competition agency against the offending government body and for the application of the usual sanctions against such conduct. In enforcing these provisions the competition agency is limited by practical realities; it may not have sufficient political power to confront directly another body of government, especially a part of the national government, such as a ministry. Still, in several transition countries there have been cases or investigations instituted under these provisions. More often than not these cases are resolved not by mandatory sanctions or orders, but by negotiations that lead to a voluntary solution.

This appears to have been the experience in Latvia. Article 3(2) states that state and local government institutions have “the obligation to promote the development of free and fair competition and to not allow unfair competition, when taking decisions within the realm of their competence.” Article 4(1), on the other hand, states that the competition law applies to state and local

government institutions “only insofar as they act as market participants in private law relationships.” These two provisions can be interpreted as applying the law fully to entrepreneurial conduct of government bodies, and imposing a more general obligation upon governments to promote competition in the course of their official duties. In any case, there are examples of the competition agency acting informally to eliminate anticompetitive conduct by government agencies.

School Textbooks

Textbooks for use in the public schools in Latvia must come from an approved list of books published by the Ministry of Education. There were as many as 22 book publishers in Latvia, but more than 67 per cent of the approved books were published by one company, the ABC Company. Moreover, ABC’s prices were found to be higher than those of other publishers by as much as 20 per cent. The Antimonopoly Committee began an investigation of the situation and discovered that the Education Ministry had entered into an exclusive arrangement with a predecessor company of ABC, which ABC now controlled. The Antimonopoly Committee determined that ABC held a dominant position in school textbooks which it was exploiting by charging higher prices. The Committee entered into negotiations with the Ministry to bring about changes in the textbook selection process that would introduce more competition, which would result in lower prices for textbooks.

Comment

There is little doubt that anticompetitive regulations and procedures of state and local governments continue to impede economic progress in Latvia. Interviews with representatives of the private sector indicate that this is a primary concern within the Latvian business community. While the competition law apparently does not permit the Council to proceed directly against such restraints, the requirement of Article 3(2) noted above, that government institutions must “promote the development of free and fair competition” when taking official decisions, authorises the Council to be aggressive in attempting to resolve competitive problems with government agencies on a voluntary basis.

The elimination of improper regulation or discrimination by government bodies is one of the most important missions of the Council. Freeing the business community from unnecessary

government restraints will make markets in Latvia more competitive and more efficient, which will yield significant benefits for consumers. Pursuing such remedies requires skill and diplomacy on the part of the competition agency, however, as it may be dealing with bodies that are relatively more powerful than the competition agency within government.

Recommendations

- Place strong emphasis upon elimination of anticompetitive restraints by government bodies. Make the business community an ally in this effort.
- Approach offending government bodies judiciously. Enlist their co-operation, rather than opposition, in this program.
- When there are successes, use available means to inform the public of them, thereby strengthening support for the work of the Council and for competition policy.

2.6 *Unfair Competition*

Article 22 of the competition act prohibits unfair competition, which is defined generally as conduct which “violates normative acts or the fair practice of business activity and has created, or could create, the prevention, restriction or distortion of competition.” The Article lists specific acts of unfair competition, which include: misuse or unlawful duplication of the name or marks of another business entity; the dissemination of false or misleading information about another entity, its products, prices or employees; the acquisition, use or distribution of commercial secrets of another business entity; and the use of threats or bribery against an employee of another business entity.

Investigations of unfair competition were by a small margin the most numerous type of investigation in 1998. Twenty-four investigations were initiated; 12 were closed after a determination that no violation had occurred; three were resolved satisfactorily by negotiation; and in four cases enforcement orders were entered.

Comment

Protection of intellectual property rights and against untruthful and misleading disparagement of a competitor are important to the proper functioning of free markets. In countries whose economies have been recently liberalised, it is not uncommon for the competition agency to institute a relatively large number of cases of unfair competition, even when the practices do not have an impact on the economy as a whole. As markets mature, however, the number of such cases brought by the competition agency tends to decline, for at least two reasons. First, businesses become more knowledgeable about what the law permits in this area. Second, and possibly more important, in developed economies there is generally easier access to courts for resolution of private disputes, and businesses tend to resort to such remedies directly in cases of unfair competition. It is not clear whether in Latvia entities have the ability to bring their own actions in court for acts of unfair competition. The Council could encourage the development of such a remedy as a means of conserving its own resources for prosecution of broader anticompetitive conduct.

Recommendations

- Continue to prosecute important cases of unfair competition, especially where significant issues of protection of intellectual property are involved, but to conserve important resources, encourage businesses to resolve their disputes privately, where possible.
- Use the authority of the Council to achieve voluntary compliance when it appears that violations have occurred, again to conserve resources.

2.7 *Consumer Protection*

The Council does not have the responsibility for consumer protection. That function is provided by the Consumer Rights Protection Center under the Ministry of Economy.

2.8 *State Aids*

The Europe Agreement between Latvia and the European Union, as well as other free trade agreements to which Latvia is a party, place significant restrictions on the provision of state aids by government entities. In 1997 the Cabinet of Ministers adopted a regulation for the purpose of implementing the requirements of these agreements, and in 1998 the regulation was replaced by a law on control of state aid. Under the law, a State Aid Surveillance Commission was created for the purpose of evaluating state aid projects and preparing an inventory of such projects.

The Commission is an independent body, not a part of any government ministry. It has 13 members, including a representative of the Competition Council. The Commission has powers to require state and local institutions to submit information relevant to possible state aids. Applications for state aid projects are submitted to the Commission, which can order elimination or restitution of projects that do not conform to Latvia's international obligations. The Commission is responsible for publishing an annual survey of state aids in Latvia. Surveys have been published for 1997 and 1998. The Competition Council is an active participant on the State Aid Surveillance Commission. The Council Chairman reviews all applications and submits comments as appropriate.

Comment

State aids can have important implications for competition policy. Improper and indiscriminate granting of state aids can result in significant market distortions, impeding competition and harming consumers. The competition agency should have an advisory role in this area, to ensure that markets function as free from government interference as possible. On the other hand, direct involvement in the state aid granting and monitoring functions could impose a heavy burden on the resources of the Competition Council. The role of the Council should be limited to the review of applications and decisions of the State Aid Surveillance Commission to ensure that they properly incorporate relevant principles of competition policy.

Recommendations

- Continue to participate as an advisor in the State Aid Surveillance Commission at a level consistent with the limited resources of the Competition Council. Review

state aid applications for the purpose of ensuring, to the maximum extent possible within overall government policy, that markets remain competitive and free from unnecessary government interference.

2.9 *Competition Advocacy*

The competition law authorises the Council to participate actively as competition advocate in the legislative and regulatory spheres of government. Articles 7 and 8 provide that the Council may review and provide opinions on legislation which has a direct or indirect impact on competition, and it may participate in privatisation and demonopolisation efforts of the state by submitting opinions in specific matters regarding the protection and development of competition.

The scheme for regulation of natural monopolies is still in the process of reformation in Latvia. Currently there exist national regulatory bodies for energy and telecommunications, and municipalities exercise regulatory functions in other sectors. Tariffs for telecommunications and postal services are currently regulated by the Telecommunications Tariff Council. A recently enacted energy law placed supervision of that sector under two inspectorates of the Ministry of Economic Affairs. Deregulation and demonopolisation of these sectors, especially telecommunications, is under active consideration. It is proposed that a single body be formed to conduct all regulation at the national level, but that proposal is still under discussion.

In its relatively brief existence the Competition Council has participated as competition advocate in a few matters, although its involvement is apparently not widespread. The Council has made a presentation to the Cabinet of Ministers on the subject of deregulation of telecommunications services, and it provides input into the decisions of the Telecommunications Tariff Council.

Comment

The Competition Council currently participates in a limited way as competition advocate in legislative and regulatory affairs. Both time and resources are required to develop expertise and credibility in competition advocacy, and so it could be expected that the newly reorganised Council would proceed carefully in this area. As noted above in connection with removal of anticompetitive government restraints, however, the potential

benefits to consumers from participation by the competition agency in legislative and regulatory affairs are potentially great. There are few areas in an economy in which competition is not possible, even where conditions favouring natural monopolies are thought to exist. Where regulation is necessary, some forms of regulation are more effective than others in promoting efficiency. The competition agency can be a powerful voice on behalf of consumers in these situations.

The Competition Council faces a significant challenge in this important area. It has limited resources, so it must carefully select the matters in which it will participate. Perhaps most important, its independence within the government, or lack thereof (discussed further below), will control the extent to which it can be effective as competition advocate.

Recommendations

- Place a growing emphasis on the Council’s role as competition advocate, consistent with available resources and within other priorities facing the Council. Select the matters in which it will participate carefully, with an eye toward the impact of the decision under consideration on consumers.
- Prepare the Council’s competition advocacy comments with care, striving for accuracy, to enhance the Council’s credibility in this arena. Where the Council lacks expertise in a technical area, enlist the aid of interested and sympathetic outsiders who have the requisite knowledge, such as academics or business groups.

3. Institutional Issues

3.1 Independence of the Council Within the Government

Under the 1998 law the Competition Council is created as a separate state institution, whose activities are financed by the state budget. It is established as a legal person, with a seal, and is not part of a government ministry. Council members are nominated by the Minister of Economy and approved by the Cabinet of Ministers. They serve for terms of five years. With respect to removal of Council members, the law states only that “The Cabinet of

Ministers may remove a member of the Competition Council before the end of his/her term.”¹³ In another important provision of the law, however, it is stated:

The Cabinet of Ministers or the Minister of Economy shall not issue any instructions to the Competition Council Chairman and to the Competition Council members regarding the initiation of an investigation for a particular matter or regarding the manner in which a particular investigation shall be undertaken or a particular decision shall be adopted.¹⁴

Comment

It is generally accepted within the international competition community that a national competition authority should operate with as much independence from the rest of the government as possible. Its decisions, like those of regulatory agencies, may affect the interests of large and powerful businesses, which may have strong political influence with the government. The competition agency should be free of such influence to the extent possible. Thus, it is often recommended that the competition agency be created as a separate entity that is not a part of any other government ministry. The agency would be answerable directly to the legislature for its funding, and the head of the agency or the members of the commission would be appointed by the president or other chief executive, subject to removal only for gross negligence, corruption or clear inability to perform the functions of the office.

Such a structure may be the ideal, however, and does not exist in many countries. The new Latvian law does, by its terms, provide the Competition Council with a substantial degree of autonomy. The Council is created as a separate body, not part of a ministry. The relatively long term (five years) for Council members promotes their independence, although this feature may be more than offset by the apparent lack of restrictions on the removal of Council members by the Cabinet of Ministers. A potentially important guarantee of independence is found in Article 9(3), quoted above, which forbids direct interference by the ministers in the decisions of the Council.

Perhaps as important as these formal, statutory guarantees of independence, a significant degree of “informal” independence

can be achieved over time by the Council, by means of measured, impartial and transparent decision making, coupled with the building of public understanding and support for the Council's mission. The achievement of such independence should be a long term goal of the Council.

3.2 *Investigative Powers*

Article 8(1)(3) of the competition law authorises the Competition Council to obtain information “necessary for execution of the tasks set forth in this law” from any physical or legal person, as well as from state and local government institutions. It can require the submission of information containing commercial secrets, though it must carefully preserve the confidentiality of such information. It can require the production of written or oral explanations from relevant individuals. Article 13(1)(2) provides similar powers to the Competition Bureau. The Bureau can also inspect documents at a person's place of business and obtain copies thereof. Article 16 of Regulation No. 444 elaborates further on these powers, authorising Council employees to visit a business enterprise and have access to and make copies of documents and records on the premises, and to take oral and written explanations from officials and employees on the premises.

It appears that the Council and the Bureau have used these powers sparingly to date. Most evidence is taken voluntarily from relevant parties. Bureau employees have made visits to enterprises, however, and have conducted interviews with parties who possessed relevant information. When investigating possible restrictive agreements, especially cartel conduct, the Bureau has found it difficult to obtain direct evidence of an agreement.

Comment

It appears that the Council and the Bureau have adequate information gathering powers under the competition law. To date their powers to compel the production of information have been used infrequently, however. If the Bureau is to be successful in enforcing the law it will need to be more aggressive in its investigation techniques. The Bureau must gain the confidence of the business community that its powers will be used fairly, however. Demands for information should not be issued indiscriminately, generating heavy burdens of compliance on investigative subjects and corresponding burdens on the Bureau of reviewing the information. Finally,

the Bureau must be firm in enforcing these new powers, vigorously prosecuting intentional untruthfulness or willful failure to comply with information demands.

Recommendations

- Employ the new information powers selectively and fairly.
 1. Continue to use voluntary means of investigation whenever possible, especially when seeking information from non-subjects – “third parties” – in an investigation.
 2. Conduct unannounced “dawn raids” and searches of business premises sparingly, for example only when serious, ongoing anticompetitive conduct is suspected, and co-operation by the subjects of the investigation is unlikely.
 3. Perfect techniques of requesting and reviewing relevant business documents from relevant parties. Documents written in the regular course of business often are the best source of evidence for use in defining markets and assessing the competitive effects of relevant conduct.
 4. Be willing to discuss demands for information with recipients with the purpose of meeting their legitimate concerns about burdens of production.
 5. Institute rigorous procedures for safeguarding the confidentiality of information that is provided, as the law requires. Take pains to assure the providers of information, both voluntary and involuntary, that the confidentiality of their information will be maintained.
- Be prepared to prosecute economic subjects who intentionally provide false information or willfully withhold information specified in a demand. Seek strong sanctions for such conduct.

3.3 *Enforcement and Sanctioning Powers*

Article 8 of the competition law contains general language relating to the remedial and punishment powers of the Council. Subsections 6 and 7 of the Article provide that

the Council may “adopt decisions about the termination of violations of this law and its requirements,” and may “adopt decisions about the assessment of fines for violations within the limits set forth in this law.”

Article 16 provides for remedies for unlawful restrictive agreements, which are prohibited by Article 15. The Council may impose a fine of up to five per cent of an enterprise’s turnover for the previous year for a violation, except that it may fine up to 10 per cent of turnover for conduct that violates subparagraphs 1-4 of Article 15. This conduct includes agreements on prices, on restriction or control of production, markets, technical development or investments, on market division, or on conditions that are unrelated to the underlying subject of a contract. The Council may also impose an order requiring the violator to “renew the situation which existed before the violation.” When a party fails to comply with a prescription of the Council under Article 16, the Council may impose a fine up to the limits described above.

Article 18 contains similar, but not identical remedies for abuses of dominance, which are prohibited by Article 17. A maximum fine of five per cent of the previous year’s turnover may be imposed. The Council may impose remedial orders as under Article 16. When a party fails to comply with the prescriptions of the Council under Article 18, the Council may impose a fine of up to 10 per cent of the previous year’s turnover.

With respect to anticompetitive mergers, as noted in **section 2.4** the Council may issue an order prohibiting consummation of a merger found to violate Article 20 or approving it subject to specified modifications. In addition, the Council may impose a fine of up to LVL 1 000 per day in situations in which a merger has been consummated without notification as required by Article 19, or in which a merger is consummated in violation of an order of the Council under Article 20.

Articles 32-40 of Regulation No. 444 elaborate the relevant factors for the consideration by the Council in imposing a fine. They include the seriousness of the violation, the magnitude of the harm that is caused, the role of each violator in the breach, and the extent of co-operation by the violator in the investigation and prosecution.

Article 8(2) of the competition law contains a potentially important provision that may impact the ability of the Council to impose remedial orders in the event of a violation. It requires the Council, “before adopting a decision, to attempt to achieve the termination of a violation through negotiations with the market participant(s) involved in the violation.” Article 23 of Regulation No. 444 contains a similar provision. Article 27 of the regulation states that if negotiations are successful and the violation and its consequences are eliminated, “the Council shall make a decision on termination of the case.” This language may mean that the Council is unable issue a remedial order if the unlawful conduct otherwise has been terminated and the status quo restored. With respect to the imposition of fines, on the other hand, Article 41 of Regulation 444 explicitly provides that fines may be imposed notwithstanding that the violation has ceased.

Article 18 provides that the Council may order the payment of illegally-obtained profits resulting from an abuse of dominance (Article 17) to the state budget. There is no comparable provision relating to restrictive agreements (Articles 15 and 16), but Article 31.2 of Regulation 444 provides that the Council may impose such an order relating to the profits resulting from all violations. Otherwise, however, the competition law does not deal with the recovery by private persons of damages suffered as a result of a violation of the law. It may be possible for private entities to pursue such remedies through the civil code. Where it is possible to bring such suits and resolve them fairly, the right of private action is an important supplement to government enforcement. The risk of large damage liability is an additional deterrent to those who would violate the law.

Comment

It appears that, on the whole, the Latvian law provides the Council with adequate sanctions for enforcing the law, although the requirement that the Council first attempt to resolve a violation through negotiation in all cases raises a potential problem in two respects. First, if the Council must always negotiate before imposing mandatory sanctions, the possibility arises for harmful delays before necessary relief is obtained. The negotiations may be extended, and indeed the violator may have an incentive to delay during this period. During the delay the harm from the violation would continue. Moreover, the competition law does not contain any provisions permitting the Council to obtain or impose “emergency” relief in cases where it is warranted. It may be that such a remedy exists under the civil code, however.

Second, as noted above, these provisions requiring preliminary negotiations raise a question regarding whether the Council can impose remedial orders in cases where the unlawful conduct has been ended. It would seem that in some circumstances such an order would be necessary to prevent resumption of the violation after the case is closed. The experience under the new law is limited, but to date few cases have resulted in mandatory remedies or sanctions imposed by the Council. As a general proposition, the termination of a violation voluntarily through negotiation is beneficial, as it conserves resources, but there may be cases in which a mandatory order is also necessary. Perhaps it is possible under the law to seek agreement on such an order in the negotiation process, and if such an agreement is not reached, to impose the order unilaterally.

In general, it may be useful for the Council to undertake a review of remedial orders that have been entered in previous abuse of dominance and restrictive agreement cases. Have they succeeded in eliminating the unlawful conduct and restoring competition to the market? A simple order to cease a violation may not be sufficient in some circumstances. Some “fencing in” provisions may also be in order, but it is also important that such an order not be too intrusive and ultimately anticompetitive itself.

The maximum fine of five per cent of annual gross revenues for most substantive violations (10 per cent for some “hard core” restrictive agreements) appears to be sufficiently large. Apparently there have been no fines imposed to date under the new law. This is not necessarily an indication that the Council has not been sufficiently aggressive with this sanctioning power. Fines are most appropriate for “hard core” violations, such as price fixing, and some egregious abuses of dominance. In such cases they must be sufficiently large to create a deterrent to future violations. As noted above in **section 2.3**, it is hoped that the Council will become more aggressive in prosecuting these violations. The threat of heavy fines has a beneficial effect in such cases. It can encourage individuals and enterprises to co-operate in investigations and cases to achieve a reduction or elimination of their liability.

As noted above the Council may impose a fine of up to LVL 1 000 per day for each day in which merging parties are in violation of the merger notification requirements of the law.

The level of this fine is relatively low compared to maximum fines for such conduct in other countries with merger notification laws. Fines for such violations must be sufficiently severe to deter willful violations of the law. The Council may wish to monitor compliance with the merger notification requirements of the law, and if violations are widespread, seek authority to increase the maximum fine.

Recommendations

- Resolve the uncertainty regarding the Council’s ability to issue remedial orders in cases where the unlawful conduct has been voluntarily terminated. Make an assessment of whether, in practice, the requirement of prior negotiation unduly hampers the ability of the Council to achieve effective relief, and if it does, attempt to resolve the problem, if necessary by seeking an amendment of the law.
- Consider the effectiveness of prohibitions and remedial orders in abuse of dominance and restrictive agreement cases. Attempt to fashion orders that are limited to eliminating the illegal conduct and its effects, are easy to administer and limited in duration.
- Impose increasingly large fines for engaging in cartel conduct and for willful disobedience of the Council’s orders or the willful submission of false or incomplete information.
- Employ the Council’s discretionary powers to fine as a tool in gaining co-operation in investigations and cases, especially those involving cartel conduct.
- Monitor compliance with the merger notification requirements of the law, and if violations are widespread, seek authority to impose higher fines for violations.
- Explore the opportunities under Latvian law for private damage actions. If such actions are possible, work to educate the business and legal communities about the opportunities in that regard.

3.4 *Administrative Procedures and Appeals*

Regulation No. 144 sets out procedures for investigations and cases conducted by the Council. Investigations may be initiated either by the Council *ex officio* or upon receipt of an application by a person who has a “vested interest” in the possible violation. “Vested interest” is defined as participating in a possible violation of the competition law or as having suffered (or being likely to suffer) losses resulting from the alleged violation. An investigation may also be initiated upon the request of another state body of government. The Council must inform an applicant of its decision on whether to begin an investigation within one month of receiving the application. It may provide an applicant with additional time, not to exceed six months, to submit additional information in support of the application.

Regulation 444 provides that upon considering the information that has been submitted to it the Council may decide to terminate the investigation because no violation has been established, to continue the investigation, or to state that a breach has occurred, which it must do in writing to the offending party.¹⁵ If it has determined that a breach has occurred, it must attempt to resolve elimination of the breach and its effects through negotiation, as discussed above. If the negotiations are not successful, the Council must issue a notice to the offending party describing the alleged violation in detail and providing an additional period, not shorter than one month, for the party to respond with additional evidence or arguments.¹⁶ Third parties with a vested interest in the proceedings also have the opportunity to present evidence. After consideration of the additional evidence, if the parties have not eliminated the breach as provided in Article 27 the Council may enter an appropriate remedial order and/or impose a fine.

The competition law provides that appeals from decisions of the Council may be taken in accordance with the procedures set forth in normative acts.¹⁷ There have been no appeals of decisions under the new law. Only a few cases were appealed under the prior law.

Comment

The procedures under the new law provide sufficient opportunity for accused parties and interested third parties to present evidence and to be heard in Council proceedings. It is important that the Council’s work be transparent. Transparency builds confidence in the business and consumer communities in the integrity of the agency and helps to generate support for the agency among its constituents.

There is some risk that the provisions relating to the institution of investigations and the participation by interested parties in Council proceedings could generate undue burdens upon the Council. The requirement that the Council must formally consider every application for an investigation could occupy a significant part of the time and resources of the Council and the Bureau, though it need not do so. The Council should ensure that it establishes procedures for receiving and evaluating applications that require a minimal expenditure of resources, and that it retains the power to reject applications for an investigation on the grounds that the complaint does not allege a violation of the law or involves an insignificant matter.

There have been few decisions of the Council appealed to the courts. As time goes on and as the public gains experience under the new law, the number of appeals will probably increase, however. Court cases may be few, but they are important. If the agency's record of success in litigation is high, private parties will tend to avoid taking the agency to court, and the agency will have greater success in negotiating and enforcing administrative decisions. If its record in court is poor, the converse will result. Thus, the Council must give priority to litigation, preparing carefully for court proceedings.

Almost certainly, Latvian judges are not experienced in competition analysis. The Council could consider means of developing its relationship with the courts and of providing opportunities for the professional development of the judges in the discipline of competition policy.

Recommendations

- Develop procedures for handling applications for investigations that minimise the resources needed to consider them. Apply fair but rigorous standards to these applications, so that the Bureau and the Council will not be preoccupied with many investigations of dubious merit.
- Develop standards and procedures for the efficient conduct of hearings and proceedings. Avoid situations in which third parties effectively gain control of a hearing, unnecessarily prolonging it and producing irrelevant, voluminous evidence or arguments.

- Work to develop a good relationship with the Latvian courts, consistent with proper legal ethics. Sponsor workshops and seminars on competition policy, to the extent that time and resources permit.

3.5 *Public Relations – Developing a Competition Culture*

In addition to making its proceedings accessible to the public, it is in the broader interests of the competition agency to educate the public about its work – to help consumers, the business community and other parts of government understand the rationale for competition enforcement and why it benefits them. There are a variety of means for doing so:

- Publish all substantive decisions of the Council.
- Publish annual reports describing the agency’s activities and important cases.
- Cultivate relations with the press; issue press releases announcing important decisions or cases.
- Make speeches or other public appearances at appropriate occasions.
- Sponsor seminars or conferences on competition policy for interested parties – lawyers, business people, consumer groups.
- Develop a page on the World Wide Web.
- Publish guidelines explaining the substantive analysis that the agency employs in specific types of matters, or outlining procedures that are followed by the agency.

Comment

The implementation of the new law and the reorganisation of the Council have left it with little time or opportunity to develop its relationship with other constituencies in Latvia. In one respect the Council has made significant strides in a brief period in this area – the promulgation of regulations that

amplify and implement the law. In general, however, it appears that the competition law is not well known or understood among the public, the business community or elsewhere in government. A “competition culture” is not created quickly, but without it, the work of the competition agency will not be effective. As time and resources permit, the Council should undertake to educate others on the importance of an effective competition policy and their role in it.

Recommendations

- Consider undertaking as many of the activities listed above as resources permit.

3.6 *Resources*

Comments and Recommendations

Resource issues have come up in several places in the discussions above. It is obvious that the Council and the Bureau require more resources than they have in some areas. This can probably be said, however, of many government agencies in Latvia and elsewhere. While the Council should aggressively seek additional resources where they are truly needed, it must also constantly strive to be more efficient with what it already has.

The staff of the Competition Bureau are dedicated, and they work hard. Many are inexperienced, however. Some of the positions are currently held by students. It appears that in the recent past the employee turnover in the Bureau has been high, although that may be changing with the new law and the reorganisation of the agency. A priority of the Council should be to find ways to attract and retain qualified people. Salary levels are obviously an important, but not the only, factor in this regard. While the Council cannot hope to be competitive with the private sector in salaries, its salaries should at least be equal to those available elsewhere in the government for people with comparable qualifications. It appears that this is not the case at present, and the Council should seek to redress this problem.

In other respects, the Council must strive to improve efficiency where possible. Measures for doing so include:

- Identifying and giving priority to the most significant substantive areas of enforcement, and within those areas, concentrating on the most significant cases and investigations.
- Streamlining procedures, to ensure against committing too many resources to the review of unnecessary notifications and unmeritorious applications for investigations, or engaging in lengthy and undisciplined hearings in which extraneous evidence and arguments are offered.
- Devising means of achieving effective relief from anticompetitive conduct other than through hearings and litigation, such as through voluntary agreements and negotiated settlements.

NOTES

1. The new law is attached hereto as an appendix.
2. Articles 5-10.
3. Articles 11-13
4. Article 15.
5. Article 17.
6. Article 19.
7. Article 22.
8. Article 23.
9. In contrast, the substantive standard in the EC Merger Regulation is “create or strengthen a dominant position” resulting in a significant impediment to competition. Regulation No. 4064/89, Article 2.
10. Articles 5-6.
11. Articles 7-8.
12. The *de minimus* market share standards in Article 13 of the regulation are subject to an important qualification, however. Article 14 provides that if after two years of the effective date of the agreement the relevant market share has increased by more than 10 per cent, the agreement must be notified.
13. Article 6(3).
14. Article 9(3).
15. Article 20.
16. Article 24.
17. Articles 9(5), 16(6), 18(5) and 21(5).

COMPETITION ENFORCEMENT IN LITHUANIA

1. The Legal and Institutional Structure

1.1 *The Competition Law*

Lithuania first enacted a competition law in 1992, but that law was replaced by a new law which became effective on 2 April 1999. Thus, competition policy in the country is in a state of flux, as the competition agency and its constituencies – the public, the business community and the government – begin to adapt to the new regime. This report of necessity focuses on the country's experience under the old law, since there has been no experience with the new one. Throughout the report, however, the possible impact of provisions in the new law will be noted where applicable.

An important aspect of the new law is its approximation to the competition law of the European Community, as required by the Europe Agreement between European Communities and their Member States and Lithuania. Thus, the provisions proscribing restrictive agreements¹ and abuse of dominance² are modeled after articles 85 and 86 of the EC Treaty, as applied. The law provides for notification of mergers (concentrations) that exceed certain size thresholds in advance of consummation, and, like the EU, establishes as substantive legal standard the prohibition of mergers that “establish or strengthen a dominant position and result in the reduction of competition in a relevant market.”³ The law prohibits certain acts that are defined as “unfair competition,” including misuse of intellectual property, dissemination of false or misleading information about one's own or another's products or operations, and obtaining or using the commercial secrets of another without permission.⁴ In many other respects, of course, the new law contains provisions that are unique to Lithuania and its institutions.

1.2 *The Competition Agency*

The new law creates a Competition Council, consisting of a Chairman and four members, who are appointed by the President of the Republic upon

nomination by the Prime Minister.⁵ The Chairman serves for a term of five years, and the four members serve for a term of six years, except that initially two members serve for a three year term. Staff of the Council conduct investigations of possible violations of the law, having powers to acquire evidence, and make recommendations to the Council.⁶ The Council may conduct public hearings, in which interested persons may participate and present evidence.⁷ After the hearing the Council may adopt resolutions to the effect that a violation of law has or has not occurred, and impose sanctions as appropriate.⁸ Sanctions may include orders to cease an illegal activity or to take action to eliminate the consequences of such activity.⁹ Fines may also be imposed, both for substantive violations and for failure to observe procedural obligations imposed by the law.¹⁰ Appeals from decisions of the Council may be made by the parties to the case and by “other persons who believe that their rights protected by this Law have been violated” to the Higher Administrative Court.¹¹

Under the 1992 law the enforcement functions were conducted by seven enforcement divisions within the State Competition and Consumer Protection Office (“Competition Office,” or “Office”; the reorganisation of the structure of the Office under the new law was still underway at the time of the writing of this report). The **Competition Policy Division** formulates broad policy within the Office, including the drafting of legislation and regulations. It also has responsibility for matters relating to the integration with the EU and for relations with competition authorities of other countries and with international organisations. The **Concentration and Financial Markets Division** has merger enforcement responsibility, including the receipt and examination of merger notifications, and non-merger enforcement responsibility for the financial sector. The **Services Division** has non-merger enforcement responsibility in the services sector and for matters involving intellectual property. The **Industry and Construction Division** has non-merger enforcement responsibilities in several industrial and manufacturing sectors. The **Agriculture and Food-Stuffs Division** has non-merger responsibilities in those markets, and also for the telecommunications sector. The **State Aid Monitoring Division**, a relatively new division, conducts those activities as provided in the Government Resolution on State Aid Monitoring Procedure approved in 1997 and amended in 1999. The **Consumer Protection Division** enforces the Law on Consumer Protection and also has responsibility for prosecuting acts of unfair competition under the competition law.

The Office employs approximately 50 people. Most of the professional employees are economists; only a few are lawyers. Each of the seven divisions has a staff of four or five people.

2. Substantive Enforcement

In this section the Office's enforcement of the substantive provisions of the competition law will be reviewed. Each area of substantive law (*e.g.*, abuse of dominance, restrictive agreements, mergers) will be discussed separately. Brief descriptions of representative cases will be included where appropriate. Comments and recommendations will also be provided at the end of each section.

2.1 Abuse of a Dominant Position

Article 3 of the 1992 law and Article 9 of the new law prohibit abuse of a dominant position. Like most competition laws, these articles contain both a general prohibition of conduct by a dominant firm that results in a restriction of competition, and an enumeration of specific types of conduct that can constitute abuse of dominance. Article 9 of the new law substantially resembles Article 86 of the EC Treaty. The types of specific conduct enumerated in Article 9 are identical to those in Article 86. Article 3 of the 1992 law was somewhat broader than the new Article 9. It also prohibited resale price maintenance and other agreements with contracting partners on prices to third parties, conduct which in most countries is usually prosecuted as a restrictive agreement.

Both the old and the new law define "dominant position" as having the ability to unilaterally exercise "decisive influence" on a market. Under the 1992 law an enterprise could not be dominant unless it had a market share of more than 40 per cent.¹² Under the new law, a 40 per cent market share establishes a presumption of dominance. In addition, the new law creates a presumption of joint dominance when the three largest firms in a market have a collective market share of 70 per cent.¹³

In 1996 The Competition Council considered a total of 41 cases involving possible substantive violations of the law, 44 cases in 1997 and 19 cases in 1998. Of these, seven in 1996, eight in 1997 and one in 1998 involved possible abuse of dominance. The cases arose in several sectors of the economy, and involved issues such as refusals to deal or discrimination by operators of essential facilities (rail, telecommunications), exclusive distribution arrangements and resale price maintenance. Market definition appears to have been a central issue in some of the cases, particularly those not involving essential facility issues. In one recent case that was appealed to the court, the determining issue was whether imported products and domestically produced products were in the same market. The Council had decided that imports were not part of the relevant market, on the basis of differences in price and quality.

The court upheld the Council. Remedies in most of the cases included orders to cease the offending conduct accompanied by fines, which were usually not large.

Comment

Abuses of a dominant position tend to occur relatively more frequently in transition countries. Monopolies or dominant positions are more common in these countries, having been created by privatisation of formerly state-owned monopolies, and they tend to be more persistent, because entry by new competitors may be hindered by imperfectly functioning capital markets and scarcity of other important inputs, such as good distributors or retail outlets. Lithuania is perhaps not typical in this regard, however. Its caseload statistics reflect fewer abuse of dominance cases as a percentage of the total than in other transition countries. Still, it is likely that the Council will be confronted with important abuse of dominance cases for the foreseeable future. It will be important that the Council select cases of significance for Lithuanian consumers. Successful prosecution of such cases will enhance the Council's reputation both within government and throughout the private sector.

Article 9 of the new law resembles the abuse of dominance provisions in the laws of Lithuania's neighbors in the Baltic region and throughout Europe, in that it specifies certain types of conduct that can constitute abuse, such as "unfair pricing" or "limitation of trade, production or technical development to the prejudice of consumers." Such terms are sometimes ambiguous and difficult to interpret. There are often situations in which such conduct is not competitively harmful, even when performed by a dominant firm. Especially problematic in this regard is so-called "unfair pricing," or similar terms. Economists agree that it is notoriously difficult to determine whether a given price is at or above the competitive level. For this reason most competition experts consider that enforcement of abuse of dominance provisions should focus on exclusionary conduct – that which unnecessarily excludes actual or potential rivals from the market – rather than "exploitative" conduct – charging prices that appear to be too high.

As noted above, abuse of dominance cases in Lithuania have tended to turn on the issue of market definition. That issue and ease of entry are likely to be determinative in most abuse cases, and in relatively small countries such as Lithuania both may depend on whether or not foreign sources of supply are reasonable substitutes for domestic products and services. tend to be fact intensive and difficult to prosecute. Market definition and conditions of entry are often crucial to the dominance analysis, and in smaller transition countries such as Lithuania both issues often revolve around the availability of imports as substitutes for domestic products or services.

Obtaining an effective remedy is essential in abuse of dominance cases. “Structural” relief – elimination of the dominant position by breaking up the dominant firm or introducing new competition – is usually preferred to “behavioural” relief –altering the conduct of the dominant firm through remedial orders. Remedial orders that are excessively regulatory are difficult to enforce and may over time themselves harm competition as market conditions change. Within the different types of structural relief, encouraging new competition through the elimination of artificial barriers to entry is vastly preferred to breakup of the dominant firm, which is quite difficult.

Recommendations

- Be alert for important abuse of dominance cases that have significant impact upon Lithuanian consumers. Concentrate on conduct that is exclusionary rather than exploitative in character.
- Focus on achieving effective relief in abuse cases. Where possible seek structural relief through the lowering or elimination of artificial barriers to entry. If remedial orders are necessary, draft them as simply and directly as possible, and limited in time.
- Continue to give importance to market definition and conditions of entry in analysis of abuse cases, and pay particular attention to imports as actual or potential market participants.

2.2 *Restrictive Agreements*

The substantive provisions prohibiting restrictive agreements in the 1992 law (Article 4) and the new law (Article 5) do not differ significantly. They contain general prohibitions of agreements that restrict competition and also prohibitions of specified types of conduct. The specific prohibitions include agreements among competitors fixing prices or terms of sale, allocating markets or sales volumes, and bid rigging. The new law provides that these types of conduct are considered as always restricting competition and are illegal unless they fall within one of the exemptions in Article 6. Other types of conduct that are specifically enumerated in Article 5 include agreements applying discriminatory conditions to contracting parties or requiring obligations unrelated to the subject of the underlying agreement, and agreements to refuse to contract with certain parties (group boycotts).

The new law departs from the 1992 law, however, in providing for certain exemptions from the general prohibitions of anticompetitive agreements. In language that parallels Article 85(3) of the EC Treaty, Article 6 provides for “general or individual exemptions” for agreements that improve investment, technical or economic progress or distribution of goods to the benefit of consumers. Such agreements must not impose restrictions on the contracting parties that are unrelated to the beneficial objectives enumerated in Article 6, however, and they must not afford the parties the ability to eliminate competition with respect to a substantial part of the relevant market. Article 7 bestows upon the Council the power to issue block exemptions relating to certain types of conduct. The Article is explicitly intended to parallel the practice in the EU relating to block exemptions. It provides for block exemptions of agreements “for which general exemption is granted pursuant to the legal provisions in effect in the European Union.” Parties may apply to the Council for a determination of whether their agreement falls within a general exemption. Article 7 also requires the parties to an agreement subject to a general exemption to provide information about the agreement to the Council on a standard form to be established by the Council. Article 8 provides for the granting of individual exemptions, upon the submission of an application to the Council “prior to the conclusion or coming into force of the agreement.” The Council must render its decision within three months of the submission of the application.

A separate law, the Law on Implementation of the Law on Competition, provides that Article 4 of the old law will continue to be in force until the year 2000 and will govern all agreements concluded before the new law on competition became effective. Beginning in 2000 the new law will apply to all agreements. During the remainder of 1999 the Council will draft the necessary regulations providing for block exemptions.

The Council has considered relatively few cases on restrictive agreements under Article 4 of the old law. Through 1996 there were no Article 4 cases, but in the past two years the Council has been more active in this area. To date, four cases involving cartel activity have been brought to the Council. In at least one other situation in a major industry a cartel was suspected, but the Competition Office was unable to generate sufficient evidence of an agreement. The subjects of the investigation were not co-operative, and the office lacked sufficient powers to compel the production of evidence. Two successful cartel cases are worthy of description, however:

Price Fixing - Meat Producers

A meat producers' association, consisting of eight members, was organised under the auspices of the Ministry of Agriculture. The members met periodically for legitimate purposes, but at these times they also met unofficially and agreed on prices for sales to the government. The Agriculture Ministry discovered a written protocol containing the agreement and notified the Competition Office. The Office interviewed the producers and several admitted to the agreement. The Council fined the members of the association LTL 500 000.

Market Allocation - Intravenous Solutions

A Lithuanian producer of intravenous solutions agreed with a Latvian producer of these products that each would not export to the other's country. The agreement was discovered during a routine visit to the offices of the Lithuanian enterprise by staff members of the Competition Office. The manager of the enterprise, apparently unaware of the illegality of the conduct, provided the competition staff with a copy of the written agreement dividing the markets. In the ensuing investigation the manager of the enterprise provided a written statement admitting to the agreement. The case was presented to the Council, which imposed a fine upon the Lithuanian enterprise and issued an order to terminate the agreement.

Comment

Like most transition countries, there have been few prosecutions of cartel cases in Lithuania, but in recent years the Council has increased its emphasis on such cases, for which it is to be commended. The intravenous solutions cases is an especially good example of a successful cartel prosecution. It should also be noted that this was an international cartel; the illegal agreement allocated markets between Lithuania and Latvia. Indeed, there is a trend worldwide in international cartel cases. Successful prosecution of such cases often requires close co-operation between the competition agencies in the affected countries.

Prosecuting cartels is difficult. Evidence of illegal agreements is not easy to obtain, especially when the subjects of the investigation are not co-operative. It is not uncommon in transition countries, however, that subjects voluntarily produce evidence of the illegal activity, often because they do not know that the conduct is unlawful. Over time it is likely that the Council will enjoy less co-operation from subjects in cartel investigations, and it will be necessary to develop more sophisticated means of investigating such conduct.

In providing for general and individual exemptions from the prohibition of restrictive agreements, the new law is a significant departure from the 1992 law. By incorporating the EU experience in this area the new law offers, in the long run, the benefit of enhanced certainty for the business community about the legality of their agreements. Implementation of the new regime may prove difficult, however. The Council must be careful not to impose burdensome notification requirements relating to these exemptions. The EU experience has shown that the competition authority is ill-equipped to deal with large numbers of applications for exemptions. In this regard, the requirement in Article 7 of the new law that parties to every agreement that is subject to a general exemption provide information to the Council about the agreement may generate a great deal of documentation that will unnecessarily occupy a significant part of the Council's limited resources.

Recommendations

- Detection and prosecution of cartels should have a high priority within the Council. There are several facets to this effort:
 1. Educating consumers about the harm to them from cartels – higher prices and lower quality; encouraging consumers to co-operate with the Council's efforts to eliminate cartel activity by providing information about suspected illegal conduct.
 2. Educating businesspeople about their obligations under the competition law, encouraging voluntary compliance with its requirements; helping them also to realise that businesses are consumers too, and therefore that they benefit from the elimination of cartels.
 3. Becoming more aggressive in gathering evidence in situations of non-co-operation by investigation subjects; in particular, a) developing methods of obtaining potentially incriminating documentary evidence from the files of suspected cartel members, and b) encouraging co-operation by witnesses with information about cartel conduct by providing them with incentives, such as immunity from prosecution or reduced fines.
 4. Punishing cartel operators with significant fines, especially in situations where the activity was conducted in secret and the operators were aware of the illegality of their conduct.
- Place a high priority on promulgation of block exemptions under Article 7 of the new law. Avoid, as much as possible, the implementation of unnecessary and burdensome notification and information procedures relating to exemptions. In particular, minimise the burdens that could result from the requirement in the new law that all agreements subject to a block exemption be notified to the Council.
- Be alert to possible international implications of cartel agreements, and develop good relations with competition agencies in neighboring countries to facilitate co-operation in investigations and cases where necessary.

2.3 *Mergers*

Both the 1992 law (Articles 10-11) and the new law (Articles 10-15) provide for premerger notification and merger control. The substantive standard under both laws is “create or strengthen a dominant position.” The 1992 law provided that the Council would establish the size thresholds for notifications. Those thresholds were set at a relatively low level: notification was required if the merging parties together had any of the following: annual turnover of eight million Lt., total capital of 2 million Lt., or 300 employees. These thresholds generated a relatively large – and growing – number of notifications: 38 in 1996, 77 in 1997 and 158 in 1998. The law required the Council to adopt a decision on the merger within one month after notification. The period could be extended for up to nine months, but only with the agreement of the parties.

The new law is an improvement on the 1992 in some respects. The notification threshold is set at combined turnover of 30 million Lt., each party having at least 5 million Lt. It is expected that the higher threshold will reduce notifications by at least one-half. The Council can adjust the applicable thresholds not more frequently than every two years. The law provides that the Council must within one month after notification make a final decision on the merger or decide to extend the examination. In the latter event, the final decision must be made within four months of notification.

Notified mergers have occurred in many sectors of the economy. In approximately half of the transactions a foreign economic entity was involved. All types of mergers have been notified – horizontal, vertical and conglomerate – with horizontal and conglomerate being the larger categories. To date, almost all notified mergers have been approved by the Office. One merger has been disapproved completely, and a few have been approved with conditions. Two recent merger cases merit further description:

Sugar

The owner of a sugar factory proposed to acquire three other sugar factories, all located in Lithuania. The Lithuanian sugar market was highly concentrated, and the merger would increase the concentration still further. There were few imports, the result of high tariffs. The Council made a tentative decision not to approve the merger, but it was approved by the Government. The decision to approve was based on the need for restructuring and modernization of the industry in Lithuania. (Article 11 of the 1992 law provided for such approvals by the Government when it was shown that the merger would improve economic efficiency or competitiveness, and that these benefits could not be achieved in ways other than the proposed transaction. The new law does not have such a provision.) The restrictions on imported sugar remained, however, and the Government continued to exercise some control over the price of sugar.

Beer

The beer market in Lithuania has been undergoing significant changes in recent years. Production had increased significantly, but the market was still dominated by four large producers. Imports were not significant, accounting for only about five per cent of total sales. Two foreign entities proposed to acquire, through a joint venture, 50 per cent of one of the four producers. One of the foreign entities, which would acquire 19.5 per cent, already controlled one of the other four domestic producers. The Competition Office, employing the standards in the United States Horizontal Merger Guidelines, determined that concentration in beer in Lithuania was at the lower end of the “high” range. Concentration in bulk beer before consummation of the proposed transaction, measured by the Herfindahl - Hirschman Index (HHI), was 1870 (an HHI of 1800 is considered high in the U.S. Guidelines). The HHI for bottled beer was 2170. The Competition Office determined that the proposed transaction would increase the HHIs to 3074 and 3638, respectively.

This increase in concentration raised serious concerns about the effect of the transaction on competition. It was noted, however, that the competitor of the firm to be acquired would have only a minority interest in the joint venture. The Office approved the transaction on the condition that each partner in the joint venture agree to provide notification before increasing its ownership share in the venture and that the parties avoid interlocking directorates.

Comment

That the Office has to date taken action against very few of the mergers notified to it does not necessarily indicate any sort of failure on its part. In most countries, including OECD countries, only a very small proportion of notified mergers are prevented or modified – often as few as one to three per cent. Certainly it is true that merger analysis in each country must take into account the specific characteristics of local markets. In small countries, for example, imports are usually relatively more important than in larger countries. Absent significant restraints on imports, mergers of domestic firms may seldom be anticompetitive. The sugar case described above illustrates this point. The Office correctly considered the merger of domestic firms to be anticompetitive because there were significant restraints on imported sugar.

The two cases described above illustrate other points that are likely to arise in merger cases in transition countries. Domestic assets that remain from the period of central planning will be relatively inefficient. Some restructuring of these assets,

especially in the industrial sector, will almost certainly be necessary. Efficiency considerations will be important – possibly paramount – in these cases. This was apparently the deciding factor in the decision of the Government to override the decision of the Council in the sugar case. Such mergers will not be anticompetitive, however, if barriers to entry, especially by foreign producers, are not high. If, on the other hand, domestic industries are restructured and concentrated, and competitive imports are artificially excluded by government policies, consumers could be harmed by these transactions.

The beer case is a subtle illustration of another issue that can confront competition authorities in transition countries – understanding the real effect of complex mergers involving novel corporate forms and transactions, combined with participation by several entities, some of whom are foreign. Difficult and arcane concepts of “control,” “decisive influence,” “person” and “group of persons” may affect the analysis of these cases. These concepts have different meanings in different countries, depending on national laws and traditions. While the new law contains definitions of some of these terms, it will take some time and experience for the competition authority to develop expertise in this area.

In the beer case the Council was confronted with a transaction involving the acquisition of only a partial interest in a firm – one involving less than majority ownership. Even though such an acquisition might not confer absolute “control,” as that term is defined in the competition law, it could give the acquiring firm some power over the acquired firm, sufficient to have an effect on competition. This case illustrates the importance of assessing the likely actual effects of the transaction on competition, apart from the effect on concentration alone.

An important consideration for competition authorities in small countries is the need not to surrender too much of their limited resources to merger control. In the first instance, this means devising a notification scheme that does not produce an unnecessarily high number of notifications. Merely having to read a large number of notifications can siphon off important resources that would be more profitably devoted to other pursuits. Investigations of even a small number of mergers can occupy much more time and effort. Second, it means adapting

one's merger policies to the realities of the domestic market – learning to recognise and prosecute only those few mergers that truly threaten the welfare of the nation's consumers.

Recommendations

- Monitor the trends in merger notification procedures; adjust the notification thresholds as necessary to minimise unnecessary notifications.
- Develop procedures for expedited review and decision making on notified mergers, with a view toward conserving the Council's limited resources.
- Evaluate the competitive effects of mergers according to actual conditions in Lithuanian markets. Give appropriate consideration to actual or potential competition from sources outside the country.

2.4 *Anticompetitive Activities of Governments*

Article 6 of the 1992 law prohibited “bodies of state authority and government” from restricting the independence of economic entities, impeding their foundation or reorganisation, granting privileges or otherwise discriminating in favor or against economic entities, or “otherwise restrict[ing] competition.” Article 4 of the new law applies to similar conduct, but is worded differently. Public administration and local authorities are affirmatively required to “ensure free and fair competition” in the course of their regulation of economic activity. They are prohibited from discriminating in favor or against economic entities, except when such discrimination is required in the course of carrying out their responsibilities under the laws of Lithuania.

Article 19(4) of the new law provides that the Council may request governmental bodies to cease or modify conduct that is considered to violate Article 4, and if such measures are not taken, to appeal the matter to the Higher Administrative Court, except in the case of statutory acts of the Government of Lithuania.

The Council considered ten cases under Article six of the 1992 law in 1996, three cases in 1997 and none in 1998. The following 1996 case is illustrative.

Bus Transportation - Municipality of Klaipeda

The Municipality of Klaipeda granted concessions to 48 private bus operators to provide passenger bus service in the town. It also introduced a tax on these operators for the privilege of operating in the center of town. The Municipality was also the founder of one of the bus operators, and for this operator the Municipality provided a subsidy for carrying certain passengers and exempted the operator from paying the tax. The Council determined that this conduct violated Article 6 of the 1992 law, and requested that the Municipality cancel the discriminatory subsidy and tax exemption.

Comment

Lithuania is one of several transition countries whose competition laws provide for direct action against other government bodies for anticompetitive acts committed in the course of their regulatory activities. In most non-transition countries the competition law extends to governmental bodies only to the extent of their activities as entrepreneurs. There is justification for such laws in transition countries: the removal of lingering effects of central planning. There are practical and political limitations on the ability of competition authorities to enforce these provisions against their colleagues in government, however. More often than not, relief from harmful and discriminatory regulation is achieved through persuasion or public exposure rather than by fiat. This was apparently the experience in the Klaipeda bus case.

That the Council is somewhat circumscribed in its ability to act against other bodies of government under the law does not mean that it should not be active in this area. Quite the contrary, this provision of the law can be a powerful tool in the effort to rid government of unnecessary and anticompetitive regulation. It is a much stronger argument against such conduct to say that it is unlawful, rather than just bad policy.

As noted above, there has been a decline in the number of cases of this type in the past two years. This decline may simply be an indication that government bodies are engaging in this conduct less frequently than they use to. Or the lesser number of cases may simply be the result of informal resolution of violations, rather than through formal proceedings. Interviews in the private sector conducted as a part of this study, however,

suggest that significant problems of this type still exist in Lithuania.

The elimination of improper regulation or discrimination by government bodies can yield tangible, significant benefits for consumers. In transition and developing countries there is little that a competition authority can do of greater value than to pursue this conduct vigorously. Moreover, success in this area reflects quickly and favourably upon the competition agency, helping to build its credibility in the business and consumer communities.

Recommendations

- Place strong emphasis upon enforcement of Article 4. Make the business community an ally in this effort.
- Apply available sanctions judiciously, with the principal goal of elimination of the harm, not punishment or retribution. Seek to enlist the co-operation, rather than opposition, of government bodies in this effort.
- When there are successes, use available means to inform the public of them, thereby strengthening support for the work of the Council and for competition policy.

2.5 *Unfair Competition*

As noted above, the 1992 law and the new law contain similar provisions forbidding conduct that constitutes misappropriation of intellectual property of another business entity or disseminating false and misleading information about oneself or another business entity. In the first years after the enactment of the 1992 law the Council was active in this area, bringing at least 20 cases in most years. The number dropped to six in 1998, however.

Comment

Protection of intellectual property rights and against untruthful and misleading disparagement of a competitor are important to the proper functioning of free markets. In countries whose economies have been recently liberalised, it is not uncommon

for the competition agency to institute a relatively large number of cases of unfair competition, even when the practices do not have an impact on the economy as a whole. As markets mature, however, the number of such cases brought by the competition agency tends to decline, for at least two reasons. First, businesses become more knowledgeable about what the law permits in this area. Second, and possibly more important, in developed economies there is generally easier access to courts for resolution of private disputes, and businesses tend to resort to such remedies directly in cases of unfair competition. In this regard, Article 17 of the new law explicitly provides that economic entities that are harmed by acts of unfair competition may bring actions in court to obtain termination of the illegal conduct and recover damages suffered as a result of the conduct.

Recommendations

- Continue to prosecute important cases of unfair competition, especially where significant issues of protection of intellectual property are involved, but to conserve important resources, encourage businesses to resolve their disputes privately, where possible.
- Use the authority of the Council to achieve voluntary compliance when it appears that violations have occurred, again to conserve resources.

2.6 Consumer Protection

The Council has the principal responsibility within the Government for consumer protection. As noted above, the Consumer Protection Division of the Competition Office has only a few people on its staff, and also has responsibility for enforcing the provisions of the competition law on unfair competition. Attached to the Competition Office, however, is the State Quality Inspection Office (SQI), whose staff numbers more than 250 and which investigates and resolves matters of product quality. A very large number of consumer complaints are received by the Office and the SQI. In 1997 the Office received 1060 complaints, and the territorial offices of the SQI received 1881. Most of the complaints are related to issues of product quality, and the majority of these involve food products.

The current Law on Consumer Protection was adopted in 1994. In addition, other Government regulations provide certain protection to consumers, including “The Rules on the Supplying of Services,” and “The Rules on Retail Trade on Replacement of the Goods Acquired in Trade Undertakings of the Republic of Lithuania.” Work is underway on drafting a new consumer protection law, along with a law on advertising. The draft consumer protection law is modeled after EU laws on the subject. The current draft provides for consumer protection to be the responsibility of the Council. Under current law, the Council has limited power to enforce its orders regarding consumer violations. It cannot impose fines directly for such violations, for example, only for failure to observe previously issued orders. The Office lacks expertise in some areas in which consumers are often victimised, especially in financial matters. The Office attempts to be responsive to consumers, however. It has established a special telephone line for the purpose of receiving consumer complaints. It occasionally participates in public forums on consumer issues, when resources permit.

Comment

Protection of consumers against fraudulent conduct and false and misleading advertising is an important function of government, and it has special importance in emerging or transition economies, where consumers tend to be less sophisticated and more vulnerable to unscrupulous sellers. In some countries the competition office is responsible for consumer protection; more often, a separate consumer protection office is established. In either case, consumer protection requires a significant commitment of resources. The current resources in the Competition Office are clearly not sufficient for the purpose, but there appears to be an opportunity to enlist the State Quality Inspection Office to this end.

Recommendations

- Give high priority to completing and enacting the new consumer protection law. Ensure that it contains adequate powers of investigation and sanctioning.

- Whether the new law places consumer protection responsibility with the Council or in a separate office, work to ensure that the new office has substantially greater resources than are currently available in the Competition Office. In this regard, employ the resources of the State Quality Inspection to the extent possible.

2.7 State Aids/Antidumping

The State Aid Monitoring Division of the Competition Office was established in 1997 for the purpose of carrying out the requirements of the Europe Agreement and the Free Trade Agreement between Lithuania and the EU relating to the monitoring and reporting of state aids. The Office has drafted informal guidelines for the granting and reporting of state aids, which have been distributed to other departments and agencies of government. The Office is preparing more formal, permanent guidelines on the subject. The State Aid Monitoring Division works with other parts of the Government in collecting information on existing and proposed state aids and compiling it into an annual report, in accordance with the requirements of the EU agreements. The Division is developing a process for compiling a state aid inventory, based on the European Commission model. Government Decree No. 137 (1997) provides that the State Aid Monitoring Division can apply to the Government or to the courts for termination or cancellation of state aids considered in violation of Government policy.

The Competition Office also has responsibility for administering Lithuania's antidumping law. The law is relatively new, but a few dumping cases are underway. A new division of the Council will be created to handle the antidumping work.

Comment

State aids and antidumping have important implications for competition policy. Improper implementation of these policies can result in significant market distortions, impeding competition and harming consumers. In most countries, however, state aid monitoring and antidumping functions are carried out by separate government institutions. The competition agency provides input into their decisions, where possible.

The Lithuanian Competition Office is not adequately prepared and its resources are not sufficient to handle these two important and difficult tasks. There are currently five people in the division to which work of state aid monitoring is assigned. The new antidumping division has received six additional employees in 1999, but this number will not be sufficient to handle any significant number of cases. It is hoped that financial assistance from PHARE will be made available for the state aid work.

In most countries, antidumping responsibilities are not assigned to the competition agency. To be sure, antidumping cases can significantly impact competition, and for that reason the competition authority should have an advisory role in this area. The work is highly technical and resource intensive, however, and for resource reasons alone, it is usually better that the case work be done by an agency with specific expertise in the area. In the alternative, if the work remains with the Council, the Office must receive significantly more resources with which to handle it.

Recommendations

- Work within the Government to have antidumping responsibilities transferred to another agency that has, or has the resources to develop, expertise in the area. Retain an advisory role for the Council in these cases, however. In the alternative, if the antidumping responsibility is to stay with the Council, seek a significant augmentation of resources to handle it.
- Work to obtain significant additional resources, including money from PHARE, which is distributed by the Lithuanian Government, for the state aid monitoring project. In addition to more employees, additional training for this task is required.

2.8 *Competition Advocacy*

Current procedures in the government provide for submission of draft new legislation to the Competition Office for comment on issues of competition policy. The new law codifies this procedure in Article 19(8), providing that the

Office may submit conclusions to the Seimas and to the Government on the effect of draft laws and other legal acts on competition. In exercising this responsibility the Office has commented on dozens of pieces of legislation in recent years. Members of the Office have consulted with other ministries on specific cases or proposed regulations. One of the more visible examples of the Office's competition advocacy role occurred in the recent privatisation of the telecommunications industry in Lithuania.

The privatisation of the state-owned telecommunications system, which was accompanied by the enactment of a new law on telecommunications, was a difficult and controversial procedure in Lithuania, as it is in any country. Substantial investment in facilities was needed; the equipment required modernisation and penetration of households by landlines was low. A majority interest in the operations ultimately was sold to a consortium headed by Swedish and Finnish interests. The new owners acquired in the transaction an exclusive right to provide service through fixed facilities through 2002. In its comments on the legislation the Office raised certain objections to the exclusive arrangement. Its views apparently were not heeded, however. Later, the Office raised objections to the fact that Telekomas, the fixed asset operator and owner of one of two mobile telephone licenses, also was a shareholder in the owner of the second mobile license. Telekomas was ordered to sell those shares.

Comment

The Council is active in competition advocacy within the Government of Lithuania, more so than competition agencies in some other transition countries. It is to be commended for its efforts in the telecommunication privatisation program. As noted in the description of that case, however, the Council's advice as competition advocate is not always heeded, which is true in every country. That a competition agency is not always successful does not mean that it should abandon this activity. The benefits to consumers from an active competition advocacy program can be significant, and this is especially true in transition and developing countries, which are engaged in wholesale reformulation of their economic policies.

The Competition Council faces a significant challenge in this important area. It has limited resources, so it must carefully select the matters in which it will participate. Perhaps most important, its independence within the government, or lack thereof (discussed further below), will control the extent to which it can be effective as competition advocate.

Recommendations

- Continue to place emphasis on the Council's role as competition advocate. Select the matters in which it will participate carefully, with an eye toward the impact of the decision under consideration on consumers.
- Prepare the Council's competition advocacy comments with care, striving for accuracy, to enhance the Council's credibility in this arena. Where the Council lacks expertise in a technical area, enlist the aid of interested and sympathetic outsiders who have the requisite knowledge, such as academics or business groups.

3. Institutional Issues

3.1 *Independence of the Council Within the Government*

Under the 1992 law the Competition Council initially existed within the Institution of Price and Competition. In 1995 the Institution was reorganised into the State Competition and Consumer Protection Office. The director of the Council was appointed by the government. The Council consisted of seven members, also appointed by the government, who served for terms of three years. Council members did not serve full time in their positions. The Competition Office was an institution under the Government of the Republic of Lithuania. The law did not explicitly state the conditions under which a Council member or director of the Competition Office could be removed.

The new law is more explicit on several aspects of the status of the Competition Council, and in some respects provides the Council with a greater measure of independence. Article 20 provides that the Chairman and the Council members are appointed by the Government, according to the proposal of the Prime Minister and approval of the President. The terms of the Council members are six years (the longer term conferring more independence). The law lays out the conditions under which Council members can be terminated before the end of their term, and they are limited to criminal misconduct or the equivalent of dereliction of duty.

Comment

It is generally accepted within the international competition community that a national competition authority should operate with as much independence from the rest of the government as possible. Its decisions, like those of regulatory agencies, may affect the interests of large and powerful businesses, which may have strong political influence with the government. The competition agency should be free of such influence to the extent possible. Thus, it is often recommended that the competition agency be created as a separate entity that is not a part of any other government ministry. The agency would be answerable directly to the legislature for its funding, and the head of the agency or the members of the commission would be appointed by the president or other chief executive, subject to removal only for gross negligence, corruption or clear inability to perform the functions of the office.

Such a structure may be considered an ideal, however, and does not exist in that form in most countries, including Lithuania, although as noted above, the new law does provide an expanded degree of independence for the Council. In any case, a significant degree of “informal” independence can be achieved over time by the competition agency, by means of measured, impartial and transparent decision making, coupled with the building of public understanding and support for the agency’s mission. The achievement of such independence should be a long term goal of the Council.

3.2 *Investigative Powers*

The 1992 law (Article 8) provides in general language for the right of the Competition Office to “obtain information . . . as well as explanations - oral or written - which are necessary to carry out the functions established in this law and in the regulations of the Institution.” The new law is much more explicit in this regard. Article 26 provides for extensive powers to obtain information from the subjects of an investigation. The powers include entering and searching the subjects’ premises with or without notice, examining and copying documents therein and taking documents away, obtaining oral and written explanations from subjects, including by requiring individuals to appear at the offices of the Competition Office. Before entering and searching the subjects’ premises and reviewing and removing documents, however, a court order must be obtained. In addition, Article 26 provides for the Office to obtain

information and documents from other economic entities – non-subjects – and from public administration and local authorities in the course of an investigation.

Under the 1992 law the Competition Office seldom exercised its power, to the extent that the law conferred it, to compel the production of information or documents. As described above in **section 2.2**, most investigations were conducted on a voluntary basis, and success depended to a large extent on the willingness of subjects to co-operate. Sometimes the subjects co-operated because they were ignorant of the law and of their potential liability under it. The new law provides the Office with significantly expanded information gathering powers. The Office is still faced with the significant challenge of employing these new powers effectively and judiciously, however.

Comment

The general language in the 1992 law on investigative powers was clearly insufficient. The Office was seldom successful in compelling the production of evidence. The new law corrects many of the deficiencies of the 1992 law in this area, but successful implementation of these new powers will not be easy. The Office will need to gain the confidence of the business community that these new powers will be used fairly. Demands for information should not be issued indiscriminately, generating heavy burdens of compliance on investigative subjects and corresponding burdens on the Office of reviewing the information. Finally, the Office must be firm in enforcing these new powers, vigorously prosecuting intentional untruthfulness or willful failure to comply with information demands.

Recommendations

- Employ the new information powers selectively and fairly.
- 1. Continue to use voluntary means of investigation whenever possible, especially when seeking information from non-subjects – “third parties” – in an investigation.

2. Conduct unannounced “dawn raids” and searches sparingly, for example only when serious, ongoing anticompetitive conduct is suspected, and co-operation by the subjects of the investigation is unlikely.
 3. Make use of the power to compel subjects to come to the offices of the Competition Office and provide information. Require them to bring relevant documents with them, which can be specified in the notice of the meeting.
 4. Perfect techniques of requesting and reviewing relevant business documents from both subjects and third parties. Documents written in the regular course of business often are the best source of evidence of for use in defining markets assessing conduct’s likely effects.
 5. Be willing to discuss demands for information with recipients with the purpose of meeting their legitimate concerns about burdens of production.
 6. Institute rigorous procedures for safeguarding the confidentiality of information that is provided, as the law requires. Take pains to assure the providers of information, both voluntary and involuntary, that the confidentiality of their information will be maintained.
- Be prepared to prosecute economic subjects who intentionally provide false information or willfully withhold information specified in a demand. Seek strong sanctions for such conduct.

3.3 *Enforcement and Sanctioning Powers*

The enforcement and sanctioning powers provided by the 1992 law and the new law (articles 40-44) are similar, although there are some differences. Under both laws the Council can issue binding orders requiring economic entities to cease specified conduct or to take affirmative actions restoring the situation that existed prior to a violation and removing the consequences of a violation. The 1992 law granted the Council the power to impose fines on economic entities (defined to include both legal and natural persons) of up to 10 per cent of the entity’s total gross annual income for substantive violations of the competition law, and up to three per cent of annual

gross income for submission of misleading information to the Competition Office. The 1992 law also authorised the Council to impose fines of up to three months average earnings for failure to comply with orders of the Council.

The new law provides that the Council may impose a fine for unlawful restrictive agreements, abuse of dominance, consummating a notifiable merger without the Council's permission and failure to observe orders of the Council relating to mergers of up to LTL 100 000 (currently about US\$25 000), except that when such violations occur in "aggravating circumstances" a fine of up to 10 per cent of gross annual income may be imposed. A fine of up to LTL 30 000 may be imposed for acts of unfair competition, again with the "aggravating circumstances" exception permitting a fine of up to three per cent of gross annual income. A maximum fine of LTL 100 000 may be imposed for hindering the entry of investigators on to the premises of economic entities or interfering with their activities when they enter, as provided by the law. A maximum fine of LTL 10 000 may be imposed for providing incorrect or incomplete information to the Council or Office, and an entity who fails to comply with an order of the Council may be fined up to LTL 10 000 for each day in which it is not in compliance.

The new law adds some useful provisions setting forth relevant criteria for determining appropriate fines, within the limits in the law. Fines shall be influenced by the amount of injury caused by the violation, the duration of the violation and other aggravating circumstances, including whether the violation was carried out in secret, in defiance of an order of the Council to cease the conduct, or is a repeated violation. The law recognises as extenuating circumstances the co-operation of an entity with the investigation, whether it voluntarily provided useful information to the Competition Office, whether it unilaterally took steps to cease the violation, and whether it voluntarily reimbursed losses or eliminated injury caused by its violation. The law excuses from liability for fines certain acts constituting abuse of dominance, where the dominant firm co-operates with the Office's investigation, it ceases the violation voluntarily, its acts did not result in substantial and irreparable damage to others and it compensates those who were damaged by its conduct.

The new law provides the Council with important new powers to impose interim measures to prevent immediate harm from violations of the law during the time that the Council considers a matter and before it reaches a final decision (Article 29). To prevent "substantial and irreparable damage" the Council may issue orders to cease an activity during the pendency of the matter. The Council may also attach the property of an economic subject if necessary to ensure the payment of fines. Appeals from these interim orders may be made to the Higher Administrative Court within one month of the order.

Both the 1992 law (Article 15) and the new law (Article 46) provide that recovery of losses or damages caused by violation of the competition law must be obtained according to the civil laws of the country. It appears that to date there have been few if any private damage cases in Lithuania. Where it is possible to bring such suits and resolve them fairly, however, the right of private action is an important supplement to government enforcement. The risk of large damage liability is an additional deterrent to those who would violate the law.

Comment

It appears that, on the whole, the Lithuanian law provides the Council with adequate sanctions for enforcing the law. The challenge is to apply them fairly and effectively. It may be useful for the Council to undertake a review of remedial orders that have been entered in previous abuse of dominance and restrictive agreement cases. Have they succeeded in eliminating the unlawful conduct and restoring competition to the market? A simple order to cease a violation may not be sufficient in some circumstances. Some “fencing in” provisions may also be in order, but it is also important that such an order not be too intrusive and ultimately anticompetitive itself.

The maximum fine of 10 per cent of annual gross revenues for substantive violations appears to be sufficiently large. Under the new law, however, fines above LTL100 000 may not be imposed except in cases of “aggravating circumstances.” That term is not otherwise defined. Large fines are usually appropriate for “hard core” cartel conduct, such as price fixing. In such cases the fines must be sufficiently large to create a deterrent to future violations. The threat of heavy fines can also have a secondary purpose. It can encourage individuals and enterprises to co-operate in investigations and cases to achieve a reduction or elimination of their liability. A fine of LTL100 000 would not always be sufficient for such purposes.

Recommendations

- Consider the effectiveness of prohibitions and remedial orders in abuse of dominance and restrictive agreement cases. Attempt to fashion orders that are limited to eliminating the illegal conduct and its effects, are easy to administer and are limited in duration.
- Impose increasingly large fines for engaging in cartel conduct and for willful disobedience of the Council's orders or the willful submission of false or incomplete information.
- If it is possible under the new law, consider designating "hard core" cartel conduct as always constituting "aggravating circumstances," thereby permitting fines above LTL100 000. In other respects, the Council should periodically review the 100 000 maximum, and if it appears to be inadequate in some situations, seek an appropriate increase through the Seimas.
- Employ the Council's discretionary powers to fine as a tool in gaining co-operation in investigations and cases, especially those involving cartel conduct.
- Work to educate the legal community about the opportunities for private damage actions.

3.4 *Administrative Procedures and Appeals*

The 1992 law did not explicitly set out the procedures to be followed by the Council and the Competition Office in prosecuting cases, but the Council had developed and implemented internal regulations governing the process. The Office could decide to begin an inquiry based on information that its officers had developed or that had been supplied by complainants. A recommendation to begin a formal investigation was made to the Investigative Commission, an internal body composed of the Director of the Office, the two Deputy Directors and two senior heads of divisions. If the Commission authorised the investigation the Office instituted formal contacts with the subjects of the investigation and third parties.

If the Office determined preliminarily that a violation of law had occurred it could negotiate voluntary termination of the illegal conduct, in situations where such relief would be sufficient. Otherwise it prepared recommendations to the Council, whose decisions required a 2/3 majority vote.

The new law (Articles 24 and 25) sets forth the hearing procedures in more explicit detail. As under the 1992 law the Council has the power to begin an investigation on its own initiative. In a potentially significant departure from the 1992 law, however, other entities, including economic entities that have been injured by allegedly anticompetitive conduct, bodies of public administration and local authorities, and associations and unions of economic entities and consumers, may submit a formal request for an investigation. The Council is obligated to decide whether it will grant the request within 14 days of the application. If an investigation is begun it must be completed within three months, except that the Council can extend the period for up to an additional two months.

The new law provides that Council hearings are to be conducted in public, except when it is necessary to close the proceeding to protect state or commercial secrets. The potential offender has the right to attend and participate, as do the initiator of the investigation, other economic entities whose interests are directly affected by the case and representatives of public administration and local authorities. Decisions of the Council are determined by majority vote, with at least four members participating. That part of its decisions containing the official resolution must be published in an official journal.

Under the new law, appeals from decisions of the Council may be made to the Higher Administrative Court. Previously appeals were heard by the Vilnius District Court. In 1996, four cases were appealed to the court. The Council prevailed in all of them, but in one case the court reduced the fine that was imposed by the Council. One case was appealed in 1997, in which the Council was upheld, and two cases were appealed in 1998, which are still pending.

Comment

The new law is a substantial improvement over the 1992 law in providing explicitly for openness in Council proceedings. Transparency builds confidence in the business and consumer communities in the integrity of the agency and helps to generate support for the agency among its constituents. Transparency

has certain costs, however. It is more difficult and time consuming to conduct business in public than to do so in private. Transparent procedures may interfere with the deliberative process by inhibiting the ability of the decision makers to meet and exchange views candidly. Inevitably there must be some consideration of trade-offs when designing the procedures that will govern the activities of the agency.

There is some risk that the provisions relating to the institution of investigations and the participation by interested parties in Council proceedings could generate undue burdens upon the Council. The requirement that the Council must formally consider every application for an investigation could occupy a significant part of the time and resources of the Council and the Competition Office, though it need not do so. There are adequate grounds in point 4 of Article 25 of the new law to permit the Council to reject applications for an investigation on the grounds that the complaint does not allege a violation of the law or involves an insignificant matter. The Council should ensure that it establishes procedures for receiving and evaluating applications that require a minimal expenditure of resources.

There have been few decisions of the Council appealed to the courts, and it appears that to date the Council has a good record in court. As time goes on and as the public gains experience under the new law, the number of appeals will probably increase, however. Court cases may be few, but they are important. If the agency's record of success in litigation is high, private parties will tend to avoid taking the agency to court, and the agency will have greater success in negotiating and enforcing administrative decisions. If its record in court is poor, the converse will result. Thus, the Council must give priority to litigation, preparing carefully for court proceedings.

It is almost certain that the judges in the Higher Administrative Court are not experienced in competition analysis. The Council could consider means of developing its relationship with the court and of providing opportunities for the professional development of the judges in the discipline of competition policy.

Recommendations

- Develop procedures for handling applications for investigations that minimise the resources needed to consider them. Apply fair but rigorous standards to these applications, so that the Office and the Council will not be preoccupied with many investigations of dubious merit.
- Develop standards, consistent with the law and practice in Lithuania, for the participation of third parties in hearings and appeals. Limit eligibility for participation to those whose interests are directly affected by the conduct in question in a manner consistent with the underlying purpose of the competition law.
- Similarly, develop efficient procedures for the conduct of hearings. Avoid situations in which “third parties” effectively gain control of a hearing, unnecessarily prolonging it and producing irrelevant, voluminous evidence or arguments.
- Work to develop a good relationship with the Higher Administrative Court, consistent with proper legal ethics. Sponsor workshops and seminars on competition policy, to the extent that time and resources permit.

3.5 *Public Relations – Developing a Competition Culture*

In addition to making its proceedings accessible to the public, it is in the broader interests of the competition agency to educate the public about its work – to help consumers, the business community and other parts of government understand the rationale for competition enforcement and why it benefits them. There are a variety of means for doing so:

- Publish all substantive decisions of the Council.
- Publish annual reports describing the agency’s activities and important cases.
- Cultivate relations with the press; issue press releases announcing important decisions or cases.

- Make speeches or other public appearances at appropriate occasions.
- Sponsor seminars or conferences on competition policy for interested parties – lawyers, business people, consumer groups.
- Develop a page on the World Wide Web.
- Publish guidelines explaining the substantive analysis that the agency employs in specific types of matters, or outlining procedures that are followed by the agency.

Comment

The Council has made significant strides in this area in the relatively short time that it has existed. It publishes an informative and comprehensive annual report, and it has established a Web page. Where the Council is known, it has a good reputation. One person in the private sector interviewed in the course of this study stated flatly that the Council is “one of the best state institutions in Lithuania.” As noted above, however, some business people, perhaps many, do not know even that a competition law exists. It can do more to establish the public regard for competition policy, consistent with the obvious limitations in resources that it faces.

Recommendations

- The enactment of the new law provides a good opportunity for Council members and senior officers to make public appearances and publish articles describing the law’s new features.
- It appears that the Council’s cases and decisions are little publicised. Work with the local press to expand this coverage. In preparing explanations of the cases for the public, explain how the matter affects them as consumers, for example by helping to bring about lower prices for the relevant product or service.

3.6 *Resources*

Comment and Recommendations

Resource issues have come up in several places in the discussions above. It is obvious that the Council and the Competition Office require more resources than they have in some areas. This can probably be said, however, of many government agencies in Lithuania and elsewhere. While the Council should aggressively seek additional resources where they are truly needed, it must also constantly strive to be more efficient with what it already has.

The quality and dedication of the staff are distinctly positive aspects of the resources that are currently available to the Council. Its employees work hard and they are aggressive. They are relatively experienced. The rate of turnover on the staff appears to be lower than at competition agencies in some other transition countries. As noted above, the Council generally enjoys a good reputation.

In the limited time available for this study, it appears that the following are some priorities for augmentation of resources within the Council.

- Increase the salary levels within the Council to a level that is commensurate, not with the upper levels of the private sector, which is unrealistic, but with other parts of government. It appears that salaries for a comparable level of expertise are lower for employees of the Council than in other agencies. There would seem to be no justification for this disparity, given the technical requirements for positions there. Salaries that are “competitive” within the public sector, at least, would help to attract and retain the type of employees who are needed for this important work.
- There appears to be a serious shortage of lawyers in the Office. This situation may be attributable, in part at least, to the rigorous and lengthy course of study and preparation required for qualification as a practicing lawyer in Lithuania. In the longer run, the Council can work within the government to encourage review of these standards, which may be too restrictive. In the short run,

if resources can be found to hire and retain only a few qualified lawyers, priority can be given to hiring and training qualified people as paralegals – assistants who can conduct most of the work required in litigation, thereby making the few lawyers more efficient.

- As noted above, two areas that appear to be significantly understaffed are the new responsibilities of antidumping and state aid monitoring. If one or both of these functions are not transferred elsewhere in the government, then additional staff will be required to perform them.

It must be assumed, however, that the Council staff will not grow in numbers significantly in the near term. The principal task therefore will be to improve the efficiency of the resources that do exist. Those issues too are discussed above in several places. Improving efficiency requires:

- Identifying and giving priority to the most significant substantive areas of enforcement, and within those areas, concentrating on the most significant cases and investigations.
- Streamlining procedures, to ensure against committing too many resources to the review of unnecessary notifications and unmeritorious applications for investigations, or engaging in lengthy and undisciplined hearings in which extraneous evidence and arguments are offered.
- Devising means of achieving effective relief from anticompetitive conduct other than through hearings and litigation, such as through voluntary agreements and negotiated settlements.

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