

COMMUNICATION BY CANADA

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PROVISIONS ON HARD CORE CARTELS – A STARTING POINT

1. This note seeks to stimulate discussion regarding the feasibility and desirability of using the OECD Recommendation on Hard Core Cartels (Recommendation of the Council Concerning Effective Action Against Hard Core Cartels referred to in this note as the "Recommendation" or the "OECD Recommendation") as a starting point for considering potential WTO provisions in the same area.

2. Our discussions in the Working Group recognize that there is a shared concern with regard to international cartel activity. The 1997 Annual Report of the World Trade Organization highlighted the growing salience of international cartels for the multilateral system, noting: "There are some indications that a growing proportion of cartel agreements are international in scope. Distortionary cartels in the international marketplace undermines the operation of a liberalized trade system and competitive domestic markets." Indeed, this concern is reflected in the Doha Ministerial Declaration.

I. WHY CONSIDER MULTILATERAL ANTICARTEL PROVISIONS?

3. If many nations already prohibit certain cartels and the OECD and UNCTAD have worked steadily to heighten awareness regarding the private cartel problem, why consider a multilateral agreement in this area? What would be the value-added of a WTO agreement in this area? It has been argued that there are at least three benefits:

- First, not all WTO Member nations have competition regimes in place and, hence, in many nations there are no legal prohibitions on private cartels.
- Second, a WTO agreement would affirm a multilateral consensus regarding the harmful effects of hard core cartels and the interests of member countries in combatting these cartels.
- Third, a WTO agreement would give notice to global cartels that there are fewer safe havens for their activities.

II. DIMENSIONS OF THE CARTEL PROBLEM

4. The World Bank in 2001 issued a background paper entitled "Private International Cartels and Their Effect on Developing Countries" by Margaret Levenstein and Valerie Suslow. The Levenstein-Suslow paper examines the possible effects of recent private international cartels on developing countries by looking at five case studies. Many of the larger cartels have had an effect on markets worldwide. Some tentative conclusions from the paper are:

- It is impossible to gauge the true number of international cartels in existence in the 1990s;
- The authors note that the lack of antitrust prosecutions by developing countries themselves reinforces the paucity of information on these cartels in developing country markets.
- The authors measured the overpayment by developing countries to cartel participants. Levenstein-Suslow indicate that in 1997, developing countries imported US\$81.1 billion of goods from industries which had seen a price-fixing conspiracy during the 1990s. These imports represented 6.7% of imports and 1.2% of GDP in developing countries. They represented an even larger fraction of trade for the poorest developing countries, for whom some of these cartelized products is estimated to have represented 8.8% of imports.
- There are a variety of techniques that cartels use to block entry into their industries. This is a critical observation pointing to the dual effects of cartels: diversion of scarce resources or foreign currency reserves because of overpayments and the negative effects on competition in general and on the industrial, technological and export capabilities of local firms and producers. These effects can create serious problems for both developed and developing countries.

5. Other sources also provide convincing evidence regarding the extent of the damage caused by hard core cartels. The OECD report entitled "New Initiatives, Old Problems" (23 March 2000) reported on US estimates of the economic effects of cartels. It is estimated that the average illegal gain from price fixing is 10% of the selling price, but, the generalized harm to consumers may amount to 20% of the volume affected by the cartel.

III. RECENT ANTI-CARTEL ENFORCEMENT TRENDS

6. The 1990s witnessed a major shift in enforcement attention given to hard core cartels. Over the course of that decade important initiatives were taken: stronger national enforcement measures by major developed country authorities, the introduction of corporate leniency programs and in some jurisdictions, a reduction in the number of permitted exceptions under national anti-cartel statutes.

7. A major milestone occurred in 1998, when OECD Members adopted the Recommendation. This was the first detailed international statement of consensus on anti-cartel enforcement. It was developed in response to a clear competition law and policy challenge related to the growing evidence regarding the harm to consumers from these cartels. The Recommendation was negotiated by antitrust officials to strengthen enforcement.

8. A number of considerations led to the adoption and issuance of this Recommendation, including the recognition that hard core cartels are the most egregious violations of competition law and that they injure consumers in many countries by raising prices and restricting supply. Thus, goods and services become completely unavailable to some purchasers and unnecessarily expensive

for others. Effective action against hard core cartels is particularly important from an international perspective because their distortions of world trade cements market power, waste and inefficiency.

9. The OECD Recommendation underscored the policy consensus in favour of anti-cartel enforcement. This consensus was premised on the following economic rationale:

- (a) Hard core cartels lack any relationship to productive functions.
- (b) These cartels diminish social welfare, create allocative inefficiency and transfer wealth from consumers to the participants in the cartel by reducing output below market-driven levels.
- (c) Such restraints are harmful over the long run. The use of cartels to avoid the rigors of competition can result in the creation of artificial, uneconomic and unstable industry structures, lower productivity gains and sustained higher prices.

IV. ELEMENTS OF THE OECD RECOMMENDATION

- A hard core cartel is one of the following forms of conduct – price fixing, output restriction, bid rigging and market division, which are not further defined in the Recommendation. Exclusions under Members' laws are permitted.
- The Recommendation encourages OECD Member countries to adopt competition laws that effectively prohibit and deter hard core cartels.
- The Recommendation constitutes a non-binding, commitment. It is built on a common approach to the prohibition of hard core cartels. It does not pursue or adopt a set of common standards.
- The Recommendation urges OECD Members to ensure that their competition laws provide "effective" sanctions at a level "adequate" to detect and remedy hard core cartels. These terms are not spelled out.
- There is no binding dispute settlement mechanism. Consultations regarding cooperation issues are provided for, but have not been used to date.
- International co-operation is a core objective. Instruments and details are left to each Member to work out.
- The Recommendation's institutional design is premised on the principle of national autonomy of each enforcement authority.

V. FROM THE OECD TO THE WTO?

10. Could the OECD Recommendation provide WTO Members with a starting point for considering a WTO approach to hard core cartels? In substantive terms, the Recommendation is the only highly articulated multilateral instrument on this form of conduct. As such it merits close examination. We focus below on key concepts or themes in the Recommendation which might provide some lessons for a WTO approach. We do not pursue an article-by-article analysis.

VI. INSTITUTIONAL MODELS

11. The Recommendation was adopted by the OECD and, therefore, was inevitably shaped by the logic and purpose of that institution. The OECD Competition Committee (CC) is the chief forum for the regular exchange of views on competition policy issues by antitrust enforcement officials. The Committee pursues a soft convergence approach to antitrust issues. This approach involves structured international activities through which national laws and enforcement are made more congruent through the exchange of experiences. This process relies on contact and cooperation between national enforcement officials. Even where formal agreements or recommendations do exist, they are tantamount to reference points for ongoing activities.

Are there elements of the OECD model which could be usefully adapted to the WTO work on cartels?

VII. LEGAL FRAMEWORK

12. The OECD Recommendation is built on the explicit and initial prerequisite that every Member should enact a sound competition law with appropriate scope: "Member countries should ensure that their competition laws effectively halt and deter hard core cartels."

13. On the basis of the Recommendation, legal provisions on hard core cartels need to be embodied in a general competition statute. The statute would need to contain effective sanctions and enforcement procedures and provide for a national enforcement authority with sufficient powers. Additionally, exceptions need to be transparent and reviewed periodically.

14. While "Member countries should ensure that their anti-cartel laws effectively halt and deter hard core cartels", the Recommendation does not take a position as to whether a national law should be based on per se rules or a rule-of-reason approach. Nor does the Recommendation attempt to impose a civil or criminal law framework with regard to enforcement, sanctions and fines. These matters are issues to be decided by national authorities.

Does the Working Group accept the Recommendation's starting point- i.e., enacting a national legal framework and establishing an enforcement authority?

VIII. DEFINITIONS

15. The Recommendation identifies four forms of conduct deemed to constitute hard core cartels but does not define these, at least not in detail. Instead, it relies on the national law of each OECD Member to provide precise meaning. Thus, at the extreme, one might argue that the Recommendation has 30 different definitions set out in the national laws of its 30 Members. In addition, sectoral exemptions, indeed varying national exemptions, may exist under each Member's law. There was no effort to harmonize these exemptions, nonetheless the value of transparency and periodic review should be acknowledged.

16. During the course of the negotiations on the OECD Recommendation, an attempt was made to develop more detailed definitions. This approach was abandoned as potentially leading to the development of "common standards". Common standards imply a harmonized approach, while the needs and circumstances of different Member nations are not identical. Also, a harmonized or common standards approach might have provided a basis for determining whether a Member's law conforms to the Recommendation. This was not the direction or outcome sought by the Members.

Does the absence of a common and detailed definition in the Recommendation present a desirable methodology for a potential WTO approach? Should any WTO anti-cartel initiative recognize the need for certain exemptions in national laws on hard core cartels?

IX. SCOPE

17. The difference in treatment between hard core cartels and other cartels can generally be explained on the basis of differing presumptions regarding their effects on competition. On the basis of this logic, the Recommendation states that hard core cartels excludes those cartels recognized by Members as resulting in "cost-reducing or output-enhancing efficiencies". In some jurisdictions, this logic extends to export (marketing) cartels, which are sometimes assessed on a case-by-case basis to ascertain their potential effects on competition.

Should any WTO competition initiative address hard core cartels as per the OECD Recommendation? Does the OECD Recommendation reflect the extent of the current multilateral consensus with regard to the desirable scope of any WTO anti-cartel initiative?

X. BARRIERS TO ENTRY

18. Discussions of the WGTCP have illustrated that there are a number of anti-competitive practices which can have an impact on trade. It has been clear that hard core cartels are of particular interest for their impact on trade since they can distort the price of key products, preclude new entrants and segment markets on a geographic basis. They present not only a traditional antitrust concern posed by anti-competitive business practices, but also a significant trade concern. From the trade perspective, the excluded exporters' home economy may be hurt by the limitations placed on their businesses.

19. The Preamble of the Recommendation states: "effective application of competition policy plays a vital role in promoting world trade by ensuring dynamic world markets and encouraging the lowering or reducing of entry barriers to imports". In terms of a practical response, the Recommendation implicitly endorses the tenet that the most effective way to redress private restraints which restrict market entry is to empower competition authorities to take enforcement action. After all, the more competition that exists in a domestic market, the greater the benefit to consumers and to all suppliers, whether domestic or foreign.

20. The Recommendation while sensitive to a multiplicity of policy concerns, including the trade dimension, does not address the question of how to weigh diverse concerns. It leaves to each Member to frame a coherent body of rules and enforcement practices.

XI. ENFORCEMENT COOPERATION

21. The major set of issues covered under the Recommendation relate to enforcement cooperation. The Recommendation recognizes that Members have a common interest in preventing hard core cartels and encourages Members to cooperate in enforcing their laws against such cartels in accordance with the principles of comity, taking into consideration the following:

- (a) consistency with a country's laws, regulations, and important interests;
- (b) safeguards to protect commercially-sensitive and other confidential information;
- (c) freedom to decline a request for assistance or to limit or condition cooperation;
- (d) potential for non-binding consultations over issues relating to co-operation.

22. Cooperation under the Recommendation is premised on a common interest among Members to prevent hard core cartels. Members are urged to enter into bilateral or multilateral enforcement cooperation agreements. The Recommendation does not create any expectation that national

discretion will be restrained through future initiatives. Thus, the OECD recognizes that nations are likely to have more success by exchanging views and working together on specific matters than by negotiating detailed multinational rules.

How could the WTO agreement on competition policy take into account some of the basic precepts underpinning the OECD approach to cooperation?

XII. DEVELOPING COUNTRIES

23. The Recommendation was developed among countries with diverse economic philosophies and competition institutions. Nonetheless, the OECD adopted a unified set of provisions applicable to all OECD Members across different legal systems and competition experiences. This is achieved through the use of a "common approach" methodology. The common approach is less detailed and more flexible than standards. It sets out a list of criteria or objectives to be considered. It does not indicate how these criteria would be applied or what precise weight should be assigned to particular elements of the criteria.

24. The "common approach" is further supplemented by a continuous exchange of experiences and a peer review process. These supplementary processes are designed to achieve ever greater coherence and convergence with regard to the "common approach". It provides Members with an opportunity to discuss practical issues related to the process of refining, integrating and customizing the common approach to best suit their respective national systems. The common approach methodology may hold lessons today for the WTO community which is grappling with the challenge of developing a competition framework for its highly diverse membership.

Would the OECD's common approach provide a suitable methodology for negotiating a single set of provisions on hard core cartels in the WTO, applicable to all Members regardless of their situation?

Would this approach provide a basis for addressing the needs of developing countries, i.e. common substantive elements (e.g. requirement for a legal framework, scope, definitions, etc.) but variable implementation provisions (e.g. a longer phase-in schedule)?
